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AUDITOR-CONTROLLER

**AUDITOR-CONTROLLER  
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March 13, 2007

TO: Members of the Audit Oversight Committee

SUBJECT: Auditor-Controller Internal Audit Unit

Attached for your consideration is a document entitled "Purpose and General Operating Procedures of the Auditor-Controller Internal Audit Unit." The document outlines the procedures for a proposed Internal Audit Unit operating within the Auditor-Controller Office that would be established to perform the mandated audit work required of my office as County Auditor. This proposal, of course, is subject to funding and approval of the Board of Supervisors during the annual budget process. It is being presented to you as an information item and is listed on the Audit Oversight Committee Agenda of the March 15, 2007 meeting as Item Number 4.

David E. Sundstrom  
Auditor-Controller

DES:lr  
Attachments

cc: Supervisor Bill Campbell, Third District  
Supervisor Pat Bates, Fifth District  
First Supervisorial District  
Jim Godsey, Partner, Macias, Gini & O'Connell  
Ann Fletcher, Deputy County Counsel  
Rob Richardson, Assistant to the CEO  
Robert Franz, Chief Financial Officer  
Peter Hughes, Director, Internal Audit Department  
Orange County Grand Jury

## ITEM 4, AOC Meeting of March 15, 2007

### Purpose and General Operating Procedures of the Auditor-Controller Internal Audit Unit

#### Purpose of Auditor-Controller Internal Audit Unit

- A. To perform the legally required audits of the auditor controller (see matrix, Attachment A) for a discussion of the mandates. The specific mandates of the Auditor-Controller are:
  - 1. Quarterly Cash Reviews of the County Treasury
  - 2. Annual Audit of the Treasury
  - 3. Audits of Special Districts
  - 4. The Biennial Audit of Probation
  - 5. Cash Loss Investigations
  
- B. To manage the general audit mandates that are required in performing the Auditor-Controller's responsibilities as the County's Chief Accounting Officer.
  - 1. Monitor the all internal and external audits to assist in determining the adequacy of departmental and countywide internal controls.
  - 2. Review internal and external audits to determine the adequacy and effectiveness of accounting policies.
  - 3. Initiate and perform internal audits that may be required to supplement (not supplant) the activities of the Internal Audit Department. Some of these audits may be initiated to immediately address concerns in county departments and agencies that are identified by central office accounting personnel.
  - 4. Perform any internal audits that are specifically requested by the Board of Supervisors to be performed by the Auditor-Controller.
  - 5. Act as a liaison between the Internal Audit Department and the Office of the Auditor-Controller to share specific risk information.
  - 6. Monitor and test the Auditor-Controller's departmental risk assessment and risk mitigation program.

#### Procedures

- 1. Audits will be submitted to the Audit Oversight Committee for review and discussion.
- 2. Internal Audit Unit will be functionally independent of all accounting units in the Auditor-Controller's Office (see organizational chart, Attachment B). Assignments will be controlled to ensure independence. The Auditor-Controller will not review internal audit reports until they are finalized.
- 3. Internal Audits will be conducted under the Professional Standards for Internal Auditing as promulgated by the Institute of Internal Auditors and/or the United States Government Auditing Standards as promulgated by the Government Accountability Office.
- 4. A peer review will be conducted on a three year cycle. The results will be submitted to the Audit Oversight Committee for review.

## Attachment A

### 1.0 Auditor-Controller Mandates

#### 1.1 Quarterly Cash Reviews of the County Treasury

Code Reference	Mandate	Board Resolution	
		#	Text
Government Code §26920 (a)	At least once in each quarter, the county auditor shall perform, or cause to be performed, a review of the treasurer's statement of assets in the county treasury. Each county shall fund and allocate the cost of the review in accordance with that county's established budgetary practice. The auditor's review shall be accomplished in accordance with the appropriate professional standards, as determined by the county auditor. The treasurer shall prepare a statement showing the amount and type of assets in the county treasury as of the date of the review.	None	Not Applicable

#### 1.2 Annual Audits of the Treasury

Government Code §26920 (b)	The auditor shall, at least annually, perform or cause to be performed an audit of the assets in the county treasury and express an opinion whether the treasurer's statement of assets is presented fairly and in accordance with generally accepted accounting principles. The audit report shall be addressed to the board of supervisors. The review required by subdivision (a) need not be performed for the period when an audit is conducted in accordance with this subdivision.	None	Not Applicable
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#### 1.3 Audits of Special Districts

Government Code §26909	The county auditor shall either make or contract with a certified public accountant or public accountant to make an annual audit of the accounts and records of every special purpose district within the county for which an audit by a certified public accountant or public accountant is not otherwise provided.		
Government Code §26910	The auditor may at any reasonable time and place examine the books and records of any special purpose assessing or taxing district located wholly in the county.		

