OC Board of Supervisors'

Internal Audit Department

ORANGE COUNTY

INDUSTRY STANDARDS/ BEST PRACTICE RESEARCH: INTERNAL AUDIT REPORTING MODELS FOR LARGE U.S. COUNTIES AND CITIES BY POPULATION

UPDATE #1

As of August 31, 2008

Orange County's Internal Audit Department 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.

REPORT NO: 2807- 4
REPORT DATE: SEPTEMBER 26, 2008

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Providing Facts and Perspectives Countywide

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To access and view audit reports or obtain additional information about the OC Internal Audit Department, visit our website: www.ocgov.com/audit

Orange County's Internal Audit
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Letter from Director Peter Hughes

Transmittal Letter

Report No. 2807- 4 **September 26, 2008**

TO: Members, Board of Supervisors

FROM: Dr. Peter Hughes, CPA, Director
Internal Audit Department

SUBJECT: Industry Standards/Best Practice Research: Internal Audit Reporting Models for Large U.S. Counties and Cities by Population – Update #1

We have completed our periodic research on the industry standards/best practices of internal audit reporting models for large U.S. counties and cities. The final results are attached for your review.

Our research indicates that Orange County's Internal Audit Department 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 Government Accountability Office (GAO), American Institute of Certified Public Accountants (AICPA), and Institute of Internal Auditors (IIA).

Each month I submit an **Audit Status Report** to the Board of Supervisors (BOS) and the results of this report will be included in a future status report to the BOS.

As always, the Internal Audit Department is available to address areas of interest to the Audit Oversight Committee. Please feel free to call me should you wish to discuss any aspect of our report.

Attachments

Other recipients of this report are listed on the Internal Auditor's Report on page 3.

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OC Internal Audit Report

INDUSTRY STANDARDS/BEST PRACTICE RESEARCH RESULTS

Report No. 2807- 4 **September 26, 2008**

TO: Members, Board of Supervisors

FROM: Dr. Peter Hughes, CPA, Director

SUBJECT: Industry Standards/Best Practice Research: Internal Audit Reporting Models for Large U.S. Counties and Cities by Population – Update #1

Audit Highlight

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.

Background

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."

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).

Our research continues to reveal that the most regularly and widely used reporting model was the one adopted by the Orange County Board of Supervisors in 1995 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 no management duties.

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.

Changes Reflected in Update #1

We have updated our research since our initial November 21, 2007 report to reflect current data including the addition of four counties and cities based on updated census estimates and the recent reporting change for the City of San Diego internal audit function. [1]

With the passing of Proposition C, the San Diego voters elected to split the Auditor and Comptroller's Office into two separate offices: the Office of the City Auditor and the Office of the City Comptroller, effective July 1, 2008. In accordance with the proposition, the new City Auditor was appointed by the elected Mayor, in consultation with the Audit Committee and confirmed by the City Council, to serve a ten year term subject to reappointment. The City Auditor reports to the Council's Audit Committee and may be removed for cause by a vote of two-thirds of the City Council. The City of San Diego now has a similar reporting model as Orange County.

Additionally, Orange County implemented a new Performance Audit function and we identified that Miami-Dade County has two internal audit entities.

Work Performed

We identified 5 different internal audit reporting models used by the 34 largest U.S. counties and cities by population. We determined the best source of readily available information regarding county and city internal audit functions was the 2006 membership directory and the 2008 Local Government Audit Survey compiled by the Association of Local Government Auditors. In addition, we reviewed the relevant city and county audit websites to rule out any audit functions that perform management duties. See source data in the attachments.

Results

Orange County's Internal Audit Department reporting model is the most widely used throughout the U.S. in large counties and cities.

A combined average of **53%** of the **34** largest U.S. Counties **(17)** and Cities **(17)** based on population, including Orange County, **share the Orange County model (Model 1)**. 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.

[1] While not a large city included in our data, we also identified a charter change for the City of Modesto Auditor. On February 5, 2008, with the passing of Measure M: The Increase Accountability in City Hall Measure of 2008, the City of Modesto citizens elected to separate the City Auditor from the City Clerk, and have the City Auditor report directly to the City Council.

The other 4 internal audit reporting models had the following average percentage of use:

Model 2: **9%** The Auditor/Internal Audit Director is an appointed position that reports to the County/City Manager and performs no management or accounting duties.

