



INTERNAL AUDIT DEPARTMENT

COUNTY OF ORANGE

**2005 Recipient of the Institute of Internal Auditors
Award for Excellence**

Integrity ♦ Objectivity ♦ Independence

DRAFT

FY 06-07 Audit Plan

Date: Date

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**COUNTY OF ORANGE
Internal Audit Department**

FY 06-07 Audit Plan

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EXECUTIVE SUMMARY

MISSION STATEMENT

The mission of the Internal Audit Department is to provide reliable, independent, objective evaluations and business and financial advisory services to the Board of Supervisors and County executive management. Our role is to assist both parties with their important business and financial decisions; as well as, to contribute to protecting and safeguarding the County's resources and assets.

We support and assist the Board of Supervisors and County Executive Management in the accomplishment of their functional business goals and objectives. Our contribution to this effort is testing and reporting on their internal control systems and processes. County executive management is responsible for establishing and maintaining these control processes because they must rely on these systems and processes in managing their complex organizations. These systems and processes are used for safeguarding the County's assets and resources, and for reasonable, prudent, and effective financial stewardship and for accurate recording and reporting.

The IAD is recognized for our internal controls expertise. We apply this expertise in assisting County Executive Management in enhancing their business processes and constantly improving and strengthening the internal control environment the public expects, relies upon, and demands of its government. We are committed to a process of continuous learning and improvements within our department. We keep ourselves updated on relevant issues in business and industry with regard to accounting trends and developing financial best practices. Such constant renewal keeps the IAD and its staff professionally current, refreshed, invigorated, and responsive to the County's needs for attestation, compliance assurance, accountability testing, and business improvement. We assist management in helping to implement best business practices with regard to internal controls, accounting systems, and business processes.

To meet our clients' expectations for integrity, objectivity, and independence and for us to function effectively with consistent reliability and credibility, the IAD applies professional auditing standards to all engagements. This allows us to ensure reviews and assessments of County operations are always informative, accurate, and objective. Where required, the IAD follows the ethical and professional standards promulgated by the American Institute of Certified Public Accountants (AICPA), the Institute of Internal Auditors (IIA), the Information Systems Audit and Control Association (ISACA), and the Government Accountability Office (GAO). Moreover, the quality of IAD operations is regularly and independently assured by rigorous peer reviews conducted by outside CPA firms. We have passed three such quality reviews to date; the last in 2004 being the most extensive quality review conducted outside the jurisdiction of the GAO. The next quality review is now being planned for 2007. As further validation of our department's commitment to quality, we received the IIA's "Award for Excellence" in 2005.



Our Business Plan goals are consistent with our annual Audit Plan because our role within Orange County is limited and well defined. Our annual Business Plan is reviewed by the CEO's Office and our Audit Plan is submitted, discussed, and approved each fiscal year by the Audit Oversight Committee (AOC). Our annual Audit Plan is challenging to complete, but it does include some flexibility to be responsive to the Board of Supervisors. At times, they request audit services during the year and we have hours specifically reserved for this purpose. In 2005, we converted our annual Audit Plan from a calendar year basis back to a fiscal year basis. The purpose of this change was to better synchronize the annual Audit Plan with the budget and business plans.

Our Audit Plan has as its foundation the traditional internal audits of "hard-control areas" such as segregation of duties, limiting access to cash, and accurate originating accounting entries and transactions. Examples of such traditional audits in our Audit Plan include those audits included in the Financial Audits and Mandates (FAM), Internal Control Reviews (ICR), and Information Technology Audits (IT) sections. These audit reports contain opinions regarding the status of internal controls or the County's compliance with grant or other governing provisions. Our audit reports also include recommendations to management regarding improvements to specific accounting processes and internal controls in order to enhance or strengthen them. As part of our internal improvement process, we distribute a customer survey with each of our audit reports to allow customer evaluation and feedback.

