

## MONTHLY AUDIT ACTIVITY REPORT FOR SEPTEMBER 2008 TO THE BOARD OF SUPERVISORS

Presented on Board Agenda  
October 28, 2008

Project No. 2807-5

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

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# Letter from Director Peter Hughes



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October 28, 2008

Honorable Board of Supervisors,

It is my pleasure to submit to you the Monthly Audit Activity Report for the month of September 2008. Each report has an overview and a detailed briefing for your review.

We are happy to present as Exhibit B the Fiscal Year 2007/2008 Annual OC Internal Auditor Report to the Board. It was a successful year and this report details our accomplishments and activities.

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

Respectfully submitted,

A handwritten signature in blue ink that reads "Peter Hughes".  
Dr. Peter Hughes, CPA

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

**MONTHLY AUDIT ACTIVITY – September 2008**  
Status Report to the Board of Supervisors by IAD

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**THE FOLLOWING ITEMS ARE SUMMARIZED BELOW:**

Exhibit

Audits:

- B. Internal Audit Department: Annual OC Internal Auditor Report for Fiscal Year Ending June 30, 2008. This annual Internal Auditor's report details the year's accomplishments and activities. We've had another productive year. We provided audit coverage, presence or services to **twenty of the County's twenty-three departments and agencies**. We completed **seven (7) special request audits** directed by the Board of Supervisors and Audit Oversight Committee; **sixty-two (62) financial, operational, internal control, lease, and information technology audits**; and **(135) other audit projects** and support activities.
- C. County Executive Office: Analysis of the Savings from the Health Insurance Change as Part of the New Retirement Cost Offset. The County actually experienced cost savings of \$16 million and therefore \$16 million of savings was applied on a pro-rata basis to all participating labor organizations based on their medical cost totals. The pro-rata amount applied to OCEA members was \$11.2 million per fiscal year.
- D. Internal Audit Department: Industry Standards/Best Practice Research: Internal Audit Reporting Models for Large U.S. Counties and Cities by Population – Update #1. Orange County's IAD reporting model is the most widely used throughout the U.S. for similar sized counties and cities. This means that the Internal Auditor is an appointed position that reports to the elected Board of Supervisors/City Council and performs no management or accounting duties. This reporting model ensures the Internal Auditor's independence in strict accordance with the standards of the U.S. GAO, AICPA, and IIA.

Exhibit

Monthly Computer Assisted Audits of Vendor Payments (CAATs):

- E. Auditor Controller – Duplicate Payments to Vendors – September 2008: We analyzed **13,029** vendor invoices paid in August 2008 amounting to about **\$88 million** and found **99.99%** of the invoices were only paid once. Of the \$8 million vendor invoices, we identified **2** duplicate payments made to vendors totaling **\$2,492**.

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Exhibit

**Follow Up Audits:**

- F. Probation: **Final Close-Out** First Follow-Up Audit of Internal Control Review of Probation Department Bi-Weekly Payroll Process (Original Audit 2725). Satisfactory corrective action was taken on all **3** recommendations. **As such, this represents the final close-out of the original audit.**
- G. Auditor-Controller: **Final Close-Out** First Follow-Up Audit of Internal Control Review of Auditor-Controller Claims & Disbursing's Educational and Professional Reimbursement Process (Original Audit 2720-1). Satisfactory corrective action was taken on all **8** recommendations. **As such, this represents the final close-out of the original audit.**

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**Detailed Breakout**

**MATERIAL FINDING:**

	Department and Description	Comments
		None issued during September 2008.

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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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**NON-MATERIAL FINDINGS**

Exhibit	Description	Comments
B.	<p>DEPT: Internal Audit Department</p> <p>TITLE: <b>Annual OC Internal Auditor Report</b> for Fiscal Year Ending June 30, 2008</p> <p>Presented to the Audit Oversight Committee on September 17, 2008</p>	<p><b>Background:</b> The FY 2007/2008 Annual <b>OC Internal Auditor Report to the Board of Supervisors</b> is designed to provide the highlights and audit accomplishments of the audit activities during the past fiscal year. I am please to report we completed a very demanding audit plan that included several special request audits by the Board of Supervisors and the Audit Oversight Committee.</p> <p>The governance and accountability that the Board of Supervisors has established continue to ensure this department has the independence necessary to comply with all governmental and professional requirements. Clients and employees expressed satisfaction and continue to rate us highly in the areas of quality and communication.</p> <p><b>Conclusion:</b> We've had another productive year. We provided audit coverage, presence or services to <b>twenty of the County's twenty-three departments and agencies</b>. We completed <b>seven (7) special request audits</b> directed by the Board of Supervisors and Audit Oversight Committee; <b>sixty-two (62) financial, operational, internal control, lease, and information technology audits</b>; and <b>(135) other audit projects</b> and support activities for a total of <b>(204) completed audits and audit projects</b> for the year.</p> <p>The 135 audit projects noted above include 34 quarterly and monthly reports to the Board and AOC that supports giving them timely and critical detailed information to act on in their decision making process and to enable them to oversee the effectiveness of the internal audit department. All this achieves the accountability and transparency that the BOS is committed to and known for. Please see the report for full detail and all accomplishments.</p>