Model 3: **20%** The Auditor/Auditor-Controller is elected and performs both audit and management duties.

Model 4: **12%** The Auditor/Auditor-Controller is an appointed position that reports to the elected Board of Supervisors/District Judges and performs both audit and management duties.

Model 5: **6%** The Auditor-Controller/Controller-Treasurer is an appointed position that reports to the Chief Administrative Officer/Chief Financial Officer and performs both audit and management duties.

State Laws/Historical Precedent May Impact Our Results

When conducting our research we identified two States, California and Texas, with statewide laws generally stating that the Auditor also be given the duties of Controller. The laws were made many years ago prior to the current revisions to the U.S GAO's Government Auditing Standards regarding auditor independence.

Specifically, under the U.S. GAO's Government Auditing Standards a government internal audit function is organizationally independent if the head of the audit organization is accountable and reports to the head of the government entity and is located organizationally outside the management function and has no management duties.

Our data of 34 large U.S. Counties and Cities includes 7 California and Texas counties (includes San Francisco City/County) that have internal audit functions within the Auditor Departments that also perform Controller duties (i.e., accounting and management duties).

As such, they do not reflect current views for independence of the internal audit function, but rather continue the historical/law based precedent.

Attachments

Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Audit Oversight Committee
Thomas G. Mauk, County Executive Officer
Foreperson, Grand Jury
Darlene J. Bloom, Clerk of the Board of Supervisors

DETAILED RESULTS

Based on our research, the five most common reporting models for the internal audit function in the 34[2] largest U.S. counties and cities (based on population) are as follows:

Model #1 (OC Model): The Auditor/Internal Audit Director is an appointed position that reports to the elected Board of Supervisors/City Council and performs no management or accounting duties. See details:

47% Top U.S. Counties Adopted Model #1

Size Ranking	County	State
2	Cook	IL
4	Maricopa	AZ
5	Orange – Internal Audit Dept[2]	CA
5	Orange – Performance Auditor[2]	CA
8	Miami-Dade – Commission Auditor[2]	FL
13	Wayne	MI
14	King	WA
16	Broward	FL

59% of Top U.S. Cities Adopted Model #1

Size Ranking	City	State
3	Chicago	IL
7	San Antonio	TX
8	San Diego	CA
9	Dallas	TX
10	San Jose	CA
11	Detroit	MI
12	Jacksonville	FL
13	Indianapolis	IN
16	Austin	TX
17	Fort Worth	TX

Model #2: The Auditor/Internal Audit Director is an appointed position that reports to the County/City Manager and performs no management or accounting duties. See details:

12% of Top U.S. Counties Adopted Model #2

Size Ranking	County	State
8	Miami-Dade – Audit and Mgmt Services[2]	FL
15	Clark County	NV

6% of Top U.S. Cities Adopted Model #2

Size Ranking	City	State
5	Phoenix	AZ

[2] Two New York Burroughs are not included in the County percentage as already presented in the City percentage. In addition, two counties (Orange and Miami-Dade) have two internal audit functions with countywide audit responsibilities. Both internal audit functions are included in the counts/percentages.

Model #3: The Auditor/Auditor-Controller is elected and performs both audit and management duties. See details:

12% of Top U.S. Counties Adopted Model #3

Size Ranking	County	State
11	Riverside	CA
12	San Bernardino	CA

29% of Top U.S. Cities Adopted Model #3

Size Ranking	City	State
1	New York	NY
2	Los Angeles	CA
4	Houston	TX
6	Philadelphia	PA
15	Columbus	OH

Model #4: The Auditor/Auditor-Controller is an appointed position that reports to the elected Board of Supervisors/District Judges and performs both audit and management duties. See details:

