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EXHIBIT A

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

Presented on Board Agenda June 23, 2009

Project No. 2807-17

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

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RISK BASED AUDITING

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Letter from Dr. Peter Hughes





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RISK BASED AUDITING



June 23, 2009

Honorable Board of Supervisors,

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

Additionally, for the 10th consecutive year I am pleased to present the approved Annual Fiscal Year 2009-10 Audit Plan and Risk Assessment (Exhibit B). This comprehensive report details our plan for audits and reviews in the upcoming fiscal year and incorporates the results of our extensive risk assessment.

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 Annual Audit Plan and Risk Assessment

B. For the 10th consecutive year I am pleased to present the approved Annual Fiscal Year 2009-10 Audit Plan and Risk Assessment. This comprehensive report details our plan for audits and reviews in the upcoming fiscal year and incorporates the results of our extensive risk assessment. Per Resolution No. 95-271, the Board directed the Audit Oversight Committee (AOC) to act in an oversight capacity to the Internal Audit Department and to approve the Annual Audit Plan. The AOC reviewed and approved the FY 09-10 Audit Plan and Risk Assessment on May 27, 2009. Accordingly I am presenting it to the Board of Supervisors as part of my required monthly **Audit Status Report** to the BOS.

Exhibit AUDITS:

- C. CAPS+ Audit Alert No. 4: Review of Internal Controls in Cost Accounting Documentation: We found that the CAPS+ Cost Accounting 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 **five** (5) recommendations that will improve the planned internal controls and/or improve the system implementation documentation. The CAPS Steering Committee concurred with all five of our recommendations.
- D. Board Directive: Report on Review of Contractual Terms Related to the "Profit and Loss Statements" of Two Vendors utilized by HCA to Provide Inmate Medical Services: The Board of Supervisors directed the County Internal Auditor to review the contractual terms of the two vendors as related to the "Profit and Loss Statement" findings raised by the Office of Performance Audit Director in its audit of HCA/Correctional Medical Services. In reviewing the contractual terms, it was determined both the CMC and WMC-A contract terms (page 8 of contracts) require the vendor to annually provide an "Expenditure and Revenue Report" to HCA for informational purposes. Neither contract contains penalties or financial consequences for non-conformance as related to the "Profit and Loss Statement" findings cited by the Office of Performance Audit. Lastly, the Profit and Loss Statement" contract terms do not impact or change in any way the payment obligations of the County in this regard as the contracts are fixed price.

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Executive Summary

E. <u>Audit of Revenue Generating Lease</u>: We found that Caterina's records adequately supported gross receipts and rent owed was properly paid. Annual gross receipts reported during our audit period were approximately \$969,000 and annual rent paid to the County was approximately \$213,000. From the lease inception date of March 1996 through March 2009, the County has received approximately \$2 million in rent.

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

F. <u>Auditor Controller and Human Resources – Duplicate Payments to Vendors and Other Routines – May 2009:</u> We analyzed **13,604** vendor invoices paid in April 2009 amounting to about **\$87 million** and found **100%** of the invoices were only paid once. Of the \$87 million vendor invoices, we identified no duplicate payments made to vendors. To date we have identified **\$812,044** in duplicate vendor payments, of which **\$754,036** has been recovered and is a noteworthy achievement by the Auditor-Controller's Office.

Other Routines: In April 2009, we identified **23** potential employee/vendor address matches that were submitted to Human Resources for their review. As of May 22, 2009, Human Resources determined that 1 was not a valid match and 2 were not a conflict. Their review of the 20 remaining matches is in process. In addition, we identified no findings from our direct deposit, deleted vendor, and working retiree routines.

Exhibit Follow UP AUDITS:

G. Integrated Waste Management/Performance Measure Validation (Original Audit No. 2754) (New Name: OC Waste & Recycling): Final Close-Out First Follow-Up of Performance Measure Validation Audit of Integrated Waste Management 2005-2006 Performance Indicators. We found that 1 recommendation was fully implemented, as such, this report represents the final close-out of the original audit.

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Executive Summary

- H. OCCR/OC Parks Review of Concession Revenue for David L. Baker Memorial Golf Course (Original Audit No. 2738): Final Close-Out First Follow-Up Review of Concession Revenue for David L. Baker Memorial Golf Course. The agreement is for the operation of a golf course, driving range, snack bar, and pro shop located at the County's Mile Square Regional Park. Over its 40 year life, this concession is estimated to generate over \$13 million in rent to OC Parks. We are pleased to report that OC Parks and David L. Baker Memorial Golf Course satisfactorily implemented or addressed all thirteen (13) recommendations from the original audit report. As such, this report represents the final closeout of the original audit.
- I. OC Dana Point Harbor/Ocean Institute (Original Audit No. 2577): Final Close-Out First Follow-Up Audit of Review of Lease Revenue for Ocean Institute. The Agreement is for the operation of County approved facilities and programs specifically related to marine science education and research. This lease agreement of about 35 years is estimated to generate at least \$1.2 million in rent to OC Dana Point Harbor. We are pleased to report that OC Dana Point Harbor and Ocean Institute satisfactorily implemented or addressed all seventeen (17) recommendations from the original audit report. As such, this report represents the final close-out of the original audit.

