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#### **EXHIBIT A**

## MARCH 2011 AUDITS BY IAD

MONTHLY AUDIT ACTIVITY REPORT

### Presented on Board of Supervisors' Agenda **April 19, 2011**

- Audit of the Ladera Ranch Community Facilities District identified 2 Critical Control Weaknesses, 5 Significant Control Weaknesses, and 6 Control Findings resulting in 21 recommendations where internal controls and processes need to be improved in the calculation of the special tax rate and to ensure that bond proceeds are used only for authorized projects. The critical control weaknesses relate to the Auditor-Controller Public Finance Accounting's method for the calculation of the special tax levy and for unexplained project costs for El Toro Branch Library of \$803,000 charged to the Ladera Ranch CFDs.
- Monthly CAAT Reveals 99.99% of Vendors Payments Are Only Paid Once: We found 1 duplicate payment for \$2,702 out of 15,007 vendor invoices paid in February 2011.
- First and Final Follow-Up Audit of Revenue Generating Lease Audit of JWA/Budget Rent A Car Systems, Inc.: Our First Follow-Up Audit found the 1 recommendation was satisfactorily implemented.

#### by Dr. Peter Hughes, MBA, CPA, CIA, CFE, CFF, CITP, CCEP **Director of Internal Audit**

Assistance in assembling this report provided by: Eli Littner, Deputy Director, CPA, CIA, CFE, CFS, CISA Alan Marcum, Senior Audit Manager, MBA, CPA, CIA, CFE Michael Goodwin, Senior Audit Manager, CPA, CIA Autumn McKinney, Senior Audit Manager, CPA, CIA, CGFM, CISA

## Project No. 1007-9

#### **RISK BASED AUDITING**

GAO & IIA Peer Review Compliant - 2001, 2004, 2007, 2010

AICPA American Institute of Certified Public Accountants Award to Dr. Peter Hughes

as 2010 Outstanding CPA of the Year for Local Government

2009 Association of Certified Fraud Examiners' Hubbard Award to Dr. Hughes for the Most Outstanding Article of the Year-Ethics Pays

2008 Association of Local Government Auditors' Bronze Website Award



2005 Institute of Internal Auditors' Award to IAD for Recognition of Commitment to Professional Excellence, Quality, and Outreach

## Letter from Dr. Peter Hughes, CPA





**Dr. Peter Hughes, CPA DIRECTOR**PH.D., MBA,
CCEP, CITP, CIA, CFE, CFF

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RISK BASED AUDITING



April 19, 2011

Honorable Board of Supervisors,

It is my pleasure to submit to you the Monthly Audit Activity Report for the month of March. For each audit report we provide 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 Reports:

B. Audit of Ladera Ranch Community Facilities District: We identified 2 Critical Control Weaknesses, 5 Significant Control Weaknesses, and 6 Control Findings resulting in 21 recommendations where internal controls and processes need to be improved in the calculation of the special tax rate and to ensure that bond proceeds are used only for authorized projects. The critical control weaknesses relate to the Auditor-Controller Public Finance Accounting's method for the calculation of the special tax levy and for unexplained project costs for El Toro Branch Library of \$803,000 charged to the Ladera Ranch CFDs.

# Exhibit Monthly Results of Continuous Auditing Using CAATS (COMPUTER ASSISTED AUDIT TECHNIQUES):

C. <u>Auditor-Controller, Human Resources, and County Procurement Office – Duplicate Vendor Payments and Other Periodic Routines – March 2011</u>: We analyzed **15,007** vendor invoices paid in February 2011 amounting to about **\$190 million** and found **99.9%** of the invoices were only paid once. Of the \$190 million vendor invoices, we identified **1** duplicate payment totaling **\$2,702** made to vendors. To date we have identified **\$976,989** in duplicate vendor payments, of which **\$918,138** has been recovered and is a noteworthy achievement by the County.