#### 1.4 Biennial Audit of Probation

Code Reference	Mandate	Board Resolution	
		#	Text
Health and Welfare Code §275	<p>“(a) For the purpose of handling the reimbursement and other payments provided for in this chapter, the probation officer or other county officer designated by the board of supervisors of the county shall keep suitable books and accounts and shall give and keep suitable receipts and vouchers.</p> <p>(b) The auditor of the county shall audit these books and accounts annually, or at least biennially if so ordered by the board of supervisors upon the recommendation of the county auditor, on a fiscal year basis ending June 30 and shall make a report thereon to the judge of the court and to the supervisors of the county prior to the 31st day of the next succeeding month of January. This subdivision shall become inoperative on July 1, 1993, and shall remain inoperative until July 1, 1994, on which date this section shall become operative.”</p>	None	Not Applicable

#### 1.5 Cash Loss Investigations

Government Code §29390	<p>“The board of supervisors may, by a resolution incorporating such limitations and safeguards as may be deemed in the best interests of the county, provide that county officers and employees who are responsible for receiving and paying out money may be relieved of shortages in their accounts, where there is no proof of fraud or gross negligence in connection with the shortage and where the loss is not covered by insurance. If the board of supervisors after an investigation and report by the county auditor approves the coverage of such shortage, it shall be entered in its minutes and shall be a charge against the general fund of the county.”</p>	83-354	“. . .the Board hereby provides that an application to have a shortage not exceeding \$100 in County funds replenished shall be made with the Auditor-Controller instead of with the Board and authorizes the Auditor-Controller to perform the functions of the Board to replenish the shortage.”
		88-767	Per Resolution 05-003, “authorized an increase from \$100 to \$300 in the dollar limit for the Auditor-Controller to replenish cash shortages.”
		05-003	“The Board does hereby rescind Board Resolution No. 88-767 and amend Resolution 83-354 to authorize the Auditor-Controller to replenish cans losses up to \$2,500 where there is no proof of fraud or gross negligence in connection with the shortage, where the loss is not covered by insurance; and after appropriate review by the Auditor-Controller and the Internal Audit Department of such shortage.”

## 2.0 Board Directed Audits

### 2.1 Biennial Audits of County Officers

Code Reference	Mandate	Board Resolution	
		#	Text
Government Code §25250	<p>“At least biennially the board of supervisors shall examine and audit, or cause to be audited, the financial accounts and records of all officers having responsibility for the care, management, collection, or disbursement of money belonging to the county or money received or disbursed by them under authority of law. The audit shall encompass the immediately preceding two-year period, or any portion thereof not included in a prior audit.”</p> <p>“In connection with the requirements of this section and Section §25253, the board of supervisors may employ the services of an independent certified public accountant or licensed public accountant to perform an examination of the financial statements in accordance with generally accepted auditing standards.”</p>	95-271	<p>1. “Establish an Internal Audit Unit independent from the Auditor-Controller reporting directly to the Board of Supervisors to perform the biennial audits of County Officers required by Government Code Section 25250.</p> <p>2. Authorize the Internal Audit Unit to perform the Auditor-Controller’s legally required audits, <b>if requested by the Auditor-Controller.</b>”</p> <p>Note: Because the CAFR satisfies the requirement of Government Code §25250, any additional audit work performed under this section is discretionary at the Board’s direction.</p>

### 2.2 Annual CAFR Audit

§25253	<p>“Annually the board shall cause to be prepared and published a statistical report showing in compendious form all the financial transactions of the county for the last fiscal year, exhibiting separately the receipts and expenditures by or on account of all courts and each office, board, commission, institution, and departments, and classifying the principal items of income and expenditure so as to show the financial transactions and the financial condition of the county.”</p>		<p>Note: The annual audit has performed by a contracted independent CPA since 1978.</p>
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### 2.3 Tax Redemption Officer

Revenue and Tax- ation Code §4108.5	<p>“(a) The records and accounts of the tax collector pursuant to this part shall be audited at least once each three years.”</p>	None	Not Applicable
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### 3.0 General Mandates

