# MONTHLY AUDIT ACTIVITY REPORT FOR SEPTEMBER 2009 TO THE BOARD OF SUPERVISORS

Presented on Board Agenda October 27, 2009

Project No. 2907-3

# by Dr. Peter Hughes, MBA, CPA Director of Internal Audit

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# Letter from Dr. Peter Hughes, CPA





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RISK BASED AUDITING



October 27, 2009

Honorable Board of Supervisors,

It is my pleasure to submit to you the Monthly Audit Activity Report for the month of September 2009. Each report has an overview and a detailed briefing for your review.

As always, I'm available at your convenience to discuss any aspect of these items.

Respectfully submitted,

Dr. Peter Hughes, CPA

The Internal Audit Department is an independent audit function reporting directly to the Orange County Board of Supervisors.

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#### **Executive Summary**

#### Exhibit AUDITS:

- B OCCR/OC Parks RM Fisheries, Inc: We found that RM Fisheries, Inc.'s records adequately supported gross receipts and rent owed was properly paid. Gross receipts reported during the 12-month audit period were approximately \$412,000 and rent paid to the County was approximately \$33,000 million. Over its 5-year term, this lease agreement is estimated to generate over \$160,000 in rent to the County.
- C. OC Dana Point Harbor Harbor Revitalization Plan Contract Administration and Payments: We audited internal controls and processes over OCDPH's contract administration and contract payments, specifically for Harbor Revitalization Plan contracts, where during the audit period, OCDPH administered 84 contracts, including four harbor revitalization contracts, totaling over \$14 million and paid over \$2 million in contract expenditures. We identified six (6) Control Findings resulting to enhance existing contract administration controls and processes.
- D. <u>Probation Department Title IV-E Foster Care Program:</u> We audited the internal controls and processes over the Probation Department's Title IV-E Foster Care Program claims where total costs for administrative activities during the audit period from October 1, 2007 through September 30, 2008 were approximately \$16 million, and claimed matching reimbursement totaled \$5.7 million during the same period. We identified five (5) Control Findings to enhance existing controls and processes.
- E. Compliance Audit of the Boards' Audit Oversight Committee: The Audit Oversight Committee was found fully compliant in all material regards with all key AOC established requirements. In addition, we found that the Board and AOC had already adopted both practices and policies (governing rules) that embraced the majority of the better/best practices presented in the AGA's 2008 Research Report that we considered most closely aligned with the audit character and related governing rules approved by the Board. We identified eight recommendations for the BOS and AOC to consider for further enhancing the AOC oversight effectiveness.
- F. OC Dana Point Harbor Dana Point Yacht Club
  We found that Dana Point Yacht Club records adequately supported gross receipts and rent owed was properly paid. Gross receipts reported during the 12-month audit period were approximately \$1.5 million and rent paid to the County was approximately \$82,405. For the period of June 30, 1998 (lease assignment) through November 31, 2012 (lease expiration), this lease is estimated to generate over \$1 million in rent to the County.

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#### **Executive Summary**

G. OC Public Works – Transportation: We audited the internal controls and processes over the Transportation's Interdepartmental Billing Process where for the year ending September 30, 2008, County departments/agencies were billed over \$22 million for asset management, parts, labor, fuel, vehicle pool rental and depreciation costs on a newly implemented Flagship Billing System and other supporting information systems. We identified fifteen (15) Control Findings to enhance existing controls, processes and information systems.

#### Exhibit Monthly Computer Assisted Audits of Vendor Payments (CAATs):

H. <u>Auditor Controller and Human Resources – Duplicate Payments to Vendors and Other Routines – September 2009:</u> We analyzed **8,261** vendor invoices paid in August 2009 amounting to about **\$206 million** and found **99.65%** of the invoices were only paid once. Of the \$206 million vendor invoices, we identified **29** duplicate payments made to vendors totaling \$23,033. To date we have identified **\$893,552** in duplicate vendor payments, of which **\$825,518** has been recovered and is a noteworthy achievement by the Auditor-Controller's Office.