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Exhibit	Description	Comments
C.	<p>DEPT: County Executive Office</p> <p>TITLE: <b>Analysis of the Savings from the Health Insurance Change as Part of the New Retirement Cost Offset</b></p> <p>AUDIT NO: 2807-3</p> <p>ISSUED: September 5, 2008</p>	<p><b>Scope:</b> This report is in response to the Board of Supervisors' directive requesting that the Internal Audit Department provide the Board with a more detailed analysis of the savings realized from the health insurance changes as part of the new retirement cost offset.</p> <p><b>Conclusion:</b> The County actually experienced cost savings of \$16 million and therefore \$16 million of savings was applied on a pro-rata basis to all participating labor organizations based on their medical cost totals. The pro-rata amount applied to OCEA members was \$11.2 million per fiscal year.</p> <p><b>Background:</b> In Audit Report 2765, dated April 3, 2008 and titled Audit of the Source of Funding for the 2004 OCEA Pension Enhancements, the Internal Audit Department determined OCEA (the major labor organization in the County representing approximately 11,700 employees and composing approximately 71% of all County employees) employees accurately paid for their enhanced pension benefit for the three year period of our review.</p> <p>We reviewed Fiscal Years 2005/06, 2006/07, and 2007/08 and concluded that OCEA members paid \$80 million for the enhanced pension benefit component. This was the total of the annually required contributions for the three year period. The \$80 million dollar total is composed of \$46.4 million paid directly from employee contributions and \$33.6 million from medical insurance savings applied as a cost offset. Furthermore, the OCEA employee members continue to pay their annually required payments for their share of costs under their old plan.</p> <p><b>Type of Recommendations:</b> None</p>

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**MONTHLY AUDIT ACTIVITY – September 2008**  
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D.	<p>DEPT: Internal Audit Department</p> <p>TITLE: <b>Industry Standards/Best Practice Research: Internal Audit Reporting Models for Large U.S. Counties and Cities by Population – Update #1</b></p> <p>AUDIT NO: 2807-4</p> <p>ISSUED: September 26, 2008</p>	<p><b>Scope:</b> The Audit Oversight Committee (AOC), at their September 5, 2007 meeting, requested that the Internal Audit Department identify other similarly sized counties and cities throughout the U.S. that have an independent internal audit function similar to Orange County where the Internal Auditor is an appointed position that reports to the elected Board of Supervisors/City Council and has no management duties. In response to the AOC’s request, we issued a report, dated November 21, 2007, with our results that the OC internal audit reporting model was in fact widely used in large U.S. counties and cities. Our objective continues to be to identify the most regularly and widely used models or approaches to internal audit reporting for similarly sized counties and cities in the U.S. in order to determine both industry models as well as “best practices.”</p> <p>In this report, we identify the “Industry Standards” and compare them to the Best Practices specified by the three most widely recognized authoritative bodies in auditing; the U.S. Government Accountability Office (GAO), the Institute of Internal Auditors (IIA), and the American Institute of Certified Public Accountants (AICPA).</p> <p><b>Conclusion:</b> Our research continues to reveal that <b><u>the most regularly and widely used reporting model was the one adopted by the Orange County Board of Supervisors in 1995</u></b> and continued to this day. Specifically, the reporting models has the entity’s internal audit function report to the elected Board of Supervisors/City Council and perform <u>no</u> management duties.</p> <p>Our research also revealed that this reporting model fully complies with all three authoritative regulatory bodies for both external and internal auditing and as such is considered the “Best Practice” for an entity’s internal audit function.</p>

