

# Internal Audit Department

O R A N G E C O U N T Y  
6<sup>th</sup> Largest County in the USA

## SECOND FOLLOW-UP AUDIT OF TREASURY COST ALLOCATIONS TO POOL PARTICIPANTS

AS OF MARCH 20, 2013

Our Second Follow-Up Audit found that the Treasurer-Tax Collector and County Executive Office are in-process of implementing the six (6) recommendations remaining from our original audit containing thirteen (13) recommendations.

Previously, six (6) recommendations were implemented and one (1) was closed in our First Follow-Up audit report dated August 28, 2012.

During the original audit, the Treasurer-Tax Collector's allocated \$6.3 million of administrative costs to pool participants pertaining to investing, depositing, and handling of funds.

AUDIT No: 1219-B  
ORIGINAL AUDIT No: 2915

REPORT DATE: APRIL 16, 2013

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**Senior Audit Manager:** Alan Marcum, CPA, CIA  
**Audit Manager:** Kenneth Wong, CPA, CIA

### RISK BASED AUDITING

GAO & IIA Peer Review Compliant – 2001, 2004, 2007, 2010



American Institute of Certified Public Accountants Award to Dr. Peter Hughes as 2010 Outstanding CPA of the Year for Local Government

GRC (Government, Risk & Compliance) Group 2010 Award to IAD as MVP in Risk Management



2009 Association of Certified Fraud Examiners' Hubbard Award to Dr. Peter Hughes for the Most Outstanding Article of the Year – Ethics Pays



2008 Association of Local Government Auditors' Bronze Website Award



2005 Institute of Internal Auditors' Award to IAD for Recognition of Commitment to Professional Excellence, Quality, and Outreach



ORANGE COUNTY BOARD OF SUPERVISORS'  
**Internal Audit Department**

*GAO & IIA Peer Review Compliant - 2001, 2004, 2007, 2010*

*Providing Facts and Perspectives Countywide*

**RISK BASED AUDITING**

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Certified Information Technology Professional (CITP)

Certified Internal Auditor (CIA)

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**OC Fraud Hotline (714) 834-3608**



## Transmittal Letter



**Audit No. 1219-B April 16, 2013**

**TO:** Shari L. Freidenrich, CPA  
Treasurer-Tax Collector  
Robert J. Franz, Interim County Executive Officer

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

**SUBJECT:** Second Follow-Up Audit of Treasury Cost Allocations to Pool Participants, Original Audit No. 2915, Issued October 31, 2011

We have completed a Second Follow-Up Audit of Treasury Cost Allocations to Pool Participants. Our audit was limited to reviewing, as of March 20, 2013, actions taken to implement the **six (6) recommendations** remaining from our First Follow-Up Audit report dated August 28, 2012. We conducted this Second Follow-Up Audit in accordance with the *FY 12-13 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and the Board of Supervisors (BOS).

The results of our Second Follow-Up Audit are discussed in the **OC Internal Auditor's Report** following this transmittal letter. Our Second Follow-Up Audit found the Treasurer-Tax Collector and County Executive Office are in-process of implementing six (6) recommendations from our original audit containing thirteen (13) recommendations. Previously, six (6) recommendations were implemented and one (1) was closed. Because this is our Final Follow-Up Audit, the recommendations not fully implemented will be reported to the Audit Oversight Committee in our Quarterly Status Report.

Each month I submit an **Audit Status Report** to the BOS where I detail any material and significant audit findings released in reports during the prior month and the implementation status of audit recommendations as disclosed by our Follow-Up Audits. Accordingly, the results of this audit will be included in a future status report to the BOS.

Other recipients of this report are listed on the **OC Internal Auditor's Report** on page 6.

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Treasury Cost Allocations to Pool Participants  
Audit No. 1219-B*

As of March 20, 2013

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# OC Internal Auditor's Report



**Audit No. 1219-B**

**April 16, 2013**

TO: Shari L. Freidenrich, CPA, Treasurer-Tax Collector  
Robert J. Franz, Interim County Executive Officer

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

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

SUBJECT: Second Follow-Up Audit of Treasury Cost Allocations to Pool Participants, Original Audit No. 2915, Issued October 31, 2011

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## Scope of Review

We have completed a Second Follow-Up Audit of Treasury Cost Allocations to Pool Participants. Our audit was limited to reviewing, as of March 20, 2013, actions taken to implement six (6) recommendations remaining from our First Follow-Up Audit report dated August 28, 2012.