#### 3.1 Petty Cash

Code Reference	Mandate	Board Resolution	
		#	Text
Government Code §29321.1.	“The board of supervisors may, by ordinance or resolution, authorize the county auditor to perform the functions of the board in establishing, increasing, reducing, or discontinuing any of the revolving funds provided for in this article. In the event that the board authorizes the county auditor to perform such functions of the board, the county auditor shall (a) be subject to the same requirements and limitations otherwise prescribed for the board in this article, (b) in lieu of acting by resolution, act by signed statement having the same content otherwise prescribed in this article for resolutions, and (c) render a written report to the board at the end of each fiscal year identifying the revolving funds in existence during the fiscal year, the amount of such fund, and the officer using the fund.”	85-1684	“Pursuant to Government Code Section 29321.1, the Auditor-Controller, in consultation with the Purchasing Agent, and subject to provisions herein, is authorized to perform the functions of the Board in establishing, increasing, reducing, or discontinuing any of the revolving funds provide for in Article 2 of Chapter 2 of Division 3 of Title 3 of the Government Code.”
N/A	Note: There is no law that specifies the audit of revolving funds. However, audits by the Auditor-Controller would be necessary to determine the need for “increasing, reducing, or discontinuing any of the revolving funds” noted in Government Code §29321.1, above.	92-1008	“The Auditor-Controller and General Services Agency are directed to periodically review Agency/department petty cash functions for cost effective- ness, internal controls, and overall appropriateness, and are authorized to lower the individual purchase limit for agencies/departments found to be in non-compliance with one or more of these factors.”

### 3.2 Audits Required of the Auditor-Controller by Virtue of Office as the County's Chief Accounting Officer

Code Reference	Mandate	Board Resolution	
		#	Text
Government Code §26881	<p>"The county auditor, or in counties that have the office of controller, the auditor-controller shall be the chief accounting officer of the county. Upon order of the board of supervisors, the auditor or auditor-controller shall prescribe, and shall exercise a general supervision, including the ability to review departmental and countywide internal controls, over the accounting forms and the method of keeping the accounts of all offices, departments and institutions under the control of the board of supervisors and of all districts whose funds are kept in the county treasury."</p>	82-162	<p>"II. That the County Auditor shall be ex-officio County Controller and Chief Accounting Officer of the County.                      "IV. That the County Auditor-Controller as Chief Accounting Officer of the County shall:                      "A. Prescribe and exercise a general supervision . . .                      "B. Maintain such accounts and statistics. . .                      "C. Audit the accounts, records, accounting procedures and operating practices. . ."</p>
		85-337	<p>"Whereas, periodic reviews of the systems of internal accounting control and administrative control are the responsibility of the Auditor-Controller. . ."</p>

Code Reference	Mandate	Board Resolution	
		#	Text
<p>Note: County Counsel has opined that “pursuant to sections 26881, 26883, and 26915, the Board of Supervisors may provide internal auditing responsibilities to the Auditor, Internal Audit or a certified public accounting firm.”<sup>1</sup> They also conclude that language contained in 95-275<sup>2</sup> “demonstrated the Board’s intent that internal audits be performed by the Internal Audit Department.”</p> <p>Several facts and points of law challenge counsel’s conclusion:</p> <p>1. Resolution 95-275 recognized two types of internal audits, “the biennial audits of County Officers required by Government Code §25250.” and “Auditor-Controller’s legally required audits.” The other mandates previously prescribed by the Board in Resolutions 92-1008, 82-162, or 85-337 were not noted. As required by the resolution, all the internal audit positions in the Auditor-Controller’s Office were transferred, including the positions used to perform the Auditor-Controller’s mandates. As part of the agreement, the Auditor-Controller requested that the Internal Audit Unit perform the Auditor-Controller’s legally mandated audits.</p> <p>2. The Auditor-Controller’s “ability to review departmental and countywide internal controls” is critical to the proper performance of his other duties contained in Government Code §26881 and delegated by the Board of Supervisors in Resolution 82-162. It is not appropriate to parse these responsibilities. In order to perform general supervision over accounting, the Auditor-Controller requires methods to directly assess departmental and countywide internal controls.</p> <p>3. The provisions of the Orange County specific legislation, Government Code §26915, appear to be inoperative. This section was cited by counsel in forming his opinion that “any requirement an audit be performed by the county auditor may, at the election of the board of supervisors, also be performed by a county employee or officer who meets both of the following qualifications: . . . *(2) the employee of officer is independent in accordance with Rule 101 of the American Institute of Certified Public Accountant’s Code of Professional conduct.” This law appears to be inoperative. The AICPA released the following interpretation of Rule 101: “Independence shall be considered impaired if: . . . during the period of the . . . professional engagement . . . a professional employee of the firm . . . was simultaneously associated with the client as an . . . employee or in any capacity equivalent to that that of a member of management.” The California Senate recently recognized that internal auditors can not meet AICPA independence standards. According to Senate floor analysis for SB 1196, no county employee can meet that standard “because the county board of supervisors is both the client and the employer.”<sup>3</sup></p> <p>4. Government Code §26915 further specifies “Nothing in this section is intended to preclude a county auditor from performing his statutorily prescribed duties.” Reviewing internal controls (through internal auditing) is a statutorily prescribed duty upon order of the Board of Supervisors. That order was given in 1982 by Resolution 82-162 and has not yet been superseded.</p>			

#### 4.0 Other Audits

##### 4.1 Treasury Oversight Compliance

Government Code §27134	“The county treasury oversight committee shall cause an annual audit to be conducted to determine the county treasury’s compliance with this article. The audit may include issues relating to the structure of the investment portfolio and risk.”		Not Applicable
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<sup>1</sup> County Counsel Opinion No. 2006-016(a)

<sup>2</sup> Board of Supervisor’s Resolution 95-271, dated April 25, 1995.