#### Exhibit Follow-Up Reports:

D. <u>First and Final Follow-Up Audit of Revenue Generating Lease Audit of JWA/Budget Rent A Car Systems, Inc.</u>: Our First Follow-Up Audit found the 1 recommendation was satisfactorily implemented. **As such, this represents the final close-out of the original audit.** 

Board Date: April 19, 2011 Exhibit A, Page 3 of 9

#### **Detailed Report**

## **New Audit Findings & Recommendations by Risk Category**

Description	Results
Critical Control Weaknesses A serious audit finding or a combination of Significant Control Weaknesses that represent critical exceptions to the audit objective(s) and/or business goals. Management is expected to address "Critical Control Weaknesses" brought to their attention immediately.	<ul> <li>2 critical control weaknesses resulting in 5 recommendations issued during March 2011.</li> <li>5 recommendations issued since July 2010.</li> </ul>
Significant Control Weaknesses Audit findings or a combination of Control Findings that represent a significant deficiency in the design or operation of internal controls. Significant Control Weaknesses generally will require prompt corrective actions.	<ul> <li>5 significant control weaknesses resulting in 7 recommendations issued during March 2011.</li> <li>14 recommendations issued since July 2010.</li> </ul>
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.	6 control findings resulting in 9 recommendations issued during March 2011. 68 recommendations issued since July 2010.

Total Audit Recommendations for FY 2010-11: 87

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### **Detailed Report**

Exhibit	Description	Comments
В	TITLE: Audit of the Ladera Ranch Community Facility Districts  DEPT: Auditor-Controller County Executive Office OC Public Works  Audit No: 2919  Issued: March 7, 2011	Scope: This is the first audit of the Ladera Ranch Community Facilities Districts (CFD) to ensure that: (1) special tax rates are calculated in accordance with pertinent governing documentation, and (2) bond proceeds are used for projects in compliance with pertinent documentation. In addition, we evaluated internal controls over processes for the Ladera Ranch CFDs.  Conclusion: We identified 2 Critical Control Weaknesses, 5 Significant Control Weaknesses, and 6 Control Findings resulting in 21 recommendations where internal controls and processes need to be improved in the calculation of the special tax rate and to ensure that bond proceeds are used only for authorized projects. The critical control weaknesses relate to the Auditor-Controller Public Finance Accounting's method for the calculation of the special tax levy and for unexplained project costs for El Toro Branch Library of \$803,000 charged to the Ladera Ranch CFDs.
		Background: The 6 Community Facilities Districts (CFDs) for Ladera Ranch received principal bond proceeds totaling \$287 million. The Ladera Ranch CFDs are designed to fund required infrastructure (e.g., roads, storm drains, fire stations, libraries, schools) to support current and future residential and commercial growth within land-based taxing regions called CFDs. Funds for CFDs are generated through the issuance of bonds. The County of Orange issued the 6 bonds on behalf of the Ladera Ranch CFDs pursuant to the terms and provisions of the Mello-Roos Community Facilities Act of 1982 (Government Code section 53311, et seq.).  The Public Finance Division (CEO/Public Finance) is part of the County Executive Office (CEO) under the leadership and oversight of the Chief Financial Officer (CFO) and the Director CEO/Public Finance. CEO/Public Finance is primarily responsible for managing the County's public debt programs, including CFDs.

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### **Detailed Report**

<b>Exhibit</b>	Description	Comments
	(Exhibit B continued)  TITLE: Audit of Ladera Ranch Community Facility Districts  DEPT: Auditor-Controller County Executive Office	CEO/Public Finance Accounting (PFA) is one of the Auditor-Controller's Satellite Accounting Operations (Auditor-Controller PFA). Auditor-Controller PFA is primarily responsible for providing specialized accounting support/services in accordance with the complex needs of CEO/Public Finance. An Accounting Services Agreement is in place between CEO and Auditor-Controller. Included in this Agreement is the requirement that the Auditor-Controller PFA develops accounting policies and procedures and develops and maintains accounting related internal controls.  Type of Recommendations:
	OC Public Works  Audit No: 2919  Issued: March 7, 2011	Objective #1 special tax rates are calculated in accordance with pertinent governing documentation. Results: We found that the calculation method and internal controls need to be improved over the annual special tax levy calculation process. We noted 1 Critical Control Weakness and 1 Significant Control Weakness in the area of the special tax levy calculation and 2 Control Findings in the areas of controls over monitoring special tax levy collections, and controls over notifying tax consultants of changes to parcel's information.
		Objective #2 bond proceeds are used for projects in compliance with pertinent documentation. Results: We found that internal controls and processes need to be improved to ensure that bond proceeds for projects are used in compliance with governing documentation. We noted 1 Critical Control Weakness in the area of project costs for the El Toro Branch Library charged to Ladera Ranch CFD, 4 Significant Control Weaknesses in the areas of monitoring project costs and cash available for project costs, incomplete policy and procedures, missing approval for allocating costs between CFDs, and controls over transfers of bond proceeds from Ladera Ranch CFD funds, and 4 Control Findings in the areas of administrative costs charged to incorrect funds, the use of anticipated interest earnings in the Acquisition, Funding, and Disclosure Agreements (AFDA) and amendments, and AFDA amendments not signed.

