



2004 INTERNAL AUDITOR'S REPORT TO THE BOARD OF SUPERVISORS

Orange County Board of Supervisors



**Supervisor
Lou Correa
1st District**



**Supervisor
James W. Silva
2nd District**



**Chairman
Bill Campbell
3rd District**



**Supervisor
Chris Norby
4th District**



**Vice Chairman
Thomas W. Wilson
5th District**



*Integrity
Objectivity
Independence*

COUNTY OF ORANGE INTERNAL AUDIT DEPARTMENT

OFFICE OF THE DIRECTOR

PETER HUGHES
Ph.D., MBA, CPA, CIA, CFE, CITP
DIRECTOR

MAILING ADDRESS:
400 CIVIC CENTER DRIVE WEST
BUILDING 12, ROOM 232
SANTA ANA, CA 92701

TELEPHONE: (714) 834-5475
FAX: (714) 834-2890
EMAIL: peter.hughes@ocgov.com
WEBSITE: www.ocgov.com/audit/

March 2005

**Honorable Board of Supervisors
County of Orange
Santa Ana, CA 92701**

Dear Honorable Supervisors:

I am proud to present our 2004 Internal Auditor's Report. Over the course of the calendar year, we completed nearly 100 projects in 14 different audit categories. We provided audit services to 18 of the County's 21 agencies and departments. One of our department's highlights was receiving the highest possible rating during a Peer Review from a nationally recognized CPA firm for our performance and professionalism.

It has been my pleasure to serve you.

Sincerely,

**Peter Hughes, Ph.D., MBA, CPA
Director, Internal Audit Department**

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

In this Issue:

- Page 2 A Message from Orange County's Director of Internal Audit
- Page 4 2004 Detailed Achievements
- Page 8 The Orange County Internal Audit Department



**A MESSAGE FROM ORANGE
COUNTY'S DIRECTOR OF INTERNAL
AUDIT**

**Internal Audit
Director**

**Peter Hughes, Ph.D., MBA,
CPA, CIA, CFE, CITP**

Find us at:

www.ocgov.com/audit

E-mail your comments to:

peter.hughes@ocgov.com

Transparency

The Internal Audit function reports directly to the Board of Supervisors on a monthly basis in a public forum. Additionally, the Internal Audit function reports quarterly to the Board appointed advisory group known as the Audit Oversight Committee.

IAD Mission Statement

The mission of the Internal Audit Department (IAD) is to provide reliable, independent and objective evaluations of business processes to the Board of Supervisors and County management in order to assist them in making business and financial decisions, and to protect and safeguard the County's resources and assets.

Greetings,

*We had a **very successful and productive year**, finishing nearly **100 projects**. In addition, we reached our highest level of coverage in the past six years having performed audits or provided services to **18 out of the County's 21 agencies and departments**. This level of coverage represents an impressive presence in the County's \$5 billion plus business operations, which employs over 17,000 full-time employees to provide critical services to 34 cities and more than 3.5 million residents.*

*As we experienced in past years, we received the **full support and cooperation of all levels of County personnel and management** in answering our questions, facilitating our audits and addressing our audit findings and concerns.*

*We are also proud to have received the **highest ratings possible** for quality and professionalism from two nationally recognized accounting firms for each of the **three Peer Reviews** conducted of our department during the past five years. Moreover, the last peer reviewer asked to **use our department as a benchmarking model** for their clients.*

*During the past two years, our **duties have expanded** and now include providing audit assistance to the newly established Health Care Agency Compliance Office and the County's Health Insurance Portability and Accountability Act (HIPAA) Office. In addition, Internal Audit now plays the lead role in coordinating the many County Departmental and Agency "Fraud Hotlines". Lastly, the department has also seen its role elevated as the County's lead in monitoring and reporting upon all external Federal and State audits of County operations.*

Throughout the year, we spent our audit resources reviewing and assessing the adequacy of County internal controls, verifying the accuracy and completeness of financial reports, evaluating the effectiveness of business processes, and assessing the degree management complies with applicable rules and regulations.