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Detailed Report

New Audit Findings by Risk Category

Description	Results
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.	None issued during May 2009. None issued since July 2008.
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.	None issued in May 2009. (2) issued since July 2008.
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.	5 issued in May 2009. (83) issued since July 2008.

Total Audit Findings for 2008-09: 90

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Detailed Report

NON-MATERIAL FINDINGS

Exhibit	Description	Com	nments
В.	TITLE: FY 2009-2010 Audit Plan and Risk Assessment REPORT NO: 2801 AOC Approved: May 27, 2009	2009-10 Audit Plan and Risk Assessment for audits and reviews in the upcoming fis extensive risk assessment. Per Resolution Oversight Committee (AOC) to act in a Department and to approve the Annual Authe FY 2009-10 Audit Plan and Risk Assessment.	d to present the approved Annual Fiscal Year. This comprehensive report details our plan scal year and incorporates the results of our on No. 95-271, the Board directed the Audit an oversight capacity to the Internal Audit udit Plan. The AOC reviewed and approved essment on May 27, 2009. Accordingly I am as part of my required monthly Audit Status
		the chief audit executive to establish a rist for internal audit activities. The Internal	nstitute of Internal Auditors' Standards require ok-based approach to determine the priorities Audit Department has completed a Risk measure, and prioritize potential audits based epare the FY 2009-10 Audit Plan.
		assessment and audits). We define	y an audit universe (all areas subject to risked the County audit universe as 22 al Audit and the Office of the Performance processes/cycles:
		Cash Receipting Accounts Receivable/Collections Budgeting Payroll	Cash Disbursements & Payables Fiduciary Funds/Special Use Funds Procurements and Contract Administration Revolving Funds

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Detailed Report

Exhibit	Description	Comments
	Exhibit B: FY 2009-20010 Annual Audit Plan and Risk Assessment Continued	Our <i>Risk Assessment Schedule</i> shown on page A-1 of Exhibit B shows the 179 auditable business processes we identified and assigned a risk rating. Of the 179 auditable business processes we identify in our general <i>Risk Assessment Schedule</i> , 77% are Medium Risk, 18% are Low Risk and 5% are High Risk. More importantly, management has corrected or mitigated all areas identified in our reports. The departments/agencies with a High risk score merely indicates that the services or functions they are responsible for are by nature a high risk activity because of such factors as having a large amount of expenditures and revenues, having a high level of liquid assets such as cash, management's assessment of the control environment, or a high degree of public interest. A high risk score indicates that if something were to go wrong, it could have a greater impact. A High risk score does <u>not</u> mean that a business process is being managed ineffectively or that internal controls are not adequate. Audit Plan hours are allocated to the audit areas as follows:
		Internal Control Audits (IC): 4,425 Financial Audits and Mandates (FAM): 2,800 Information Technology Audits (IT): 3,925 Revenue Generating Lease Audits (RGL): 2,250 Other Audit Activities*: 2,300 15,700 We would like to acknowledge the professionalism and cooperation extended to us by the management of the County agencies/departments during our Risk Assessment process. I look forward to another successful year of audit coverage and service to Orange County.

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Detailed Report

Exhibit	Description	Comments
C.	DEPT: CAPS Steering Committee TITLE:	Scope: Our review consisted of inquiry and a review of selected cost accounting 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.
	CAPS+ Audit Alert No. 4: Review of Internal Controls in Cost Accounting Documentation AUDIT NO: 2845-B	Conclusion: We found that the CAPS+ Cost Accounting 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 five (5) recommendations that will improve the planned internal controls and/or improve the system implementation documentation. The CAPS+ Steering Committee concurred with all five of our recommendations.
	ISSUED: May 22, 2009	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.
		Type of Recommendations: Open items: segregation of duties analysis, security administration function, centralized procedures, and audit log configuration. Recommendations: review of complex cost accounting table set-ups/updates; retention of equipment usage cards; reconciliation of equipment usage cards; review and reconciliation of inbound interfaces; and updating departmental procedures for more current terminology.