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### **Detailed Report**

Exhibit	Description	Comments
С	DEPT: Auditor-Controller Human Resources County Procurement Office	Scope: The monthly CAAT routines are automated queries applied to large amounts of electronic data searching for specified characteristics. We currently perform 1 ongoing CAAT routines utilizing selected payroll and vendor data. Depending on the nature of the CAAT, we perform them monthly, annually, or as necessary
	TITLE: Monthly Results of Continuous Auditing Using CAATS (Computer Assisted Audit Techniques) – March 2011	<ul> <li>Conclusion:         <ul> <li>Duplicate Payments to Vendors: We analyzed 15,007 vendor invoices paid in February 2011 amounting to about \$190 million and found 99.99% of the invoices were only paid once. Of the \$190 million vendor invoices, we identified 1 duplicate payment totaling \$2,702 made to vendors. The County currently has a recovery rate from vendors of about 94% on these duplicate payments.</li> </ul> </li> </ul>
	AUDIT NO: 1041-J ISSUED: March 17, 2011	Our prior research has indicated that duplicate payments are typically caused by a human clerical error. Based on the to-date recoveries of <b>\$918,138</b> , this CAAT routine has paid for itself and is returning monies to the County that may otherwise be lost.
		• Employee Vendor Match: All potential employee/vendor matches identified to date have been researched and resolved to Human Resource Department's satisfaction. Our next analysis will be performed at March 31, 2011.
		• Retiree/Extra Help Hours: As of February 17, 2011, no individuals have exceeded the annual limits for FY 10-11.
		Multiple Payroll Direct Deposits: No findings noted.

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### **Detailed Report**

Exhibit	Description	Comments
Exhibit	CONTINUED,  DEPT:     Auditor-Controller     Human Resources     County Procurement Office  TITLE: Monthly Results of Continuous Auditing Using CAATS (Computer Assisted Audit Techniques) – March 2011	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 Auditor-Controller, Human Resources, 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
D	TITLE: Final Close-out First Follow-Up Audit of Revenue Generating Lease Audit of JWA/Budget Rent A Car Systems, Inc.	Scope: We have completed a First and Final Follow-Up Audit of the Revenue Generating Lease Audit for JWA/Budget Rent A Car Systems, Inc. Our audit was limited to reviewing actions taken as of March 3, 2011 to implement the 1 recommendation made in our original audit report.  Conclusion: Our First Follow-Up Audit found the 1 recommendation was satisfactorily
	DEPT: John Wayne Airport	implemented. As such, this report represents the final close-out of the original audit.
	AUDIT NO: 1038-C (original audit no. 2931)  Issued: March 16, 2011	<b>Background:</b> The County entered into a lease agreement with Budget Rent A Car Systems, Inc., dated December 15, 2000, as amended, for the operation of an on-airport car rental agency at the John Wayne Airport terminal. During the original audit period, Budget Rent A Car Systems, Inc. reported approximately \$10.4 million in gross receipts and paid the County approximately \$1.6 million in rent. Over its 12 year term, this lease agreement is estimated to generate over <b>\$17 million</b> in rent to the County. The original audit reviewed whether Budget Rent A Car Systems, Inc.'s records adequately supported their monthly gross receipts reported to the County
		Type of Recommendations: None.

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