17% of Top U.S. Counties Adopted Model #4

Size Ranking	County	State
1	Los Angeles	CA
3	Harris	TX
9	Dallas	TX

6% of Top U.S. Cities Adopted Model #4

Size Ranking	City	State
14	San Francisco	CA

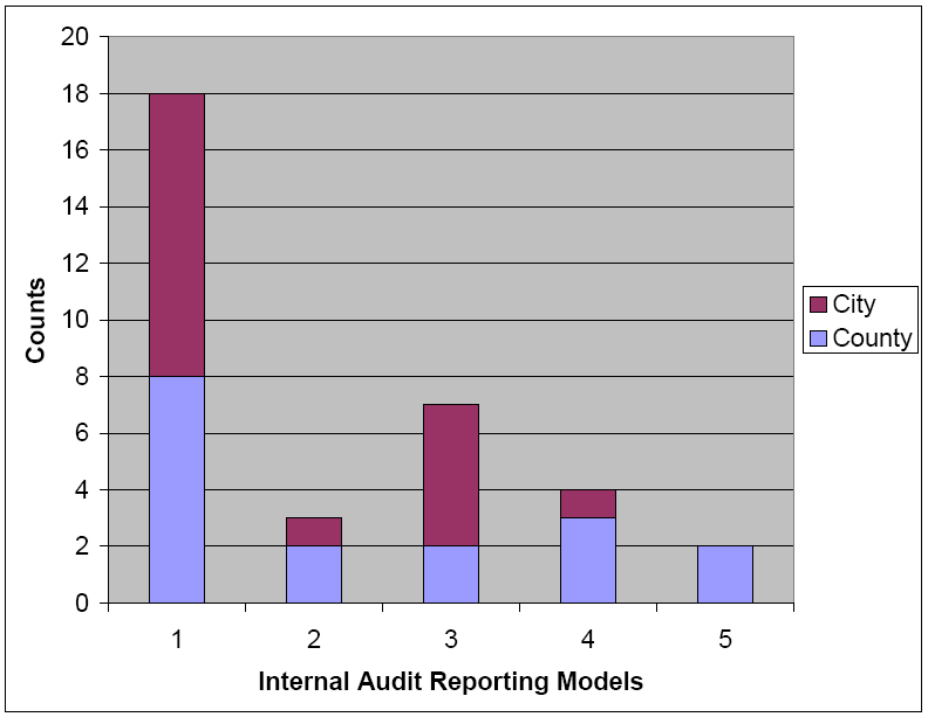
Model #5: The Auditor-Controller/Controller-Treasurer is an appointed position that reports to the Chief Administrative Officer/Chief Financial Officer and performs both audit and management duties. See details:

12% of Top U.S. Counties Adopted Model #5

Size Ranking	County	State
6	San Diego	CA
17	Santa Clara	CA

SUMMARY

Orange County's IAD reporting model (Model 1) is the most widely used throughout the U.S. in large counties and cities as depicted in the below chart:



LEGEND:

Model 1 (OC Model): 53% The Auditor/Internal Audit Director is an appointed position that reports to the elected Board of Supervisors/City Council and performs no management or accounting duties.

Model 2: 9% The Auditor/Internal Audit Director is an appointed position that reports to the County/City Manager and performs no management or accounting duties.

Model 3: 20% The Auditor/Auditor-Controller is elected and performs both audit and management duties.

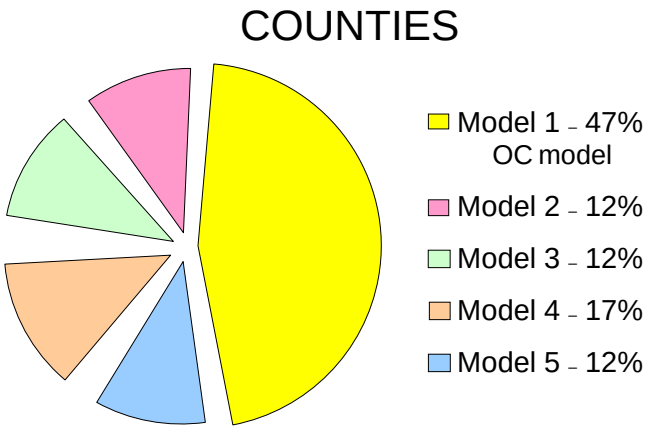
Model 4: 12% The Auditor/Auditor-Controller is an appointed position that reports to the elected Board of Supervisors/District Judges and performs both audit and management duties.

Model 5: 6% The Auditor-Controller/Controller-Treasurer is an appointed position that reports to the Chief Administrative Officer/Chief Financial Officer and performs both audit and management duties.

