

IAD'S MONTHLY ACTIVITY REPORT

FOR

AUGUST 2005

TO THE

BOARD OF SUPERVISORS

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

by the Director of Internal Audit

Dr. Peter Hughes, MBA, CPA,

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*Integrity
Objectivity
Independence*

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We finished 9 projects this month:

- We completed 5 Audits:

Treasurer's Office:

On May 6, 2005, we issued a Report on Audit of Statement of Assets Held by the County Treasury as of December 31, 2005. In addition to that report, we issued: 1) a separate Management Letter and 2) a separate Confidential Supplement to the Management Letter on the audit of the Statement of Assets Held by the County Treasury as of December 31, 2004 dated August 31, 2005. These documents identified a total of 18 internal control weaknesses: 1 material weakness, 4 significant issues, and 13 reportable conditions.

3. Orange County Development Agency: We issued an audit report of internal controls over fund expenditures of the Orange County Development Agency. We identified no material weaknesses or significant issues; however, we identified 3 reportable conditions related to internal controls.
4. Auditor-Controller: We issued an audit report of internal controls over certain aspects of the Auditor-Controller's accounts receivable and collection processes. We identified no material weaknesses or significant issues; however, we identified 3 control findings.
5. Auditor-Controller: In conjunction with the above audit, we issued an audit report of the Auditor-Controller's general information technology controls and application controls related to its automated accounts receivable and collections system. We identified no material weaknesses or significant issues; however, we identified 37 control findings.

We issued 2 Reports of Monthly Computer Assisted Audit Techniques:

6. Auditor-Controller: We completed 2 of our monthly audits of vendor payments and identified 27 duplicate payments totaling \$9,135 that are being pursued by the Auditor Controller.

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7. Human Resources: At least 6 working retirees exceeded the legal thresholds for hours worked in fiscal year 04-05. Our review is in process.

We completed 2 Follow Up Audits.

8. Human Resources: We noted both recommendations pertaining to cash receipting and disbursements were fully implemented.
9. County Executive Office: We are pleased to report that all 4 recommendations pertaining to the Unemployment Insurance Compensation Reserve Fund have been fully implemented.

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MATERIAL FINDINGS

	Department and Description	Comments
1.	<p>DEPT: Treasurer-Tax Collector</p> <p>TITLE: Confidential Supplement to the Management Letter on Audit of the Statement of Assets Held by the County Treasury at December 31, 2004 (Confidential Report)</p> <p><u>Audit No:</u> 2409</p> <p>ISSUED: August 31, 2005</p>	<p>We identified one material and three significant audit findings and two reportable conditions in this report in the Treasurer’s office. The <u>material audit findings</u> involved an internal control weakness in the wire transfer of funds. The <u>significant audit findings</u> were related to logical security controls, IT security monitoring and internal controls over granting local area network access. (Confidential Finding)</p> <p>The Treasurer concurred with our findings and proposed corrective action that addressed the control weaknesses we identified in the report. (See item 2 on Page 2 of 9).</p> <p>Due to the control vulnerabilities these 5 findings presented to the County, we limited our descriptions to very general and abbreviated details.</p> <p>The full details were provided to the Treasurer, the Audit Oversight Committee, the Board of Supervisors and the County’s external auditors, Macias, Gini and Company.</p>

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NON-MATERIAL AUDIT FINDINGS

	Department and Description	Comments
2.	<p>DEPT: Treasurer-Tax Collector.</p> <p>TITLE: Management Letter on Audit of the Statement of Assets Held by the County Treasury at December 31, 2004.</p> <p>Audit No. 2409</p> <p>ISSUED: August 31, 2005</p>	<p>SCOPE: In planning and performing our audit for the purpose of expressing an opinion on the Treasurer-Tax Collector's (County Treasurer) Statement of Assets Held (financial statement), the American Institute of Certified Public Accounts requires that we obtain an understanding of the Treasurer's internal controls over financial reporting. In doing so, we identified deficiencies relating to the design or operation of the internal controls. These deficiencies have been identified in two documents, a Management Letter and a Confidential Supplement to the Management Letter.</p> <p>CONCLUSION: Based on our audit of the Treasurer's Statement of Assets, we identified 1 material weakness, 4 significant issues, and 13 reportable conditions.</p> <p>BACKGROUND: At December 31, 2004 the County Treasury had total assets of \$5.896 billion, of which \$3.12 billion was in the County Pool; \$2.714 billion was in the Education Pool; and \$61 million was Non-Pooled.</p> <p>California Government Code requires that the elected Auditor-Controller perform three quarterly reviews and one quarterly audit of the statement of assets in the County Treasury. The Auditor-Controller contracts with the Internal Audit Department to conduct the quarterly reviews and the quarterly audit.</p> <p>TYPE OF RECOMMENDATION: The material weakness dealt with internal control weakness in the wire transfer of funds process (Confidential Finding); the 4 significant issues were related to logical security controls (Confidential Finding), IT security monitoring (Confidential Finding); and internal controls over granting local area network access. The 13 reportable conditions were related to the following: security monitoring; local administrator rights granted to users; updating of the IT risk assessment; classification of IT resources; IT physical security; and IT evidence of review.</p>