## Background

Our original audit evaluated the Treasurer-Tax Collector's internal controls over the calculation and charging of administrative costs to investment pool participants. Thirteen (13) recommendations were made to the Treasurer-Tax Collector and County Executive Office in the original audit to improve controls and processes. During the original audit period, the Treasurer-Tax Collector charged \$6.3 million of administrative costs to pool participants for services pertaining to investing, depositing, and handling of funds.

## Results

Our Second Follow-Up Audit indicated that the Treasurer-Tax Collector and County Executive Office are in-process of implementing six (6) recommendations. We believe the remaining six (6) recommendations are still appropriate and efforts should be made to fully implement them. The following is the implementation status of the thirteen (13) original recommendations:

### **1. Lapse of Oversight for the T-TC's Annual Cost Allocation Study** **(Critical Control Weakness)**

We recommend that the Treasurer-Tax Collector review and initial to authorize the annual cost allocation study.

**Current Status: Implemented (First Follow-Up Audit).** The Treasurer-Tax Collector's office completed cost allocation studies for Fiscal Years 2009/2010 and 2010/2011 in June 2012. The Treasurer-Tax Collector documented their review and authorization by signing each annual study. Since the two most recent completed annual cost allocation studies were reviewed and authorized by the Treasurer-Tax Collector, we consider this recommendation fully implemented.



## 2. Lapse of Oversight for the T-TC's Annual Cost Allocation Study (Critical Control Weakness)

We recommend that the Treasurer-Tax Collector submit the cost allocation study to the Treasury Oversight Committee for their review as required by the County's Investment Policy Statement.

Current Status: **Closed (First Follow-Up Audit).** The Treasurer-Tax Collector submitted and received approval from the Treasury Oversight Committee on October 26, 2011, for the 2006-2009 treasury administrative fees. On January 10, 2012, the Board of Supervisors approved the amended County Investment Policy Statement that removed the requirement for the Treasury Oversight Committee to review the administrative fees charged to pool participants. Since the County's Investment Policy Statement no longer requires the Treasury Oversight Committee to review the cost allocation study, we consider this recommendation closed.

## 3. Lapse of Oversight for the T-TC's Annual Cost Allocation Study (Critical Control Weakness)

We recommend that the Treasurer-Tax Collector and the Treasury Oversight Committee review the requirements of the County's Investment Policy Statement and clarify the nature and extent of the review and whether or not the Treasury Oversight Committee's approval is warranted.

Current Status: **Fully Implemented (First Follow-Up Audit).** On January 10, 2012, the Board of Supervisors approved the amended County Investment Policy Statement that removed the requirement for the Treasury Oversight Committee to review the administrative fees charged to pool participants. Since the County's Investment Policy Statement no longer requires the Treasury Oversight Committee to review the cost allocation study, we consider this recommendation implemented.

## 4. Incomplete Policies and Procedures (Critical Control Weakness)

We recommend that the Treasurer-Tax Collector develop, complete, or update policies and procedures to be followed for the annual cost allocation process. Documented policies and procedures should be reviewed and approved by the Treasurer-Tax Collector and management and current versions need to be readily available for reference by personnel responsible for the annual cost allocation process.

Current Status: **In-Process (Second Follow-Up Audit).** The Treasurer-Tax Collector issued a Request for Proposal, awarded a bid, and engaged the selected firm to review the methodology for the annual cost allocation study. The firm will perform a cost recovery fee and charge study. The study of the Treasurer-Tax Collector's 25 fees and charges includes the Treasury Administrative Fee, the cost for administering the investment funds for pool participants. The scope of services includes providing the Treasurer-Tax Collector with a methodology and a model for future calculation and update of fees. However, the Treasurer-Tax Collector has not yet updated the policies and procedures for annual cost allocations studies.

Planned Action: Once the cost recovery fee study is completed, the Treasurer-Tax Collector will evaluate the firm's recommendations, and the policies and procedures will be updated.



**5. Process to Determine the Amount of Effort Spent on Either Treasury or Tax Collection Activities Needs to be Improved (Significant Control Weakness)**

We recommend that the Treasurer-Tax Collector review the process used to establish the amount (percent) of effort spent on treasury and tax collection activities and determine if a more specific methodology would be more appropriate.