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Detailed Report

Exhibit	Description	Comments
D.	BOARD DIRECTIVE: Health Care Agency	The Board of Supervisors directed the County Internal Auditor to review the contractual terms of the two vendors as related to the "Profit and Loss Statement" findings raised by the Office of Performance Audit Director in its audit of HCA/Correctional Medical Services. In reviewing the contractual terms, it was determined both the CMC and WMC-A contract terms (page 8 of contracts) require the vendor to annually provide an
	TITLE: Review of Contractual Terms Related to the "Profit and Loss Statements" of two Vendors utilized by HCA to provide Inmate Medical Services REPORT NO: 2807-11 DATE: May 1, 2009	"Expenditure and Revenue Report" to HCA for informational purposes. Neither contract contains penalties or financial consequences for non-conformance as related to the "Profit and Loss Statement" findings cited by the Office of Performance Audit. Lastly, the Profit and Loss Statement" contract terms do not impact or change in any way the payment obligations of the County in this regard. HCA informed us that providing medical services to inmates is perhaps one of the most difficult areas HCA is obligated to address. This is because HCA is not in a position to control the population of inmates, their medical histories or addictions, or their utilization of medical services and/or the severity of their medical issues. HCA informed us that it was critical to be able to budget a known and manageable amount in advance for the provision of these services so as to avoid potentially large budget "overruns" in inmate medical care. HCA indicated that they must provide requisite medical care regardless of the authorized budget allocations.
		Conclusion: We conclude that both contracts are "fixed fee" contracts that were designed by HCA to effectively transfer the risk of potential case load and cost escalations for inmate medical care to the vendors instead of to the County. These fixed fee contracts require the vendors to assume in all material regards the risk of unforeseen escalations in utilization and medical severity and the corresponding cost increases.
	luna 22 2000	Type of Recommendations: We have one recommendation to assist in future negotiations of these contracts (these contracts expire June 30, 2009). The recommendation is detailed on page 4 of Exhibit D and addresses a contract pricing issue common to both contracts. HCA has at least eight years of medical service data on inmates and that data may enable HCA to better predict medical services required in upcoming years. HCA concurred with this approach in an effort to manage costs in their upcoming contract negotiations.

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Detailed Report

	Comments
DEPT: John Wayne Airport TITLE:	Scope: Revenue generating lease audit to determine whether the records of Caterina's adequately supported monthly rent paid to the County. During the 12-month audit period of December 1, 2007 through November 30, 2008. Caterina's generated gross receipts of \$969,000 and paid rent of \$213,000 to the County.
Revenue Generating Lease Audit of Caterina's	Conclusion: We found that Caterina's retained sufficient documentation to adequately support monthly rent paid to the County.
REPORT NO: 2832	Background: The County of Orange entered into a lease agreement with Caterina's for the operation of a nuts and candy concession located at John Wayne Airport. The lease agreement expired on June 30, 2006 and currently Caterina's is on a month-to-month tenancy. From the lease inception date of March 1996 through March 2009, the County
DATE: May 22, 2009	has received approximately \$2 million in rent.
	Type of Recommendations: None.
	John Wayne Airport TITLE: Revenue Generating Lease Audit of Caterina's REPORT NO: 2832

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Detailed Report

Exhibit	Description	Comments
F.	DEPT: Auditor-Controller Human Resources	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.
	County Procurement Office TITLE: Computer Assisted Audit Techniques – May 2009	 Conclusion: Duplicate Payments to Vendors: We analyzed 13,604 vendor invoices paid in April 2009 amounting to about \$87 million and found 100% of the invoices were only paid once. Of the \$87 million vendor invoices, we identified no duplicate payments made to vendors. The Auditor-Controller currently has a recovery rate from vendors of about 93% on these duplicate payments.
	AUDIT NO: 2844-K ISSUED: May 29, 2009	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.
		 Multiple Direct Deposits: No findings noted. Employee Vendor Match: In March 2009, 23 potential employee/vendor matches were submitted to HR for evaluation. As of 5/22/09, HR determined 1 was not a valid match and 2 were not a conflict. Their review of the remaining 20 matches is in process. Retiree/Extra Help Hours: As of 5/11/09, no working retirees exceeded annual limits. Deleted Vendors: No findings noted.
		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.