*We are committed to conducting timely Follow-Up Audits on all audit findings. **We track and monitor each finding until corrective actions are implemented.** We completed **15** Follow-Up Audits this year and found management either had implemented corrective action or was in the process of addressing our findings.*

All financial and mandated audits were completed within the mandated time-frame. 100% of the overall 2004 Audit Plan was completed.

Again, it is my pleasure to serve you. Listed below is Internal Audit's trusted, professional staff.

INTERNAL AUDIT DEPARTMENT PROFESSIONAL STAFF

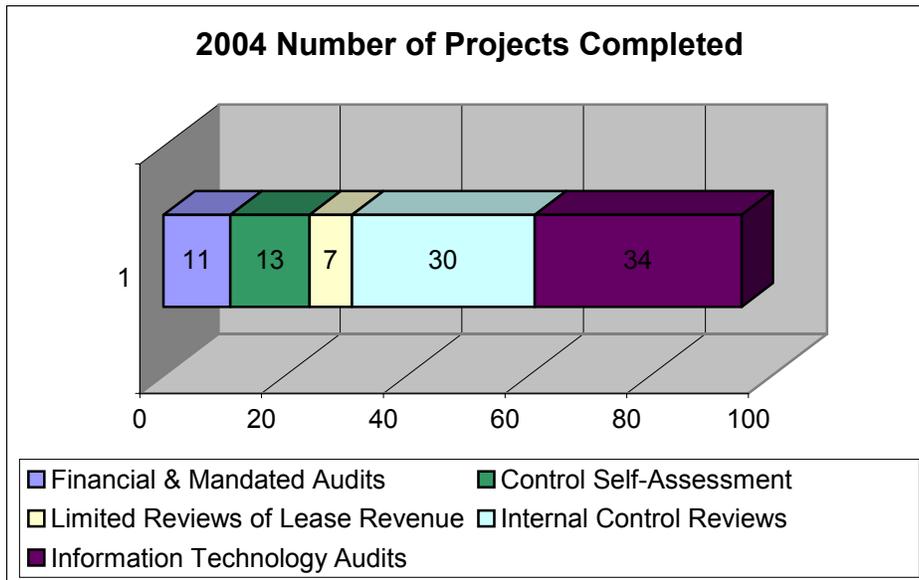
- Director, **Dr. Peter Hughes**, Ph.D., MBA, **CPA**, CIA, CFE, CITP
- Deputy Director, **Eli Littner**, **CPA**, CIA, CFE, CFS, CISA
- Audit Manager, **Michael J. Goodwin**, **CPA**, CIA
- Audit Manager, **Alan Marcum**, MBA, **CPA**, CIA, CFE
- Audit Manager, **Autumn McKinney**, **CPA**, CIA, CGFM
- Principal Auditor, **Nancy N. Ishida**, **CPA**, CIA, CCSA
- Principal Auditor, **Scott M. Suzuki**, **CPA**, CISA, CIA, CFS
- Senior Auditor, **Lily Chin**, **CPA**
- Senior Auditor, **Michael Dean**, **CIA**, CCSA
- Senior Auditor, **Camille A. Gackstetter**, **CPA**
- Senior Auditor, **Winnie Y. Keung**, **CPA**
- Senior Auditor, **Dan Melton**, **CPA**, M-Tax
- Senior Auditor, **Toni M. Smart**, **CPA**
- Senior Auditor, **Carol L. Swe**, **CPA**, CIA, CCSA
- Senior Auditor, **Kenneth Wong**, **CPA**, CIA

LEGEND	
CCSA	Certification Control Self-Assessment
CFE	Certified Fraud Examiner
CFS	Certified Fraud Specialist
CGFM	Certified Government Financial Manager
CIA	Certified Internal Auditor
CISA	Certified Information Systems Auditor
CITP	Certified Information Tech. Professional
CPA	Certified Public Accountant
MTAX	Master of Taxation

INTERNAL AUDIT DEPARTMENT ADMINISTRATIVE STAFF

- Senior Staff Analyst, **Vangie Ortiz**
- Systems Analyst, **Jerry Causey**
- Executive Secretary, **Renee Aragon**
- Secretary II, **Maribel Garcia**

2004 Detailed Achievements



Financial & Mandated Audits - We completed 11 audits in this category.