#### Exhibit FOLLOW-UP AUDITS:

I. CEO/County Procurement Office Audit Alert (Original Audit No.2766-5): Final Close-Out Second Follow-Up Audit of Audit Alert on County Procurement Office (CPO) policy for Sole Source Contracts that was issued in conjunction with a compliance audit of Sheriff-Coroner sole source contracts. We are pleased to report that the CPO fully implemented the remaining one (1) recommendation from our original Audit Alert containing four (4) recommendations. Three (3) of the recommendations were implemented in the First Follow-Up Audit in March 2009. As such, this report represents the final close-out of Audit Alert.

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### **Detailed Report**

# **New Audit Findings by Risk Category**

Description	Results
Material Weaknesses Audit findings or a combination of Significan Issues that can result in financial liability and exposure to a department/agency and to the County as a whole. Management is expected to address "Material Weaknesses" brought to their attention immediately.	None issued during September 2009. None issued since July 2009.
Significant Findings Audit findings or a combination of Control Findings that represent a significant deficienc in the design or operation of processes or internal controls. Significant Issues do not present a material exposure throughout the County. They generally will require prompt corrective actions.	None issued in September 2009. None issued since July 2009.
Control Findings  Audit findings concerning internal controls, compliance issues, or efficiency/effectiveness issues that require management's corrective action to implement or enhance processes and internal controls. Control Findings are expected to be addressed within our follow-up process of six months, but no later than twelve months.	

Total Audit Findings for FY 2009-10: 71

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# **Detailed Report**

#### **NON-MATERIAL FINDINGS**

Exhibit	Description	Comments
B.	Description  DEPT: OCCR/OC Parks  TITLE: Revenue Generating Lease Audit: RM Fisheries, Inc.  AUDIT NO: 2837	Scope: Revenue generating lease audit to determine whether the records of RM Fisheries, Inc. adequately supported monthly rent paid to the County. During the 12-month audit period, RM Fisheries, Inc. generated gross receipts of approximately \$412,000 and paid rent of approximately \$33,000 to the County.  Conclusion: We found that RM Fisheries, Inc. retained sufficient documentation to adequately support monthly rent paid to the County. We identified six (6) control findings related to improving records and/or compliance with the lease agreement.  Background: The County entered into a lease agreement with RM Fisheries, Inc., dated October 25, 2005, for the operation of a fishing concession located at the Laguna
	ISSUED: September 23, 2009	Niguel Regional Park. Over its 5-year term, this lease agreement is estimated to generate over \$160,000 in rent to the County.  Recommendations: Improving records and/or lease compliance regarding: documentation of fishing permits issued not retained; equipment rental forms not serially numbered; supporting documentation for voids not retained; special events participant lists not consistently retained; and financial statement attestation missing.

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# **Detailed Report**

Exhibit	Description	Comments
C.	DEPT: OC Dana Point Harbor  TITLE: Harbor Revitalization Plan - Contract Administration and Contract Payments  AUDIT NO: 2820  ISSUED: September 16, 2009	Scope: Audit of internal controls and processes over OC Dana Point Harbor (OCDPH) contract administration and payments for the Harbor Revitalization Plan for the year ending December 31, 2008, to determine if contracts are administered effectively; contract payments are valid, supported and allowable per contract terms; compliance with Contract Policy Manual requirements; and processes are efficient and effective.  Conclusion: We tested 100% of the Harbor Revitalization Plan contracts as well as other OCDPH contracts and found internal controls and processes are in place to ensure contracts are effectively administered; contract payments are accurate, complete, valid, timely and have appropriate supporting documentation and management review; and processes were efficient and effective. We identified six (6) Control Findings to enhance internal controls and processes in these areas.  Background: During our audit, there were four contracts for the Harbor Revitalization Plan totaling \$11.6 million and related contract payments of \$1.2 million. Because the Harbor Revitalization Plan was in its early design phase, we audited other OCDPH contracts and payments to determine effectiveness in administering future harbor revitalization contracts. During the audit period, OCDPH administered 84 contracts totaling over \$14 million and paid over \$2 million in contract expenditures, which includes the above amounts for the Harbor Revitalization Plan.  Recommendations: Include Contract Payment Spreadsheets in all contract files; update Contract Payment Spreadsheets to reflect current expenditures; date-stamp contractor invoices upon receipt; ensure contractor invoices are processed within established 15-day timeframes; obtain verification of contracted services and agree billing rates with contract terms prior to payment; establish a Memorandum of Understanding for work performed by OC Public Works Accounting on behalf of OCDPH.
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Board Date: October 27, 2009