We are now including in our audits steps for testing the economy and efficiency of operations, and our reports now where applicable, contain recommendations related to economy and efficiency enhancements. In addition, we are continuing our Performance Measure Validation Audits initiated in late 2005. These reviews validate the performance measures included in the annual business plans produced by the County departments. The Follow-Up Audit process was recently enhanced and is now continuing as a robust and mature process. Based on our Follow-Up Audits, we can state that County management substantially implements our report recommendations on a timely basis. We attribute this level of management cooperation to the partnership we have created with County management.

GOALS

Strategic Goals:

IAD continues to implement the two fundamental strategic goals of this audit organization begun in prior years. These two goals remain at the heart of our operation. We reassess them annually and they continue to be relevant in guiding the professional direction of the department.

1. We assist the Board of Supervisors and County management in ensuring the County's assets and resources are safeguarded, the County's accounting and financial reporting is timely and accurate, and the County's management has timely information and relevant analysis for its business and financial decisions.



2. We provide professional assurance, attestation, and corrective recommendations to our clientele on the County's internal controls, accounting records, and financial and business operations through our published audit reports and reviews.

We have incorporated these Business Plan goals into our Annual Audit Plan.

Outcome Measures:

For the year 2005, we successfully met our two key outcome measures. Our audit efforts and the diligence and responsiveness of County management contributed to the achievement of these measures. Our two key outcome measures were successful last year because:

- The County had no defalcation or reported cash losses material to the County.
- A high percentage of clients reported they received information and/or recommendations that were timely and helpful to them in safeguarding the County's assets and making business decisions. With few exceptions, our control recommendations are addressed by management and the majority are implemented.



ANNUAL AUDIT PLAN & KEY AUDIT CATEGORIES

Our Audit Plan is submitted, discussed, and approved at the beginning of each fiscal year by the Audit Oversight Committee (AOC). We are dedicated to completing our Audit Plan while continuing to be flexible and responsive to the Board's requests for audit services.

The Audit Plan has at its core the traditional audits of "hard-controls;" such as segregation of duties, limiting access to cash, and accurate originating accounting entries and transactions. Examples of these traditional audits in our audit plan include our core business functions identified as Financial Audits and Mandates (FAM), Internal Control Reviews (ICR), and Information Technology Audits (IT). Our reports contain opinions regarding the presentation of financial statements or the County's compliance with grant or other governing provisions. Our reports also include recommendations to management regarding improvements to specific accounting processes and internal controls.

Our Follow-Up Audit process is necessary to ensure that our audit recommendations are implemented satisfactorily. In 2005, IAD implemented a more structured and rigorous Follow-Up Audit process in response to suggestions made by the AOC and the Board of Supervisors. Our first Follow-Up Audit now begins at six months following the release of an audit report. If necessary, a second Follow-Up Audit will be conducted about 12 months from the release of the original audit report. At the request of the AOC, we are to bring to their attention any audit recommendations we find still not addressed, resolved or mitigated after the second follow-up.

We are pleased to report that County management substantially implements our recommendations on a timely basis. We also compliment County management with partnering with us with in this effort to be responsive.

For 2006, we are continuing our new category of audits called Performance Measure Validation (PMV) Audits. Our audit scope is limited to reviewing the documentation that supports the departments' assertion as to the achievement of their key outcome indicators. We issue audit reports that state the outcome indicators, the department's reported results, and whether we found adequate documentation that supports the reported results.

We combine the three core groups of "hard control" audits (FAM, ICR, and IT) with Performance Measure Validation Reviews (PMV) to achieve a balanced audit coverage of the County.



DEDICATION OF RESOURCES TO AUDIT RELATED SERVICES

Our Audit Plan is based on 18,500 direct audit hours to be provided by 13 audit professionals. We currently have 3 audit position vacancies, one of which is our IS auditor position. The Audit Plan does not include hours for these vacant positions. Because of new federal laws (Sarbanes-Oxley Act), auditors are in high demand, and we are on the low side for salaries. We may find filling these positions and in particular the IS audit position difficult at this time. We are working with Human Resources on creative recruiting efforts to counter the high demand situation. The audit hours for the Director and Deputy Director are not included in the above total and the time for the three Audit Managers is adjusted downward to allow them time for administrative management.