We audit financial reports for accuracy and completeness. We also conduct reviews to determine managements' compliance with rules and regulations. We completed all financial and mandated audits listed in the 2004 Audit Plan on schedule:

- Quarterly Treasury Fund Audits
- Quarterly Treasury Compliance Reviews
- Annual Treasury Compliance Audit
- District Attorney Auto Insurance Fraud Grant Audit
- District Attorney Workers' Compensation Fraud Grant Audit
- District Attorney Spousal Abuser Prosecution Grant Audit

We followed-up on all audit recommendations during the subsequent audit.

Control Self-Assessment (CSA) - We completed 12 workshops in this category.

In a CSA, we facilitate workshops in which management and staff target inefficiencies and obstacles in their business operations, as well as identify corrective remedies. We scheduled CSA workshops in our 2004 Audit Plan for the District Attorney, HCA/Contracts, and the Housing and Community Services Department (HCSD) Office on Aging. We conducted the following workshops:

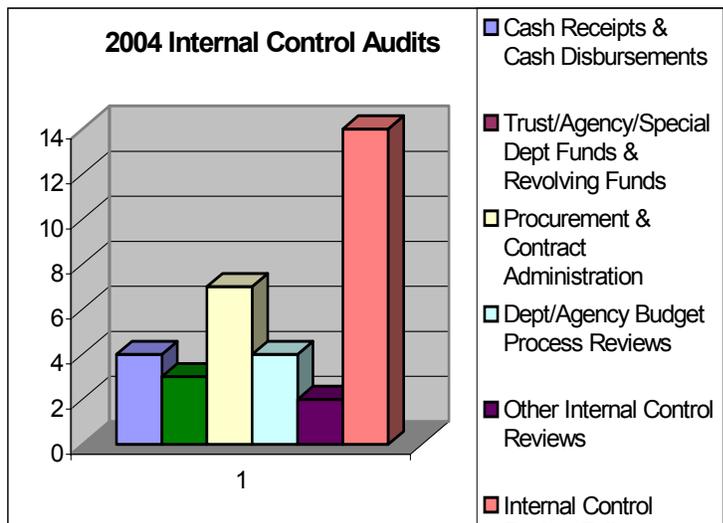
- **District Attorney** (two workshops)
- **Health Care Agency** (two workshops)
- **HCS D** (two workshops for Special Programs & two for Office on Aging)
- **Register of Voters** (four workshops)

Limited Reviews of Lease Revenue - We completed 7 audits in this category.

In these reviews, we audit to determine if all revenues due the County are properly calculated, recorded, and received. These reviews are requested by the Resource Development and Management Department (RDMD) and John Wayne Airport (JWA) and are performed on a fiscal year basis. By December 31, 2004, we will have completed the five limited reviews of lease revenue listed on the 2004 Audit Plan plus two mid-year reviews for a total of seven.

Internal Control Reviews – We reviewed 30 audit areas in this category. Additionally, in **2004, 5 reviews were started and field work was completed and finalized in 2005.** In these reviews, we determine the adequacy and integrity of internal controls for selected business processes. Most of our audits review multiple areas, issues, and activities. For example, one audit report may address an audit of cash receipts, cash disbursements, as well as selected trust funds. We performed internal control reviews in the following areas during 2004:

- 1) Cash Receipts and Cash Disbursements - **4 completed.** We performed a cash receipts review of the **Health Care Agency** and cash disbursements reviews of the **Auditor-Controller**, the **Resources Development and Management Department**, and the **Health Care Agency**. In late 2004, we started a cash disbursements review of the Orange County Development Agency, administered under Housing and Community Services. This review will continue into 2005.



