

MONTHLY AUDIT ACTIVITY REPORT FOR MARCH 2009 TO THE BOARD OF SUPERVISORS

Presented on Board Agenda
April 28, 2009

Project No. 2807-12

by Dr. Peter Hughes, MBA, CPA
County Internal Auditor

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 ORANGE COUNTY BOARD OF SUPERVISORS'
Internal Audit Department

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Letter from Dr. Peter Hughes



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April 28, 2009

Honorable Board of Supervisors,

It is my pleasure to submit to you the Monthly Audit Activity Report for the month of March 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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THE FOLLOWING ITEMS ARE SUMMARIZED BELOW:

Exhibit

AUDITS:

- B. CAPS+ Steering Committee - CAPS+ AUDIT ALERT NO. 3 - Review of Internal Controls in Capital Assets Documentation: We find that the CAPS+ Capital Assets documentation identifies several internal controls that if implemented properly will facilitate appropriate segregation of duties, reviews and approvals, audit trails, and account reconciliations.

We also identified **nine (9)** recommendations that will improve the planned internal controls and/or improve the system implementation documentation. The CAPS Steering Committee **concurred with all nine** of our recommendations.

- C. Auditor-Controller - Evaluation of CAFR Footnote Disclosure Process: We are pleased to report we noted eleven (11) Industry Leading Best Practices in the Auditor-Controller CAFR Footnote Disclosure Process. Additionally, we propose six (6) recommendations to further enhance existing controls and processes over the Auditor-Controller's CAFR Footnote Disclosure Process. The Auditor-Controller agreed with four (4) recommendations.

Exhibit

MONTHLY COMPUTER ASSISTED AUDITS OF VENDOR PAYMENTS (CAATs):

- D. Auditor Controller – Duplicate Payments to Vendors – March 2009: We analyzed **12,106** vendor invoices paid in February 2009 amounting to about **\$74 million** and found **99.94%** of the invoices were only paid once. Of the \$74 million vendor invoices, we identified **eight (8)** duplicate payments made to vendors amounting to **\$33,844**. To date we have identified **\$806,183** in duplicate vendor payments, of which **\$754,036** has been recovered which is a noteworthy achievement by the Auditor-Controller's Office.

Exhibit

FOLLOW UP AUDITS:

- E. CEO/County Procurement Office: First Follow-Up of Audit Alert for Policy on Sole Source Contracts. We issued an **Audit Alert** to the County Procurement Office with **four recommendations** to enhance the County's Contract Policy Manual on sole source contracts. Specifically, we recommended clearer guidelines and examples on policy requirements, most notably in the documentation requirements for sole source justification. Our Follow-Up Audit indicated that the County Procurement Office took satisfactory corrective action to fully implement **(3)** recommendations and **(1)** recommendation was in process.

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Exhibit

FOLLOW UP AUDITS:

- F. County Executive Office: Final Close-Out of First Follow-Up for Audit of the Source of Funding for the 2004 OCEA Pension Enhancements; We are pleased to report that the County Executive Officers satisfactorily implemented corrective actions to address the two recommendations in our audit report concerning establishing written policies and procedures for documenting the development of employee's reverse pick up rates and for conducting the annual reviews of enhanced benefits and costs.

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**Detailed Breakout
 New Audit Findings by Risk Category**

	Description	Results
	<p>Material Weaknesses Audit findings or a combination of Significant 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.</p>	<p>None issued during March 2009. None issued since July 2008.</p>
	<p>Significant Findings Audit findings or a combination of Control Findings that represent a significant deficiency 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.</p>	<p>None issued in March 2009. (1) issued since July 2008.</p>
	<p>Control Findings Audit findings concerning <u>internal controls</u>, <u>compliance issues</u>, or <u>efficiency/effectiveness issues</u> 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.</p>	<p>(15) issued in March 2009. (77) issued since July 2008.</p>