These hours are allocated to the audit areas as follows:

Financial Audits and Mandates (FAM):	3,190
Information Technology (IT) Audits:	2,000
Internal Control Reviews (ICR):	4,200
Facilitated Control Self-Assessment (CSA):	1,050
Lease Revenue Reviews & Compliance Audits:	4,940
Performance Measure Validations (PMV):	1,400

The plan also allocates an additional **1,720** hours for audit activities such as staffing the fraud hotline, reviewing cash losses, administering data collection of external audits, conducting training classes in County departments on practical internal control concepts and application, performing the annual risk assessment, HIPAA Administration, and compiling and presenting activity reports to the Board of Supervisors, Audit Oversight Committee, and Board Executive Assistant briefings.

Within the **18,500** hours, we reserved **725** hours to respond to Board requests for audit services. In addition to our 18,500 direct hours, we contract out to industry experts certain audits such as information technology audits. We estimate that these consultants will provide **700** hours of work effort. Our FY 06-07 Audit Plan is detailed on the following page.



**County of Orange Internal Audit Department
DRAFT Fiscal Year 06 - 07 Audit Plan**

<u>Audit Name</u>	<u>Audit #</u>	<u>Budgeted Hours</u>
FINANCIAL AUDITS & MANDATES (FAM)		
1 Treasury Funds Audit - 6/30/06 (carry over)		225
2 Treasury Funds Audit - 9/30/06		275
3 Treasury Funds Audit - 12/31/06		1,200
4 Treasury Funds Audit - 3/31/07		275
5 Treasury Funds Audit - 6/30/07		50
6 DA Spousal Abuser Prosecution Grant - 6/30/06		160
7 DA Workers Comp/Auto Insurance Fraud Grant - 6/30/06		250
8 DA Health & Disability Insurance Fraud Grant - 6/30/06		250
<u>Follow-Ups (Initial):</u>		
9 - Treasury Funds Audit - 12/31/05 - Management Letter		150
10 - Probation Audit - 2 YE 6/30/05		100
11 - Tax Redemption Audit - 3 YE 6/30/05		100
12 Auditing & Accounting Standards Update		115
13 Work Paper Close-Out & Final Report Issuance (audits from 2005 plan)		40
	Subtotal	3,190
INFORMATION TECHNOLOGY AUDITS (IT)		
1 CAPS - Integrated Procurement & Payables Processing Pilot (IP3) - carry over		50
2 CAATs - Monthly Analysis of Certain Disbursement and Payroll Data		600
3 Assist on IT Component of 12/31/06 TFA		100
4 IT Audit - tbd (conducted by either an external consultant or hire of new IT auditor)		700
<u>Follow-Ups (Initial):</u>		
5 HCA Self Assessment Validation		250
<u>Follow-Up Audits (Secondary):</u>		
- IWMD LIST Implementation Review		200
6 Review of New System Implementation Notifications (AM No. S-1)		75
7 IT Research & Development		25
	Subtotal	2,000
INTERNAL CONTROL REVIEWS (ICR)		
1 Purchasing Cards - CEO/Purchasing and Selected Depts.		400
2 CEO/Public Finance - scope to be determined		400
3 Department/Agency Payroll Reviews		400
4 RDMD/Contract Administration & Disbursements- specific area to be determined		400
5 Probation Dept. - Contract Administration & Disbursements (or Collections)		400
6 Tax Collector - Collections Process		400
7 Treasurer-Interest Apportionment Process		400
<u>Follow-Up Audits (Initial):</u>		
8 PA/PG Cash Receipts, Disbursements, Trust Funds & Property		1,000
9 RDMD/O.C. Zoo Cash Receipts & Disbursements		
10 SSA Accounts Receivable & Collections		



INTERNAL CONTROL REVIEWS (ICR) Continued

11	JWA Public Works Contract Administration	
12	NSF Check Notification Process	
13	tbd	
14	tbd	
15	tbd	
16	tbd	
	<u>Follow-Up Audits (Secondary):</u>	380
17	RDMD Trust and Agency Fund Disbursements	
18	tbd	
19	tbd	
20	Work Paper Close-Out & Final Report Issuance (audits from 2005 plan)	20
	Subtotal	4,200