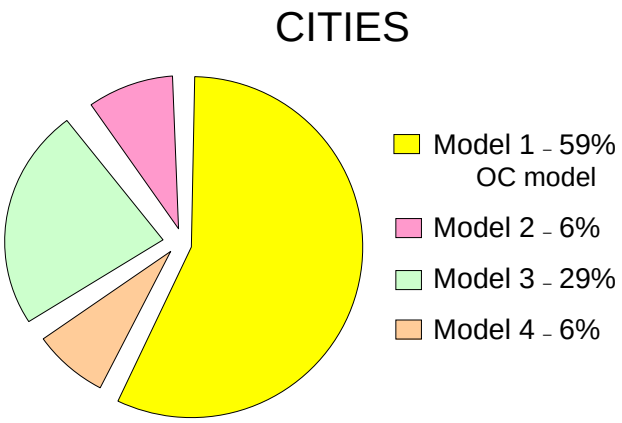
As a combined average, **53%** of the 34[3] largest U.S. Cities and Counties have established an internal audit function that **share the OC Internal Audit Department reporting model** where the Internal Auditor is an appointed position that reports to the elected County Supervisors/City Council and has no management duties.

[3] Two New York Burroughs were not included in the County percentage as already presented in the City percentage. In addition, two counties (Orange and Miami-Dade) have two internal audit functions with countywide audit responsibilities. Both internal audit functions are included in the counts/percentages.

47% of the 17[4] largest counties (based on population including Orange County) **share the Orange County model**:



59% of the 17 largest cities (based on population) **share the Orange County model**:



LEGEND:

Model 1 (OC Model) – The Auditor/Internal Audit Director is an appointed position that reports to the elected Board of Supervisors/City Council and performs no management or accounting duties.

Model 2 – The Auditor/Internal Audit Director is an appointed position that reports to the County/City Manager and performs no management or accounting duties.

Model 3 – The Auditor/Auditor-Controller is elected and performs both audit and management duties.

Model 4 – The Auditor/Auditor-Controller an appointed position that reports to the elected Board of Supervisors/District Judges and performs both audit and management duties.

Model 5 – The Auditor-Controller/Controller-Treasurer is an appointed position that reports to the Chief Administrative Officer/Chief Financial Officer and performs both audit and management duties.

[4] Two New York Burroughs were not included in the County percentage as already presented in the City percentage. In addition, two counties (Orange and Miami-Dade) have two internal audit functions with countywide audit responsibilities. Both internal audit functions are included in the counts/percentages.

ATTACHMENT A: Top 17 U.S. Counties by Population

(1) Rank	(2) County	(3) Population	(4) Function Name	(5) Has Mgmt Duties	(6) Doesn't Have Mgmt Duties	(7) Description of Management Duties	(8) Elected	(9) Appointed	(10) If appointed, reports to:
1	Los Angeles County, CA	9,878,554	Auditor-Controller	X		Controller		X	Board of Supervisors
2	Cook County, IL	5,285,107	County Auditor		X			X	Board of Commissioners
3	Harris County, TX	3,935,855	County Auditor	X		CFO		X	State District Judges
4	Maricopa County, AZ	3,880,181	County Auditor		X			X	Board of Supervisors
5	Orange County, CA	2,997,033	Internal Audit Department		X			X	Board of Supervisors
			Performance Auditor		X ^			X	Board of Supervisors^
6	San Diego County, CA	2,974,859	Auditor-Controller	X		Controller		X	CAO
7	Kings County, NY (Brooklyn)	2,528,050	A Borough of New York City	N/A *	N/A *	N/A *	N/A *	N/A *	N/A *
8	Miami-Dade County, FL	2,387,170	Audit & Management Services		X			X	County Manager
			Commission Auditor		X ^			X	Board of County Commissioners^
9	Dallas County, TX	2,366,511	County Auditor	X		CFO		X	State District Judges
10	Queens County, NY	2,270,338	A Borough of New York City	N/A *	N/A *	N/A *	N/A *	N/A *	N/A *
11	Riverside County, CA	2,073,571	Auditor-Controller	X		Controller	X		N/A
12	San Bernardino County, CA	2,007,800	Auditor-Controller Recorder	X		Controller & Recorder	X		N/A
13	Wayne County, MI	1,985,101	Legislative Auditor General		X			X	County Commission
14	King County, WA	1,859,284	County Auditor		X			X	County Council
15	Clark County, NV	1,836,333	Internal Audit		X			X	County Manager
16	Broward County, FL	1,759,591	County Auditor		X			X	County Commission
17	Santa Clara County, CA	1,748,976	Controller-Treasurer	X		Controller & Treasurer		X	Finance Agency Director
				7	**10**	**Total**	**2**	**15**	
				41%	**59%**		**12%**	**88%**	

Source:
Top 17 US Counties obtained from US Census Bureau Population Estimates for the 100 largest US Counties Based on July 1, 2007 Population Estimates. Remaining data obtained from relevant website or material available on the website.