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Detailed Report

Exhibit	Description	Comments
G.	DEPT: OC Waste & Recycling TITLE: Final Close-Out First Follow-Up Audit of Performance Measure Validation of Integrated Waste Management (New Name: OC Waste & Recycling) 2005-2006 Performance Indicators (Original Audit No. 2754) AUDIT NO: 2815-C ISSUED: May 12, 2009	Scope: Final Close-Out of Initial Follow Up Audit of the Performance Measure Validation of Integrated Waste Management (New Name: OC Waste & Recycling) 2005-2006 Performance Indicators. Our audit was limited to reviewing the actions taken to implement the 1 recommendation in our audit report dated April 11, 2008. Conclusion: We are pleased to report that the 1 recommendation was fully implemented. We commend OC Waste & Recycling personnel for their responsiveness in addressing our recommendation. As such, this report represents the final close-out of the original audit. Background: The objective of our Performance Measure Validation (PMV) was to validate the accuracy of the 2005-2006 Outcome Measure Results reported in Integrated Waste Management's 2007-2008 Business Plan. Our audit included obtaining an understanding of the methodology in place for collecting and reporting Outcome Measure Results by interviewing key personnel, observations, and reviewing source documentation. The Business Plan contained a total of 7 Performance Indictors Results, and we tested the supporting documentation for all 7. Our audit scope did not include an assessment of the appropriateness of Integrated Waste Management's outcome measures based on their mission, goals and objectives. Type of Recommendations: None

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Detailed Report

Exhibit	Description	Comments
H.	DEPT: OC Community Resources/ OC Parks	Scope: Final Close-Out of First Follow-Up Review of Concession Revenue to determine the implementation status of thirteen (13) recommendations made in our original audit report, dated May 20, 2008. No material or significant issues were identified in the original audit report. This agreement of 40 years (beginning May 1987) is estimated to generate over \$13 million in rent to OC Parks.
	TITLE: Final Close-Out First Follow Up Audit of Review of Concession Review of David L. Baker Memorial Golf Course (Original Audit No. 2738)	Conclusion: We are pleased to report that satisfactory corrective action has been taken for the thirteen (13) audit recommendations. We commend the personnel at OCCR/OC Parks and David L. Baker Memorial Golf Course for their responsiveness in addressing our recommendations. As such, this report represents the final close-out of the original audit.
	AUDIT NO: 2840-B	Background: The County of Orange entered into a concession agreement with American Golf Corporation dated April 30, 1987, as amended for the operation of a golf course, driving range, snack bar, and pro shop located at the County's Mile Square Regional Park. During the 12-months ended October 31, 2007, American Golf generated approximately \$2.8 million in gross receipts at the David L. Baker Memorial
	ISSUED: May 29, 2009	Golf Course and paid the County approximately \$413,000 in rent. Currently, the golf course is operated by Eagle Golf. After our original audit, the Board of Supervisors authorized the concession assignment from American Golf Corporation to CNL Income EAGL Leasehold Golf, LLC (CNL) and the sub-concession agreement between CNL with Evergreen Alliance Golf Limited, L.P. (Eagle Golf) in April 2008.
		Type of Recommendations: Lease compliance and/or internal control improvements regarding additional rent owed on non-alcoholic beverages, reasonableness of complimentary golf rounds, reporting barter transactions, starter sheets reconciliation, segregation of duties, special events documentation, reporting of gift certificates and event deposits, attestation on the monthly gross receipts statements, and clarification on golf lessons.

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Detailed Report

Exhibit	Description	Comments
l.	Description DEPT: OC Dana Point Harbor TITLE: Final Close-Out First Follow Up Audit of Review of Lease Revenue of Ocean Institute (Original Audit No. 2577) AUDIT NO: 2741-D ISSUED: May 29, 2009	Scope: Final Close-Out First Follow-Up Review of Lease Revenue to determine the implementation status of seventeen (17) recommendations made in our original audit report, dated November 6, 2007. No material or significant issues were identified in the original audit report. This lease agreement of about 35 years is estimated to generate at least \$1.2 million in rent to OC Dana Point Harbor. Conclusion: We are pleased to report that satisfactory corrective action has been taken for the seventeen (17) audit recommendations. We commend the personnel at OC Dana Point Harbor and Ocean Institute for their responsiveness in addressing our recommendations. As such, this report represents the final close-out of the original audit. Background: The County of Orange entered into a 35+ year lease agreement with Friends of the Marine Institute in Orange County, a California non-profit corporation, dated June 29, 1999. In January 2000, the organization was renamed Ocean Institute. The purpose of the Agreement is for Ocean Institute to develop and operate County
		approved facilities and programs specifically related to marine science education and research. For the year ended January 31, 2006, Ocean Institute reported gross receipts (not subject to percentage rent) of \$3.9 million to the County and paid \$12,000 in rent to the County. Type of Recommendations: Lease compliance regarding additional rent owed on facility rentals, security deposits, and commercial cruises; clarification of gross receipts exclusions; reporting of commercial cruise rent; periodic increases to minimum annual rent and security deposits; required financial statements and other annual reports; and certification of the monthly gross receipts statement.

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