

Board of Directors
Orange County Sanitation District
Fountain Valley, California

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*

Independent Auditor's Report

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements as of and for the year ended June 30, 2023, and the related notes to the financial statements, which collectively comprise the Orange County Sanitation District's (OC San) basic financial statements, and have issued our report thereon dated October 26, 2023.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the OC San's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the OC San's internal control. Accordingly, we do not express an opinion on the effectiveness of the OC San's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We identified the following deficiency in internal control that we consider to be a significant deficiency.

(1) Capital Asset Recordkeeping

During our audit for the fiscal year ended June 30, 2023, we performed an unpredictability test to physically inspect older capital assets. We selected a sample of 15 assets for inspection and found that 8 assets (53%) were no longer in use and

incorrectly included in OC San's capital asset listing. For the sample selected, there is no impact on net assets because the capital assets were fully depreciated.

Additionally, during our testing of construction in progress, we identified additional capital assets that were no longer in use. Many of OC San's construction projects occur over multiple years. OC San's policy is to remove any disposed of or rehabilitated asset from the capital asset listing at the time the new asset is added. The disposal of the replaced asset occurs prior to the completion of the new asset and sometimes the timing difference crosses fiscal years. During our audit, we identified \$65M of capital assets with a net book value of \$7.4M that were no longer in service that were included in OC San's capital asset listing.

Recommendation

We recommend OC San perform a detailed review of historical capital asset records for the purposes of identifying assets that should be removed from the accounting system. We also recommend OC San evaluate the policy and timing of removing old assets relating to ongoing construction projects to better align the timing of when assets are removed from service.

OC San's Response

OC San has engaged a firm to conduct a comprehensive fixed asset inventory. This effort will identify and confirm the assets in the accounting system, subsequently OC San will adjust those assets that are no longer in the capital asset listing. OC San is also developing a procedure to annually review the commissioning and decommission of assets during active construction, to better align the timing of when capital assets are recorded.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Orange County Sanitation District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

OC San's Response

Government Auditing Standards requires the auditor to perform limited procedures on OC San's response to the issues identified in our audit. OC San's response was not subjected to the other auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's

internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Davis Fan LP

Irvine, California
October 26, 2023