Legend:
***** Not included in counts/percentages because already represented by City of NY.
^ Two separate internal audit functions for the county; both internal audit functions included in counts/percentages.

8 of 17 = 47% **Model #1 (OC Internal Audit Department)** The Auditor/Internal Audit Director is an appointed position that reports to the elected Board of Supervisors/City Council (column 10) and performs no management duties (column 6).

2 of 17 = 12% **Model #2:** The Auditor/Internal Audit Director is an appointed position that reports to the County Manager (column 10) and performs no management duties (column 6).

2 of 17 = 12% **Model #3:** The Auditor/Auditor-Controller is an elected position (column 8) and performs both audit and management duties (column 5).

3 of 17 = 17% **Model #4:** The Auditor/Auditor-Controller is an appointed position that reports to the elected Board of Supervisors/District Judges (column 10) and performs both audit and management duties (column 5).

2 of 17 = 12% **Model #5:** The Auditor-Controller/Controller-Treasurer is an appointed position that reports to the Chief Administrative Officer/Finance Officer (column 10) and performs both audit and management duties (column 5).

ATTACHMENT B: Top 17 U.S. Cities by Population

(1) Rank	(2) City	(3) Population	(4) Function Name	(5) Has Mgmt Duties	(6) Doesn't Have Mgmt Duties	(7) Description of Management Duties	(8) Elected	(9) Appointed	(10) If appointed, reports to:
1	New York, NY (City and Boroughs aka Counties)	8,274,527	Comptroller	X		Comptroller/ CFO	X		N/A
2	Los Angeles, CA	3,834,340	City Controller	X		Controller	X		N/A
3	Chicago, IL	2,836,658	Inspector General		X			X	Elected Mayor & City Council
4	Houston, TX	2,208,180	City Controller	X		Controller	X		N/A
5	Phoenix, AZ	1,552,259	City Auditor		X			X	City Manager & Council's Audit Committee
6	Philadelphia, PA	1,449,634	City Controller	X		Approve disbursements	X		N/A
7	San Antonio, TX	1,328,984	City Auditor		X			X	City Council
8	San Diego, CA	1,266,731	City Auditor		X			X	City Council
9	Dallas, TX	1,240,499	City Auditor		X			X	City Council
10	San Jose, CA	939,899	City Auditor		X			X	City Council
11	Detroit, MI	916,952	Auditor General		X			X	City Council
12	Jacksonville, FL	805,605	Council Auditor		X			X	City Council
13	Indianapolis, IN (City & Marion County)	795,458	City-County Internal Audit Agency		X			X	City-County Council
14	San Francisco, CA (City & County)	764,976	Controller	X		Chief Accounting Officer		X	Elected Mayor & Board of Supervisors
15	Columbus, OH	747,755	City Auditor	X		Chief Accounting Officer	X		N/A
16	Austin, TX	743,074	City Auditor		X			X	City Council
17	Fort Worth, TX	681,818	City Auditor		X			X	City Council
				6	**11**	**Total**	**5**	**12**	
				35%	**65%**		**29%**	**71%**	

Source:
Top 17 US Cities obtained from US Census Bureau Annual Estimates of the Population for Incorporated Places Over 100,000, Ranked by July 1, 2007 Population. Remaining data obtained from relevant website or material available on the website.

10 of 17 = 59% **Model #1 (OC Internal Audit Department)** The Auditor/Internal Audit Director is an appointed position that reports to the elected Board of Supervisors/City Council (column 10) and performs no management duties (column 6).

1 of 17 = 6% **Model #2:** The Auditor/Internal Audit Director is an appointed postion that reports to the County Manager (column 10) and performs no management duties (column 6).

5 of 17 = 29% **Model #3:** The Auditor/Auditor-Controller is an elected position (column 8) and performs both audit and management duties (column 5).

1 of 17 = 6% **Model #4:** The Auditor/Auditor-Controller is an appointed position that reports to the elected Boardof Supervisors/District Judges (column 10) and performs both audit and management duties (column 5).

0 of 17 = 0% **Model #5:** The Auditor-Controller/Controller Treasurer is an appointed position that reports to the Chief Administrative Officer/Finance Officer (column 10) and performs both audit and management duties (column 5).