- 2) Trust/Agency/Special Department Funds and Revolving Funds – **3 completed.** We performed these reviews in the **Auditor-Controller’s** office, the **Resources Development and Management Department**, and the **Health Care Agency**.
- 3) Procurement and Contract Administration - **7 completed.** We completed a review of the County’s purchasing cards at selected departments. The selected departments were: the **Assessor, CEO/Purchasing, Housing and Community Services, Integrated Waste Management (IWM), Public Library, and Public Defender**. We also evaluated controls over payments made for contracted services at the **Housing and Community Services’ Office on Aging and Special Programs** Divisions. In late 2004, we agreed to participate in the County-wide Accounting and Personnel System (CAPS) Integrated Procurement and Payables Processing Project (IP3) pilot project at IWM. See comment below under IT Audits.
- 4) Department/Agency Budget Process Reviews - **4 started.** We performed these reviews in the **Health Care Agency**, the **Public Defender**, the **Sheriff-Coroner**, and the **Social Services Agency**, and they will be completed in 2005.
- 5) Other Internal Control Reviews - **2 completed.** We performed reviews of other areas based upon requests or input we received. One area was the **Auditor-Controller’s Property Tax Unit** where we assessed the controls in the Extended Tax Roll process. Another review was at the **Resource Development and Management Department** where we evaluated the process for establishing billing rates and overhead for chilled water, steam, and purchased utilities. An audit of the Auditor-Controller Collections/Accounts Receivable unit was started in 2004 and will be completed in 2005.

- 6) *Follow-Up Audits for ICR's* - **14 Follow-Up Audits completed**. We track, monitor, and conduct site reviews for all Follow-Up Audit recommendations until satisfactory corrective action is implemented by the department. We conducted 14 Follow-Up Audits in the following departments:
- 2 - **County Counsel**
 - 2 - **County Executive Office**
 - 3 - **Health Care Agency**
 - 3 - **Sheriff-Coroner**
 - 4 - One for each: **Grand Jury; District Attorney; Planning & Development Services; and Human Resources/Employee Benefits**

Information Technology (IT) Audits - We completed 34 projects in this category. An additional three projects were started and will be completed in 2005.

In these audits, we review controls in a variety of information technology areas including general IT controls, application controls, and systems development. We performed work in the following IT audit areas during 2004:

- 1) *IT Governance*: On February 18, 2004, we issued **an advisory memo** to the County Executive Office regarding our observations on the opportunity for and importance of adopting a County IT Governance model.
- 2) *Assistance on an IT Component of a Financial Audit*: **2 projects completed** in this area. We completed a general computer controls questionnaire at the Treasurer-Tax Collector as part of the December 31, 2003 Treasury Funds Audit. We also conducted a Follow-Up Review on IT related findings we identified during the prior year Treasury Fund Audit.
- 3) *IT Self-Assessment Questionnaire*: **1 project started** in this area. During 2003, we developed an information technology self-assessment questionnaire (based upon the COBIT model from the Information Systems Audit and Control Association) for County departments' use. During 2004, HCA volunteered to complete this self-assessment questionnaire as a pilot. Also in 2004, we validated a sample of HCA's completed questionnaire and plan to issue a draft report in 2005.
- 4) *Application Audit*: **1 project started** in this area. In late 2004, we began a review of the Auditor-Controller's collections and accounts receivable application (CUBS) in conjunction with an Internal Control Review of the Auditor-Controller's collections process. Our review will be carried over and completed in 2005. Additionally, we developed a new audit program for application audits.
- 5) *System Implementation Review*: **1 project started** in this area. In late 2004, we initiated our involvement in the CAPS IP3 pilot project at IWM. This project includes members of IWM, the Auditor-Controller, and CEO/Information Technology. The IP3 project will automate the routing of procurement and payable documents for review and approval, as well as make other important enhancements. We plan to review the automated and manual internal controls, as well as audit trails, associated with the IP3 process. The pilot is to be implemented in 2005. Our review will be performed in 2005.
- 6) *Follow-Up of IT Audit*: **1 Follow-Up Audit completed** for the Auditor-Controller's County Accounting and Personnel System (CAPS) Payroll Risk Assessment Audit.

- 7) Computer Assisted Audit Techniques (CAATs): **We completed 28 projects in this category.** We use a proprietary, state-of-the-art/best practice software product to help us analyze data for payroll and vendor payments (we are one of a few counties that use this great computer tool).