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Exhibit	Description	Comments
E.	DEPT: Auditor-Controller Human Resources County Procurement Office  TITLE: Computer Assisted Audit Techniques - September 2008  AUDIT NO: 2844-C  ISSUED: September 30, 2008	<p><b>Scope:</b> The monthly CAAT routines are automated queries applied to large amounts of electronic data searching for specified characteristics. We currently perform 4 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><b>Conclusion:</b></p> <ul style="list-style-type: none"> <li>• <u>Duplicate Payments to Vendors:</u> We analyzed 13,029 vendor invoices paid in August 2008 amounting to about <b>\$88 million</b> and found <b>99.99%</b> of the invoices were only paid once. Of the \$88 million vendor invoices we identified <b>2</b> duplicate payments made to vendors totaling <b>\$2,492</b>. The Auditor-Controller currently has a recovery rate from vendors of about <b>97%</b> on these duplicate payments. Our prior research has indicated that the duplicate payments are typically caused by a human clerical error.</li> </ul> <p>Based on the to-date recoveries of \$732,073 from the duplicate vendor payment routine, these CAAT routines have paid for themselves and are returning monies to the County that may otherwise be lost.</p> <ul style="list-style-type: none"> <li>• <u>Deleted Vendors:</u> No findings.</li> </ul> <p><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.</p>

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F.	<p>DEPT: Probation Department</p> <p>TITLE: <b>Final Close-Out</b> First Follow Up Audit of the Internal Control Review of Probation Department Bi-Weekly Payroll Process (Original Audit 2725)</p> <p>AUDIT NO: 2829-B</p> <p>ISSUED: September 5, 2008</p>	<p><b>Scope:</b> <b>First</b> Follow-Up Audit of the Probation Department Bi-Weekly Payroll Processes to determine the implementation status of <b>3</b> recommendations made in our original audit report, dated January 23, 2008. No material or significant issues were identified in the original audit report.</p> <p><b>Conclusion: We are pleased to report that satisfactory corrective action was taken on all 3 recommendations.</b> We commend the personnel at Probation for their responsiveness in addressing our recommendations. <b>As such, this report represents the final close-out of the original audit.</b></p> <p><b>Background:</b> Bi-weekly payroll for Probation’s approximately 1,600 employees is recorded using both Virtual Timesheet Interface (VTI) and manual timecards. About half of the Probation employees’ timecards are recorded in VTI and the other half use manual timesheets. During the audit period, the total <b>gross bi-weekly pay for Probation employees was \$128 million.</b></p> <p><b>Type of Recommendations:</b> Ensure payroll reports are reviewed and signed by the Probation/Payroll Supervisor and all documents are retained; utilize the modified <i>Timecard Audit Report</i> to monitor unauthorized changes to pay codes; Probation management continue its efforts to transition manual timecards to the automated VTI system.</p>

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Exhibit	Description	Comments
G.	<p>DEPT: Auditor-Controller</p> <p>TITLE: <b>Final Close-Out</b> First Follow-Up Audit of the Auditor-Controller Claims &amp; Disbursing's Educational and Professional Reimbursement Process (Original Audit No. 2720-1)</p> <p>AUDIT NO: 2829-C</p> <p>ISSUED: September 10, 2008</p>	<p><b>Scope:</b> <b>First</b> Follow-Up Audit of Auditor-Controller Claims &amp; Disbursing's Educational and Professional Reimbursement Process to determine the implementation status of <b>8</b> recommendations made in our original audit report, dated January 29, 2008. No material or significant issues were identified in the original audit report.</p> <p><b>Conclusion: We are pleased to report that satisfactory corrective action was taken on all 8 recommendations.</b> We commend A/C Claims &amp; Disbursing for their responsiveness in addressing our recommendations. <b>As such, this report represents the final close-out of the original audit.</b></p> <p><b>Background:</b> The Educational and Professional Reimbursement Program is designed to encourage employees to continue their professional development through a variety of opportunities, and are eligible for reimbursement of certain related expenses. The maximum qualified reimbursement an employee could receive in FY06/07 was \$2,000. During that period, A-C Claims processed <b>3,285 educational and professional reimbursement requests totaling \$1,420,893.</b></p> <p><b>Type of Recommendations:</b> Establish or enhance procedures for reimbursement requirements in areas of: professional exams, monitoring annual reimbursement limits, post quality assurance reviews, and processing timeframes; add a certification to new claim form regarding annual limit; monitor IRS maximum limits for non-taxable income.</p>

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