Total Audit Findings for 2008-09: 78

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NON-MATERIAL FINDINGS

Exhibit	Description	Comments
B.	<p>DEPT: <u>CAPS Steering Committee</u> Auditor-Controller Chief Financial Officer Chief Information Officer Human Resources Director Auditor-Controller Director of Accounting & Technology</p> <p>TITLE: CAPS+ AUDIT ALERT NO. 3: Review of Internal Controls in Capital Assets Documentation</p> <p>AUDIT NO: 2845-A</p> <p>ISSUED: March 13, 2009</p>	<p>Scope: Our review consisted of inquiry and a review of selected capital asset documentation prepared by the CAPS+ Project Implementation Team to identify internal controls related to: proper segregation of duties; appropriate reviews and approvals; audits trails related to preservation of source documents and recording of reviews and approvals; and sound account reconciliations. Our scope did not include a review of certain key open items (in progress) as further described in the report.</p> <p>Conclusion: We find that the CAPS+ Capital Assets documentation identifies several internal controls that if implemented properly will facilitate appropriate segregation of duties, reviews and approvals, audit trails, and account reconciliations. We also identified nine (9) recommendations that will improve the planned internal controls and/or improve the system implementation documentation. The CAPS+ Steering Committee concurred with all nine of our recommendations.</p> <p>Background: The purpose of a CAPS+ Audit Alert is to bring to the CAPS Steering Committee’s attention important potential issues for their assessment and if necessary, corrective action. Because of the CAPS+ Implementation Project’s schedule, timely feedback is critical. As such, this CAPS+ Audit Alert is not subject to the same rigor and formality of a traditional report in that we have not fully developed the issues and have not verified the accuracy of all information. The CAPS+ Audit Alerts have an accelerated management response timeline to ensure the timely dissemination of audit issues so as to not impede progress of the CAPS+ Implementation Project.</p> <p>Type of Recommendations: Open items for segregation of duties analysis, security administration function, centralized procedures, and audit log configuration; approval of capital asset forms is needed; define source documents and need for monitoring of data entry in the user procedures; monitor opportunities to implement capital asset shell functionality; and penetration testing scope may be limited.</p>

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C.	<p>DEPT: Auditor-Controller</p> <p>TITLE: Evaluation of the CAFR Footnote Disclosure Process</p> <p>AUDIT NO: 2767</p> <p>ISSUED: March 13, 2009</p>	<p>Scope: The Internal Audit Department conducted an evaluation of the Auditor-Controller CAFR footnote disclosure process. Our evaluation objectives were to: (1) Understand the Auditor-Controller’s CAFR footnote disclosure process; (2) Identify process and control strengths; and (3) Identify any areas that could benefit from enhancements.</p> <p>Conclusion: We are pleased to report we noted (11) Industry Leading Best Practices in the Auditor-Controller CAFR Footnote Disclosure Process.</p> <p>Additionally, we propose six (6) recommendations to further enhance existing controls and processes over the Auditor-Controller’s CAFR Footnote Disclosure Process. The Auditor-Controller agreed with four (4) recommendations.</p> <p>Background: The Auditor-Controller’s Financial Reporting Group prepares the County’s CAFR by taking raw financial data and transforming it into a coherent, accurate report that complies with Generally Accepted Accounting Principles (GAAP). Financial data is received from other Auditor-Controller management along with other County departments and agencies.</p> <p>Type of Recommendations: We recommended that the Auditor-Controller consider documenting requirements mandated in the respective financial reporting standards for CAFR footnote disclosures; enhance the instructions for specific managers to more clearly define the criteria and level of review; and process enhancements for the newly established CAFR Review Committee.</p>

Board Date: April 28, 2009

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For a copy of the complete audit report that contains the audit objective, scope, findings, recommendations, and management’s response, contact the OC Internal Audit Department’s website at <http://www.ocgov.com/audit/>