# **Detailed Report**

Exhibit	Description	Comments
D.	DEPT: Probation Department  TITLE: Title IV-E Foster Care Program Claims Process  AUDIT NO: 2822  ISSUED: September 16, 2009	Scope: Audit of internal controls and processes over the Probation Department's Title IV-E Foster Care Program (Title IV-E) claims process to determine if Title IV-E eligibility determination and preparation of claims comply with Federal and State regulations; claims are processed accurately, completely and timely; and business processes are efficient and effective as related to the Title IV-E claims process.  Conclusion: We found that overall controls are in place to ensure Title IV-E eligibility determination and preparation of claims complies with Federal and State regulations; Title IV-E claims are processed accurately, completely and timely; and business processes are efficient and effective. We identified five (5) Control Findings to enhance existing controls and processes  Background: The Foster Care Program authorized under Title IV-E of the Social Security Act helps counties to provide safe and stable out-of home care for minors until they are safely returned home, placed permanently with adoptive families or placed in other planned arrangements for permanency. The Probation Department and Social Services Agency (SSA) have an Interagency Operation Agreement to claim Title IV-E costs. Total costs for Probation's administrative activities during the audit period from October 1, 2007 through September 30, 2008 were about \$16 million, and claimed matching reimbursements totaled \$5.7 million.  Recommendations: Establish written procedures to ensure time study forms are prepared, documented and submitted by relevant personnel; establish written procedures for quarterly fiscal claiming; reconcile fiduciary fund accounts holding Title IV-E funds on a monthly basis; implement data storage controls for Title IV-E claiming spreadsheets; update Interagency Operating Agreement between Probation and Social Services Agency.

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# **Detailed Report**

Exhibit	Description	Comments
E.	TITLE: Compliance Audit of the Boards' Audit Oversight Committee  AUDIT NO: 2807-13	<b>Scope:</b> The objectives of this review are threefold: The first objective was to determine whether the AOC is complying with its duties and responsibilities. The second objective was to compare the Board of Supervisors' AOC's duties and responsibilities to the practices identified and recommended for consideration by the Association of Governmental Auditors (AGA) and the Government Finance Officers Association (GFOA) as "best practices" or "good ideas". The third objective was to review the organizational reporting relationships between the BOS, the AOC, and the County Internal Auditor for compliance with the critical "independence" requirements promulgated by the US Government Accountability Office (GAO) and the Institute of Internal Auditors (IIA).
	ISSUED: September 16, 2009	<b>Conclusion:</b> The Audit Oversight Committee was found fully compliant in all material regards with all key AOC established requirements. In addition, we found that the Board and AOC had already adopted both practices and policies (governing rules) that embraced the majority of the better/best practices presented in the AGA's 2008 Research Report that we considered most closely aligned with the audit character and related governing rules approved by the Board.
		Background: In 1995, the Board, based upon recommendations from both the Orange County Grand Jury and a Blue Ribbon Advisory Committee to the Board of Supervisors, separated the Internal Audit Department from the Auditor-Controller, the County's Chief Accounting Officer, and assigned the function to itself. The Internal Audit Department is now and has been for the past 14 years, a direct reporting function to the County's highest Governing Body, the Board of Supervisors, in order to ensure its independence from undue managerial influences and pressures as required by the applicable GAO governmental auditing standards. At the time of the separation, the Audit Oversight Committee (AOC) was also established as an oversight arm of the Board to advise the County Internal Auditor. The AOC reviewed the checklists of this report on May 27, 2009 and approved its advancement. We presented this report to the AOC on September 2, 2009.  Recommendations: We identified eight recommendations for the BOS and AOC to
		consider for further enhancing the AOC oversight effectiveness.