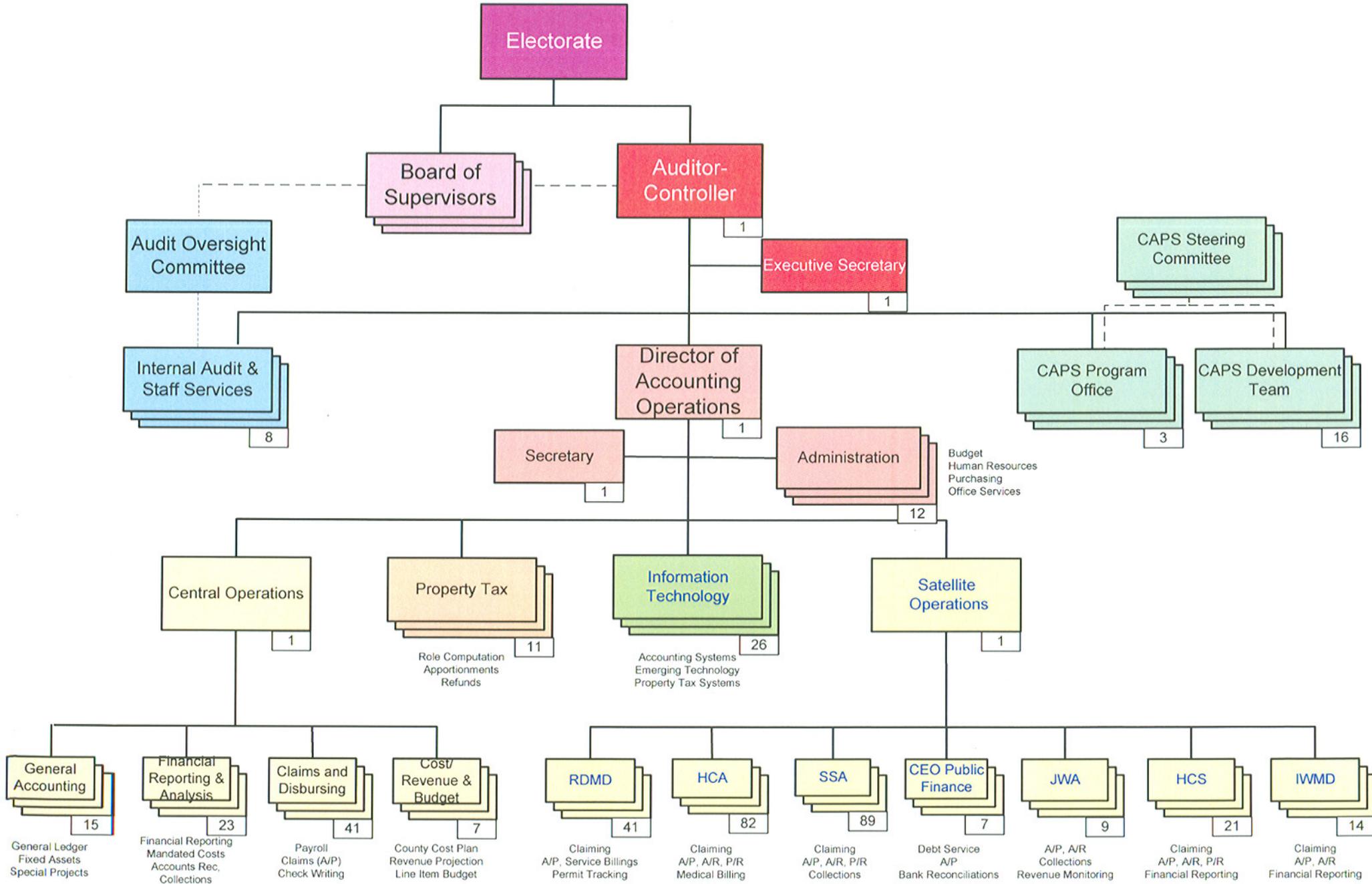
<sup>3</sup> Senate Bill 1196, Committee on Local Government Local Omnibus Act of 2006, floor analysis, 8/07/06. This bill removed an inoperative requirement that audits of the treasury be performed in accordance with AICPA standards required by Government Code §26920. The standards do not allow for employees to be considered independent in accordance with Rule 101. This bill gave the county auditor the authority to determine the appropriate standards to be employed for the treasury audits.

# Orange County Auditor-Controller



# Attachment B

## Proposed Reorganization



Total Staff Count: 431