We have developed and routinely perform the following CAAT routines on a regular basis:

- Duplicate Vendor Payments: **We conducted 12 monthly computer routines** to identify potential duplicate vendor payments. Since the inception of this routine in May 2002, duplicate payments identified are \$220,691 and amounts recovered are \$199,572.
 - Duplicate Payments to Employees: **We conducted 10 monthly computer routines** to identify employees paid twice in the same pay period or fictitious employees. No unusual activity was noted for 2004.
 - Employee/Vendor Addresses: **We conducted this annual computer routine** to help identify employees buying goods or issuing contracts to themselves or a related vendor.
 - Working Retirees: **We conducted this annual computer routine** to identify retirees working beyond legislated or contracted hour maximums. We reviewed 236 extra-help retirees for FY 03-04 and identified one retiree that exceeded allowed thresholds. That is being resolved by Human Resources.
 - Investment Compliance: **We conducted 3 quarterly computer CAAT routines** to analyze the Treasurer's investment portfolio and determine diversification percentages to compare with government regulations.
 - Annual Risk Assessment: **We conducted several computer CAAT routines** to obtain financial information (transaction amounts and activity) that we utilize in the annual risk assessment. For example, we compile cash receipt activity by the department that processed the cash receipts rather than by the department/fund where the money was deposited (some departments process monies for other departments).
- 8) Countywide IT Inventory: **We updated a listing of over 130 key computer systems being used** in the County departments and utilized this listing as part of our Annual IT Risk Assessment. We obtained relevant information, such as the platform, operating system, type of data, source/support for the system, and interfaces thereby increasing our understanding of the departments' IT environment. In 2003, we prepared the first computer system inventory listing in recent County history.
- 9) Update to Accounting Manual No. S-1: On December 22, 2003 **we provided a proposed updated draft** of County Accounting Manual No. S-1 (Development of Financial Computer Systems) to the Auditor-Controller's Department which has since been adopted in early 2005.

POSITIVE FEED BACK ON AUDIT SERVICES

"I have learned a lot from the audit performed on our unit. Thanks."

"The auditors were very professional & helpful to accounting staff & provided recommendations that will enhance our trust fund monitoring & reconciliation process."

"The auditors & their management team are excellent partners. In addition to their extensive subject knowledge of accounting & business controls, they went out of their way during our recent audit to improve their knowledge of our business & offered sound advice for strengthening our operations."

"Your auditors were very professional in the conduct of the review. They were able to quickly grasp a very technical area to complete the review."

The Orange County Internal Audit Department

The **Internal Audit Department reports directly to the Board of Supervisors**. This reporting structure is unique as Orange County is the only county in the State of California with this reporting relationship. This increased visibility and the Board's continuing support allowed the County of Orange Internal Audit Department to become a **model audit department** within just six years of operation under the leadership of Dr. Peter Hughes and through the dedication of his very capable staff.

The Board also created the Audit Oversight Committee (AOC). The AOC is comprised of the Chairman and Vice

Chairman of the Board of Supervisors, the County Executive Officer, the Auditor-Controller, and a Public Member. The AOC reviews and approves the Annual Audit Plan. The **Internal Audit Department meets quarterly with the AOC and reports on the status of its work**.

Monthly Status Report to the Board

The Audit Director **makes monthly public presentations** to the Board on the audit activity. These public reports and presentations underscore the **Board's commitment to TRANSPARENCY in County Government**.



WHO AUDITS THE AUDITORS?

Other Auditors in a Peer Review.

Have you ever wondered who audits the Orange County Internal auditors? Government code and the audit profession require that auditors be audited at least every three years. This audit is called a Peer Review or Quality Assessment. A Peer Review assesses an audit department's adherence to professional audit standards. The Department was given **the best rating possible** by its Peer Reviewers for all **three reviews** in the past five years.

Contact us at:

400 W. Civic Center Drive Room 232, Santa Ana, California 92701-4521

714.834.5475 main line – 714.834.2880 fax

Visit us online: Go to www.ocgov.com/audit