CONTROL SELF-ASSESSMENT (CSA)

1	CSA - HCA/Financial & Administrative Services	500
2	CSA - tbd	500
3	CSA Promotion	50
	Subtotal	1,050

LEASE REVENUE REVIEWS & COMPLIANCE REVIEWSLease Revenue Reviews:

1	- JWA/tbd	300
2	- JWA/tbd	300
3	- JWA/tbd	350
4	- RDMD - Science Enrichment Services	300
5	- RDMD/Green Meadows	300
6	- DPHD/Anchor Marine	350
7	- DPHD/Dana Point Jet Ski	350
8	RDMD/tbd	350

Follow-up on Lease Revenue Reviews (Initial):

		1,100
9	JWA/Signature Flight Support	
10	- JWA/Avis Rent a Car	
11	- JWA/Advantage Rent a Car	
12	- RDMD/Anaheim Arena Parking	
13	- RDMD/PCI Parking	
14	- RDMD/Swales Anchorage	
15	DPHD/Rancho Beach House	
16	DPHD/Dana Point Marina Inn	
17	RDMD/Newport Dunes	
18	DPHD/Dana West Marina	
19	DPHD/Dreamcatcher Yachts	100
20	DPHD/Ship to Shore Insurance	100
21	DPHD/Aventura Sailing	
22	DPHD/Noel Marina Canvas	
23	DPHD/OCMI	



LEASE REVENUE REVIEWS & COMPLIANCE REVIEWS (Continued)Compliance & Other Audits:

24	- HIPAA Security Review Compliance Review	300
25	Work Paper Close-Out & Final Report Issuance (audits from 2005 plan)	15
	Reserve for Additional Audit Requests	725
	Subtotal	4,940

PERFORMANCE MEASURE VALIDATION (PMV) AUDITS

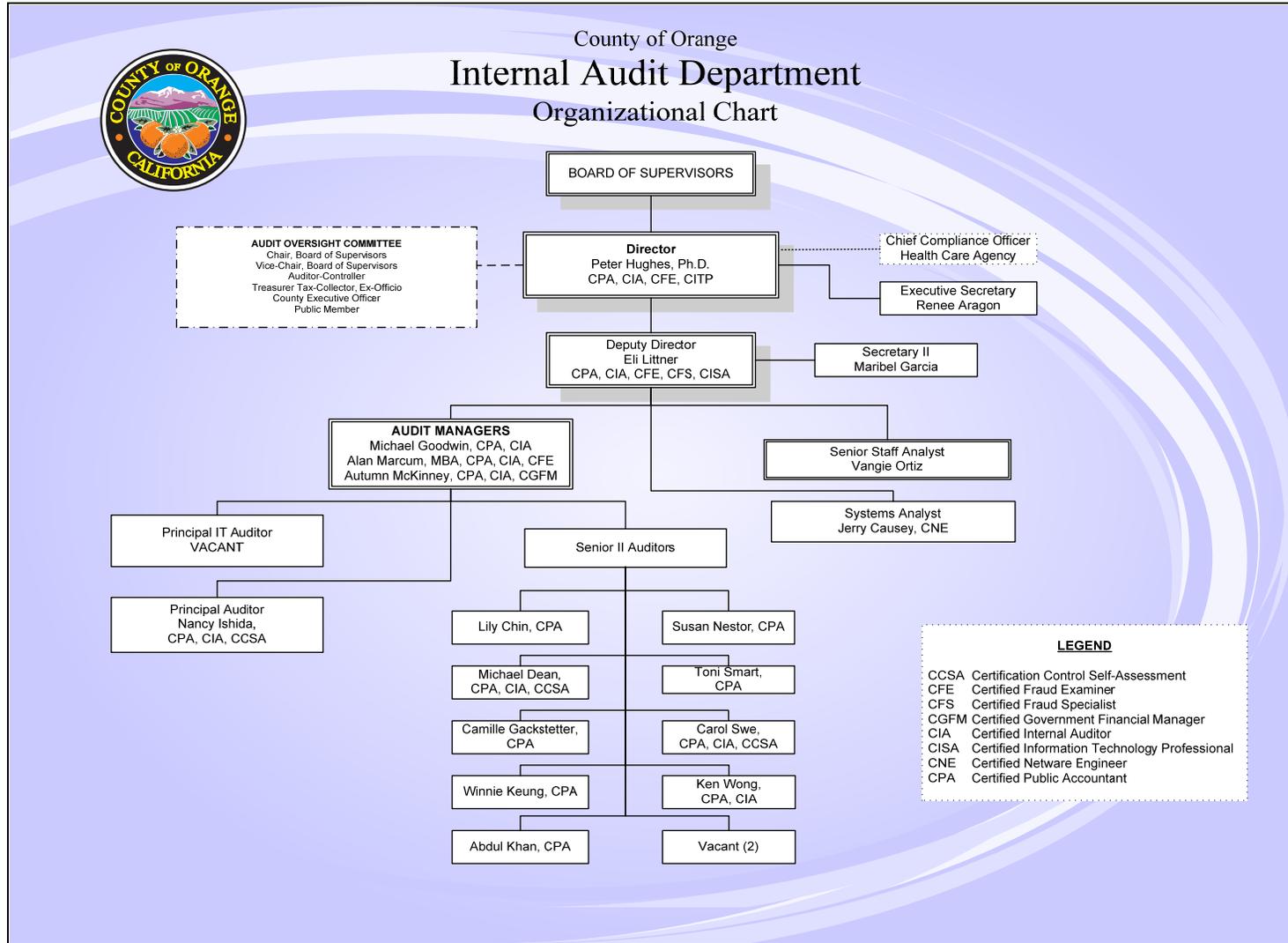
1	Health Care Agency	200
2	Clerk of the Board	200
3	RDMD	200
4	County Executive Office	200
5	Housing and Community Services	200
6	Human Resources Department	200
7	Social Services Agency	200
	Subtotal	1,400