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# **Detailed Report**

Exhibit	Description	Comments
F.	DEPT: OC Dana Point Harbor TITLE:	<b>Scope:</b> Revenue generating lease audit to determine whether the records of Dana Point Yacht Club adequately supported monthly rent paid to the County. During the 12-month audit period, RM Fisheries, Inc. generated gross receipts of approximately \$1.5 million and paid rent of approximately \$82,405 to the County.
	Revenue Generating Lease Audit: Dana Point Yacht Club	<b>Conclusion:</b> We found that Dana Point Yacht Club retained sufficient documentation to adequately support monthly rent paid to the County. We identified <b>fifteen (15) control findings</b> related to additional rent owed, improving records, and/or compliance with the lease agreement.
	AUDIT NO: 2839	Background: The County entered into a lease agreement with Dana Point Yacht Club
	ISSUED: September 23, 2009	(DPYC), originally dated November 24, 1982, as amended and assigned to DPYC on June 30, 1998, for the operation of a yacht club with public banquet facilities located at the Dana Point Harbor. Operations include food and beverage services and boating, social, and youth programs and educational activities. For the period of June 30, 1998 through November 31, 2012 (lease expiration), this lease is estimated to generate over \$1 million in rent to the County.
		Recommendations: Rent owed, record improvements, and/or lease compliance regarding: rent owed for non-member surcharge and miscellaneous service fees; rent recovery reduces catering gross receipts, certain catering charges for member events not reported as gross receipts; minor rent categories need clarification; membership fees exempt from percentage rent; missing POS system transaction numbers; retention of daily food handwritten tickets and periodic comparison to POS cashiering system reports; missing merchandise handwritten receipts and untimely recording; participant listings for sailing lesson and cruise/race applications are not retained; customer signed catering contracts; and untimely submission of financial statements.

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# **Detailed Report**

Exhibit	Description	Comments
G.	DEPT: OC Public Works	<b>Scope:</b> Audit of internal controls, processes, and information systems of OCPW/Transportation to ensure interdepartmental billings are accurate, complete, and valid; review application controls for user access in the Flagship Billing System and Fleet Focus System; perform a high-level review of IT general controls for OCPW as it
	TITLE: Transportation Interdepartmental Billing	relates to the Flagship Billing System; and determine if processes are efficient and effective as related to the interdepartmental billing process.
	Process	<b>Conclusion:</b> We found that internal controls are in place to ensure interdepartmental billings are accurate, complete, and valid; user access to the rates and account codes in the Flagship Billing System and Fleet Focus System is adequately controlled; high-level
	AUDIT NO: 2838	IT general controls for OCPW as related to the Flagship Billing System are reasonable; and interdepartmental billing processes were efficient and effective. We identified <b>fifteen (15) Control Findings</b> to enhance controls, processes and information systems.
	ISSUED: September 28, 2009	Background: Transportation (also referred as Fleet Services) is under OC Facilities, and provides fleet vehicle services, equipment, and maintenance to County departments/agencies. For the year ending September 30, 2008, County departments/agencies were billed over \$22 million for asset management, parts, labor, fuel, vehicle pool rental and depreciation costs on a newly implemented Flagship Billing System and other supporting information systems.
		<b>Recommendations:</b> Consult with Flagship vendor for adjusting sales tax calculation to eliminate discrepancies; reconcile fleet inventory changes to asset management fees; agree billing reports to JVs and/or invoices billed to departments/agencies; ensure reconciliations are prepared/reviewed timely; ensure appropriate Transportation staff are included in notifications of employee changes; improve written policies/procedures for IT security management; modify purchasing and software acquisition policies; document and test disaster recovery/business continuity plan; evaluate re-assigning report
		reconciling duties; establish process to communicate availability of billing reports to Accounting; establish procedure for updating account codes timely into Fleet Focus; establish responsibilities for reconciling changes in asset inventory; research using Flagship to calculate the monthly depreciation expense billings.