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3.	<p>DEPT: Orange County Development Agency</p> <p>TITLE: Internal Control Review Orange County Development Agency Fund Expenditures</p> <p><u>Audit No.</u> 2433</p> <p>ISSUED: August 3, 2005</p>	<p>SCOPE: Our audit was limited to internal controls over fund expenditures for the period from July 1, 2004 to December 31, 2004. Our audit <u>excluded</u> disbursements, which were not classified as expenditures, such as loans made for the development of low-income affordable housing projects or for property improvements in redevelopment project areas.</p> <p>CONCLUSION: It is our opinion internal controls over OCDA fund expenditures are effective to ensure that these disbursements are properly authorized, accurate, supported and processed timely in accordance with management’s authorization and direction.</p> <p>BACKGROUND: OCDA is an agency, which operates as a legal entity separate and distinct from the County and is broadly empowered to engage in the general economic revitalization and redevelopment of the County through acquisition and development of property, public improvements, and revitalization activities. During our period of audit, fund expenditures for OCDA totaled \$2,958,785.18.</p> <p>TYPE OF RECOMMENDATIONS: No material weaknesses or significant issues were identified. However, we identified 3 reportable conditions related to internal controls over the receipt and review of journal vouchers from other departments/agencies that are charging their fund accounts; and the reviewing of invoices for mathematical accuracy.</p>

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4.	<p>DEPT: Auditor-Controller</p> <p>TITLE: Integrated Internal Control Review of the Auditor-Controller Accounts Receivable and Collection Processes.</p> <p><u>Audit No.</u> 2428-A</p> <p>ISSUED: August 11, 2005</p>	<p>SCOPE: Audit of non-IT procedures, processes and controls to ensure claims/invoices submitted to the Auditor-Controller are recorded accurately and timely as accounts receivable; accounts receivables are monitored using reconciliation and aging reports; and that collection efforts on delinquent accounts are performed in accordance with established procedures and statutory requirements, including writing off of uncollectible debts.</p> <p>CONCLUSION: No material weaknesses or significant issues were identified. Controls and processes were in place to ensure accounts receivable were recorded accurately and completely; subsidiary A/R records are reconciled monthly; management uses aging reports to monitor the outstanding accounts receivables; and collection efforts on delinquent accounts are generally performed in accordance with established procedures and statutory requirements. Our audit identified 3 control findings and recommendations to enhance processes and internal controls.</p> <p>BACKGROUND: The Accounts Receivable Unit receives invoices from County departments for monies owed to the County. They record each invoice/claim as a receivable on the Auditor-Controller’s accounts receivable system (CUBS), and process payments received. The General Ledger balance for accounts receivable was approximately \$36.7 million as of 12/31/04 and the Unit processes approximately \$200 million in receivables annually.</p> <p>The Collections Unit performs collection services for delinquent receivables for all County departments <u>except for</u> John Wayne Airport, the Social Services Agency, the Probation Department, the Public Defender, and the Treasurer-Tax Collector.</p> <p>TYPE OF RECOMMENDATIONS: Evaluate procedure for recording invoices into CUBS (currently using date when input into CUBS rather than actual date of invoice); ensure timely collection activities are performed in accordance with established procedures; conduct documented quality control reviews of collection activities.</p>

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5.	<p>DEPT: Auditor-Controller</p> <p>TITLE: Integrated Internal Control Review of the Auditor-Controller of the Accounts Receivable and Collection Processes - IT Results.</p> <p><u>Audit No.</u> 2428-B</p> <p>ISSUED: August 11, 2005</p>	<p>SCOPE: Audit of the Auditor-Controller’s general information technology (IT) controls and application controls in support of audit #2528-A’s scope above.</p> <p>CONCLUSION: No material weaknesses or significant issues were identified. Our audit identified 37 control findings and recommendations to enhance processes and internal controls.</p> <p>BACKGROUND: The Auditor-Controller utilizes Columbia Ultimate Business Systems' Revenue Plus Collector System. This system, known as CUBS, serves as the subsidiary accounts receivable ledger. As such, the initial recording and subsequent collection of receivables are recorded in CUBS. Data in CUBS typically includes names, addresses, social security numbers, and occasionally electronic protected health information (ePHI) as described in the Health Insurance Portability and Accountability Act (HIPAA). CUBS is also used to generate collection notices, maintain collector activity, and produce aging and other management reports. CUBS resides on the Auditor-Controller's local area network (LAN) and is maintained by the Auditor-Controller's Information Technology Division.</p> <p>TYPE OF RECOMMENDATIONS: Application and data validation features; business continuity management – local and enterprise; security program planning and management; security related personnel practices, user account management; physical security; logical security; security monitoring; software development and change control; and information resource classification.</p>