CONTROL RELATED & OTHER ASSIGNMENTS

1	Annual Risk Assessment - Audit Plan	400
2	Cash Losses	100
3	Fraud Hotline	120
4	External Audit Reporting	300
5	Technical Assistance to Other Dept/Agencies	200
6	HIPAA Administration	100
7	Reports for Board, AOC, EA Meetings	500
	Subtotal	1,720
	Grand Total	18,500



DEPARTMENTAL ORGANIZATION CHART





COUNTYWIDE RISK ASSESSMENT METHODOLOGY

Overview

The IAD performed a risk assessment for purposes of preparing the FY 06-07 Audit Plan. For the 2004 and 2005 Audit Plans, we conducted comprehensive, countywide risk assessments that included meetings with members of the Board of Supervisors, the County Executive Office, and Department/Agency Executive Management to obtain their input on risks affecting their respective departments; reviewing department/agency Business Plans, and obtaining department/agency input on our risk assessment worksheets. Our risk assessment also identified financial volume and activity for each department/agency by financial process (e.g. cash receipts and cash disbursements, accounts receivable, revolving funds, procurement, budgeting), and prior audit coverage to make our risk determination.

For our FY 06-07 Audit Plan, we utilized information obtained from our prior risk assessments, in addition to obtaining recent financial volume and activity and updating our *Schedule of Prior Audit Coverage*.

Below is a discussion of our methodology for each area:

Internal Control Reviews

Internal Control Reviews (ICRs) are performed for processes involving cash receipts, revenue recovery, accounts receivable, cash disbursements, revolving funds, purchasing/contract administration, trust /special department funds, payroll, and budgeting.

To determine risk ratings for these processes, we used the following criteria and relative weight factors in our assessment:

- Department/Agency Changes (20%): Included factors such as management and/or organizational changes, significant increases/decreases in staffing and workloads, new/eliminated programs, and significant changes in laws/regulations.
- Operating Environment (20%): Included factors related to the department's operating environment such as public image, laws/regulations, safety and environmental issues, sensitivity to economic factors, pending litigation, and business continuity.
- Last Audit Performed (10%): Identified all IAD internal control reviews and mandated audits performed on the above processes since 1996.
- Financial Activity/Volume (50%): Obtained a listing of all County funds and the controlling department/agency for each fund. From CAPS, we compiled FY 04-05 financial information (dollar volume, number and nature of transactions) for each process and for each controlling department.