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# **Detailed Report**

Exhibit	Description	Comments
H.	DEPT: Auditor-Controller Human Resources County Procurement Office	<b>Scope:</b> The monthly CAAT routines are automated queries applied to large amounts of electronic data searching for specified characteristics. We currently perform 5 CAATs routines utilizing selected payroll and vendor data. Depending on the nature of the CAAT, we perform them monthly, annually, or as necessary.
	TITLE: Computer Assisted Audit Techniques – September 2009	<ul> <li>Conclusion:         <ul> <li>Duplicate Payments to Vendors: We analyzed 8,261 vendor invoices paid in August 2009 amounting to about \$206 million and found 99.65% of the invoices were only paid once. Of the \$206 million vendor invoices, we identified 29 duplicate payments made to vendors totaling \$23,033. The Auditor-Controller currently has a recovery rate from vendors of about 95% on these duplicate payments.</li> </ul> </li> </ul>
	AUDIT NO: 2941-C	Our prior research has indicated that duplicate payments are typically caused by a human clerical error. Based on the to-date recoveries of <b>\$825,518</b> , this CAAT routine has paid for itself and is returning monies to the County that may otherwise be lost.
	ISSUED: September 30, 2009	<ul> <li>Multiple Direct Deposits: No findings noted.</li> <li>Employee Vendor Match: Analysis of employee-vendor activity for FY 08-09 is in process</li> <li>Retiree/Extra Help Hours: As of 9/21/09, no working retirees have exceeded annual limits for FY 09-10.</li> <li>Deleted Vendors: This routine will no longer be performed.</li> </ul>
		<b>Background:</b> The CAATs differ from our traditional audits in that the CAATs can query 100% of a data universe whereas the traditional audits typically test but a sample of transactions from the population. The resulting matches identified by the CAATs are subjected to further review and analysis by the Internal Audit Department. We then forward any resulting findings to the A-C, HR, or County Procurement Office for their review and concurrence, and subsequent correction/recovery. We also work with these departments to identify internal control enhancements with the purpose of preventing future occurrences of the type of findings identified by the CAATs.

Board Date: October 27, 2009

# **Detailed Report**

Exhibit	Description	Comments
1.	DEPT: County Executive Office TITLE:	Scope: Second Follow-Up Audit of an Audit Alert issued to the County Procurement Office regarding sole source contract policy to determine the implementation status of (1) recommendation remaining from our First Follow-Up Audit report dated March 11, 2009 (Audit No. 2829-L). In the First Follow-Up Audit, we found (3) recommendations
	Final Close-Out Second Follow-Up Audit, Audit Alert: County Procurement Office	were implemented. The <b>(4) recommendations</b> resulted from our Audit Alert dated July 17, 2008, that was issued in conjunction with a compliance audit of Sheriff-Coroner Administration's sole source contracts.
	Policy on Sole Source Contracts (Original audit no. 2766-5)	<b>Conclusion:</b> Our Second Follow-Up Audit indicated that the County Procurement Office fully implemented the (1) remaining recommendation. <b>As such, this report represents the final close-out of the Audit Alert and original audit.</b>
	AUDIT NO: 2928-B ISSUED: September 16, 2009	<b>Background:</b> <i>CPM Section 4.4</i> – <i>Sole Source and Proprietary Requests</i> is the County's policy for requesting sole source procurements and provides criteria for departments/agencies to justify not using the County's standard competitive bidding process. The policy also allows departments/agencies to subsequently hire vendors after initially obtaining the contracts by sole source. Our review of the <i>Contract Policy Manual</i> ( <i>CPM</i> ) found the language of the policy lends itself for varying interpretations by the users and could be improved upon to provide better guidance for
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		<b>Recommendations:</b> Provide additional clarification and guidance on sole source requests, which should include examples of documentation requirements and specific criteria for issuing subsequent contracts with sole source vendors; provide periodic training to departments/agencies on sole source procurements; consider establishing a threshold by which the County Procurement Office would review and approve certain high-dollar sole source procurements prior to BOS approval; consider establishing a process by which all department/agency sole source contracts are periodically reported to the County Procurement office and the BOS for tracking and oversight of sole source usage.

Board Date: October 27, 2009