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D.	<p>DEPT: Auditor-Controller Human Resources County Procurement Office</p> <p>TITLE: Computer Assisted Audit Techniques – March 2009</p> <p>AUDIT NO: 2844-I</p> <p>ISSUED: March 31, 2009</p>	<p>Scope: 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.</p> <p>Conclusion:</p> <ul style="list-style-type: none"> • <u>Duplicate Payments to Vendors:</u> We analyzed 12,106 vendor invoices paid in March 2009 amounting to about \$74 million and found 99.94% of the invoices were only paid once. Of the \$74 million vendor invoices, we identified eight (8) duplicate payments made to vendors amounting to \$33,844. The Auditor-Controller currently has a recovery rate from vendors of about 98% on these duplicate payments. <p>Our prior research has indicated that duplicate payments are typically caused by a human clerical error. Based on the to-date recoveries of \$752,036, this CAAT routine has paid for itself and is returning monies to the County that may otherwise be lost.</p> <ul style="list-style-type: none"> • <u>Multiple Direct Deposits:</u> No findings noted. • <u>Employee Vendor Match:</u> 26 potential employee/vendor matches submitted to Human Resources for further evaluation. • <u>Retiree/Extra Help Hours:</u> As of 3/18/09, no working retirees exceeded annual limits. • <u>Deleted Vendors:</u> No findings noted. • <u>Data Validation:</u> No findings noted. • <u>High Dollar Payments:</u> No findings noted. <p>Background: 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.</p>

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E.	<p>DEPT: CEO/County Procurement Office</p> <p>TITLE: First Follow Up Audit, AUDIT ALERT of Policy on Sole Source Contracts (Original Audit No. 2766-5)</p> <p>AUDIT NO: 2829-L</p> <p>ISSUED: March 11, 2009</p>	<p>Scope: First Follow-Up Audit of an Audit Alert issued to the County Procurement Office regarding Policy on Sole Source Contracts to determine the implementation status of (4) recommendations made in our report dated July 17, 2008.</p> <p>Conclusion: Our Follow-Up Audit indicated that the County Procurement Office took satisfactory corrective action to fully implement (3) recommendations. The remaining (1) recommendation to develop examples of policy documentation requirements is still in process. The County Procurement Office is committed to implementing the remaining recommendation.</p> <p>Background: <i>CPM Section 4.4 – 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 (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 departments/agencies.</p> <p>Type of Recommendations: 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.</p>

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F.	<p>DEPT: County Executive Office</p> <p>TITLE: Final Close-Out of First Follow Up Audit of the Source of Funding for the 2004 OCEA Pension Enhancements (Original Audit No. 2765)</p> <p>AUDIT NO: 2818-A</p> <p>ISSUED: March 9, 2009</p>	<p>Scope: We have completed a First and Final Close-Out Follow-Up Audit of the Audit of the Source of Funding for the 2004 OCEA Pension Enhancements. Our audit was limited to reviewing actions taken as of January 28, 2009 to implement the two recommendations made in our original audit report.</p> <p>Conclusion: We are pleased to report that satisfactory corrective actions have taken place for the audit recommendations. The County Executive Officers satisfactorily implemented corrective actions to address two recommendations concerning establishing written policies and procedures for documenting the development of employee's reverse pick up rates and for conducting the annual reviews of enhanced benefits and costs.</p> <p>Background: On August 24, 2004, the Orange County Board of Supervisors adopted Resolution No. 2004-247 to implement a 2.7% @ age 55 retirement formula for General Members of the Orange County Employees Retirement System (OCERS) retiring on or after July 1, 2005. It is an enhanced retirement plan for the OCERS General Members. Through negotiations with the labor organizations, the bargaining units agreed that pension enhancement will be without any additional cost to the County. In addition, they agreed to make additional employee contributions to the retirement system and health benefit changes (increased co-payments, higher deductible and increased employee payroll deductions). The combination of the additional employee contributions and health insurance cost savings are to cover the annual cost of implementing the enhanced retirement benefits.</p> <p>Type of Recommendation: None</p>