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6.	<p>DEPT: Board of Supervisors</p> <p>TITLE: Monthly Report on Computer-Assisted Audit Techniques (CAAT) for the Month of July 2005</p> <p><u>Audit No.</u> 2518-G</p> <p>ISSUED: August 5, 2005</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, biannually, or annually.</p> <p>CONCLUSION: <u>Duplicate Payments to Vendors:</u> 14 duplicate payments totaling \$6,999 were identified in the June 2005 data and are being pursued by the A-C. We perform this analysis monthly to identify duplicate payments made to vendors. We analyzed 22,287 invoices paid during July 2005 amounting to \$110,100,833.</p> <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.</p> <p>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 CEO/Purchasing 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> <p>TYPE OF RECOMMENDATIONS: No recommendations given.</p>

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<p>7. DEPT: Board of Supervisors</p> <p>TITLE: Monthly Report on Computer-Assisted Audit Techniques (CAAT) for the Month of August 2005.</p> <p><u>Audit No.</u> 2518-H</p> <p>ISSUED: August 30, 2005</p>	<p>SCOPE: The monthly CAAT Routines are automated queries applied to large amounts of electronic data searching for specified characteristics. We currently perform five CAATs routines utilizing selected payroll and vendor data. Depending on the nature of the CAAT, we perform them monthly, biannually, or annually.</p> <p>CONCLUSION: <u>Duplicate Payments to Vendors:</u> 13 duplicate payments totaling \$2,136 were identified in the July 2005 data and are being pursued by the A-C. We perform this analysis monthly to identify duplicate payments made to vendors. We analyzed 14,925 invoices paid during August 2005 amounting to \$108,707,130.</p> <p><u>Working Retirees:</u> At least 6 retirees exceeded the legal hour limits for fiscal year 2004/2005. Our review is still in process.</p> <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.</p> <p>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 CEO/Purchasing 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> <p>TYPE OF RECOMMENDATIONS: No recommendations given.</p>

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8.	<p>DEPT: Human Resources</p> <p>TITLE: Final Close Out - Follow-Up Audit Department Control Review Human Resources & Employee Relations/Employee Benefits Cash Receipts and Cash Disbursements Original Audit No. 2222</p> <p><u>Audit No.</u> 2533</p> <p>ISSUED: August 4, 2005</p>	<p>SCOPE: 2nd Follow-Up Audit of cash receipting and disbursement processes to determine if corrective action had been taken for the 2 recommendations not fully implemented at the time of our 1st Follow-Up Audit, dated August 31, 2004.</p> <p>In our 1st Follow-Up Audit, one recommendation concerning reconciliation of the special use revolving fund was identified as a significant issue, and the other recommendation for accountability over cash receipts was a reportable condition.</p> <p>CONCLUSION: Both recommendations are now fully implemented and as a result this audit has been closed out.</p> <p>BACKGROUND: The original audit assessed the processes, procedures and controls over cash receipts and disbursements processed primarily for health insurance premiums paid by employees and for claim disbursements made to a 3rd party health plan administrator. Employee Benefits maintained a special use revolving fund with an authorized amount of \$50,000 (subsequently increased to \$125,000) for the purpose of paying salary continuance to management and attorney employees. At the time of our original audit and 1st Follow-Up Audit, Employee Benefits was unable to reconcile the fund to the authorized balance.</p> <p>TYPE OF RECOMMENDATIONS: The original audit identified 6 recommendations to establish accountability over cash receipts; enhance physical safeguards over cash; reconcile cash receipts and disbursements to financial records; improve monitoring of premium collections; and prepare accurate bank reconciliations of the special use revolving fund to identify fluctuating fund overages and shortages.</p>

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9.	<p>DEPT: CEO</p> <p>TITLE: Final Close Out - Follow-Up Audit of Limited Review of the County Unemployment Insurance Compensation Reserve Fund #291, Original Audit No. 2343B</p> <p>Audit No. 2550</p> <p>ISSUED: August 11, 2005</p>	<p>SCOPE: 1st Follow-Up Audit of our limited review of the County's Unemployment Insurance Compensation Reserve Fund No. 291 to determine if corrective action had been taken for the four recommendations we noted in our original audit.</p> <p>CONCLUSION: We are pleased to report that all 4 recommendations have been fully implemented and as a result this audit has been closed out.</p> <p>BACKGROUND: Fund No. 291 provides for self-insurance of unemployment claims, administrative fees and related programs associated with the State mandated unemployment insurance program. This Fund is funded by charges to County departments for unemployment costs, which goes against payrolls as its primary funding source.</p> <p>TYPE OF RECOMMENDATIONS: The original audit identified 4 recommendations regarding the appropriateness of charges to Fund No. 291; the proper reserve balance; the appropriate department to manage and control Fund No. 291; and the adequacy of procedures to ensure they protect the integrity of the Fund.</p>