Using the above criteria, each department/agency process was rated on a scale of 1 to 10 (10 being highest risk and 1 lowest risk) for each of the above weight factors. An overall risk score was then calculated showing areas of High (9 - 10), Moderate (4 - 8), and Low (1 -3) risk. The overall risk scores are shown on page A-1 of the attached risk assessment schedules, and a *Schedule of Prior Audit Coverage* since 1996 is shown on page A-2 of the attachment.



Information Technology Inventory and Assessment

We prepared a key system inventory based on information we received from each department as part of our annual survey. The departments provide information only for those systems they identified as critical or key to carrying out the mission of their respective department. Examples of applications/systems not included in the inventory are: utilities (such as anti-virus, email, backup, and Microsoft operating system and office applications), terminal emulators (allows access to a mainframe computer via a personal computer), and systems of a limited/administrative nature (such as form generation, record retention, or telephone directories).

We rated each key system based upon the six relative weight factors below:

- **Importance & Impact (30%)**: The importance and impact of the system to the County and department's mission. Systems having a countywide impact were rated high in this category.
- **Complexity (20%)**: The complexity of the system taking into consideration the number of interfaces, the number of users and transactions, the nature of the database, and the nature of the calculations made by the system.
- **Nature of Information (15%)**: The nature of the information controlled by the system such as financial, operational, or support. Systems controlling financial assets or data were rated high in this category.
- **Sensitivity of Information (15%)**: The confidentiality of the information controlled by the system. Systems controlling HIPAA regulated information or personal information were rated high in this category.
- **Maturity (10%)**: The length of time since the system was implemented or since significant upgrades occurred.
- **Last Audit Performed (10%)**: The number of years since the last audit.

Each system was rated on a scale of 1 to 5 (5 being highest risk and 1 being lowest risk) for each of the weighted factors. Then, an overall score was calculated and the system was ranked as high (400 or above), moderate (251 – 399), or low (below 250). The overall risk scores and ratings are shown on page A-3 thru A-7 of the attached risk assessment schedules.

Risk Assessment Evaluation Methodology

We have studied the history of ten years of audit reports and audit findings. We have reviewed the agencies' annual business plans and have concluded that the departments and agencies have dedicated and control conscious managers overseeing their main business processes. In the audit reports issued, we noted that less than 10% of the findings are "significant issues" and less than 1% of the findings are "material." We have audited many of the business cycles and activities that we identified initially in our risk assessment process as having a Moderate to High inherent internal control risk, including such areas as budgeting, revenue collections, cash receipts and disbursements, revolving funds, trust funds/special dept. funds, accounts receivables, contract administration and procurement.

The Internal Audit Department now has a historical basis for assessing the competence of management and the rigor of their oversight of internal controls and expenditures. We have concluded that the control environment is positive and effective and helps offset the inherent



internal control risks. The established control process counterbalance the inherent internal control risks associated with many of the County's business processes.

One contributing factor in the improvement of control awareness is a direct result of the Control Self Assessment workshops conducted in 19 of the 23 County departments and agencies over the past five years. Internal controls are discussed thoroughly in these workshops. In addition, we have also conducted several Internal Control Workshops attended by County employees. We also have Control Training Tools on our Web site and County employees can access this training at any time. In addition, the County established and maintains annual business and budget plans and strategic planning. Recently the County established annual performance goals and achievement measures. These enhancements also contribute to management's understanding of the importance of internal controls and their focus on sound business practices.

In our opinion, we can now assert that the County has demonstrated an increasing awareness of internal controls and our audit results have verified this achievement. Moreover, we can also assert that the County no longer has business processes that have High levels of control risk in our risk assessment. At this point in time, we are moving toward developing an audit rotation cycle for the County's business processes.

SEE ATTACHMENT - RISK ASSESSMENT SCHEDULES