Current Status: **In-Process (Second Follow-Up Audit).** The Treasurer-Tax Collector issued a Request for Proposal, awarded a bid, and engaged a selected firm to review the methodology for the annual cost allocation study. The firm will perform a cost recovery fee and charge study. The study of the Treasurer-Tax Collector's 25 fees and charges includes the Treasury Administrative Fee, the cost for administering the investment funds for pool participants. The scope of services includes providing the Treasurer-Tax Collector with a methodology and a model for future calculation and update of fees. However, the Treasurer-Tax Collector has not yet revised the process to determine the amount of effort spent on both the Treasury or Tax Collection activities.

Planned Action: Once the cost recovery fee study is completed, the Treasurer-Tax Collector will evaluate the firm's recommendations, and a methodology for allocating time between fee activities will be updated.

**6. A Portion of Cash Shortage Expenses For Over the Counter Property Tax Payments Were Allocated to the Treasury (Control Finding)**

We recommend that the Treasurer-Tax Collector allocate all cash shortage expenses to the tax collection work function.

Current Status: **Fully Implemented (First Follow-Up Audit).** The Treasurer-Tax Collector completed cost allocation studies for Fiscal Years 2009/2010 and 2010/2011 in June 2012. The Treasurer-Tax Collector classified all tax collection shortages as direct costs for tax collection. Since the annual cost allocation studies for Fiscal Years 2009/2010 and 2010/2011 charged all tax collection cash shortages to tax collection activities, we consider this recommendation fully implemented.

**7. Differences Between Estimated Administrative Costs Charged to Pool Participants and Actual Administrative Costs have not been Adjusted (Critical Control Weakness)**

We recommend that the Treasurer-Tax Collector make the needed adjustments to the pool participant accounts for the over/undercharge of administrative costs.

Current Status: **Fully Implemented (First Follow-Up Audit).** The Treasurer-Tax Collector processed net refunds to participant accounts in the County Investment Pool and Educational Investment Pool as follows:

Fiscal Year	Overcharge (Undercharge)	Net Refund Processed
2005/2006	\$ (80,734)	November 2011
2006/2007	83,967	November 2011
2007/2008	231,798	November 2011
2008/2009	669,971	November 2011
2009/2010	806,023	June 2012
2010/2011	1,016,654	June 2012



Since adjustments were made to the pool participant accounts for the over/undercharge of administrative costs, we consider this recommendation fully implemented.

**8. T-TC's Annual Cost Allocation Study was not Prepared on a Timely Basis  
(Critical Control Weakness)**

We recommend that the Treasurer-Tax Collector ensure that the annual cost allocation study is prepared within six months following the year-end close.

Current Status: **In-Process (Second Follow-Up Audit).** The Treasurer-Tax Collector staff substantially completed a cost allocation study for Fiscal Year 2011-2012 in December 2012. However, the cost allocation study required some additional analysis and the Treasurer-Tax Collector anticipates the date of completing, reviewing, and finalizing the annual cost allocation study for FY 2011-2012 by April 30, 2013, approximately nine (9) months following the year-end close.

Planned Action: The Treasurer-Tax Collector issued a Request for Proposal, awarded a bid, and engaged a selected firm to review the methodology for the annual cost allocation study. The scope of services includes providing the Treasurer-Tax Collector with a methodology and a model for future calculation and update of fees. Once the cost recovery fee study is completed, the Treasurer-Tax Collector will evaluate the firm's recommendations, and the policies and procedures will be updated to reflect a required timeframe to complete the annual cost allocation study within six months following the year-end close.

**9. Several Business Travel Expenses Allocated to the Treasury Pool Participants did not Clearly Appear to be "Necessary and Reasonable" as Required by County Policy  
(Significant Control Weakness)**

We recommend that the Treasurer-Tax Collector ensure more complete and adequate explanation and justification for business related travel in the documentation submitted with the reimbursement request so as to enable a meaningful third party review.

Current Status: **Fully Implemented (First Follow-Up Audit).** The Treasurer-Tax Collector developed and communicated new internal procedures and forms for reimbursement of business travel. The internal guidelines require that the request for business travel show a clear and concise description of the reason and expected benefit of the travel and applicable conference. When selecting lodging, the traveler should consider the current lodging per diem rates published by the U.S. General Services Administration (US GSA) as a guideline. Meal reimbursements will be limited to current US GSA meal per diem rates. The updated internal procedures require that staff members attending a conference prepare a summary within two weeks of returning from the event that includes an overview of the conference, specific information that benefits the staff member and the office personnel, and at least one change the office should consider for cost savings. Since more complete and adequate documentation is required for business travel, we consider this recommendation fully implemented.





## **10. County Travel Policy is Ambiguous and Internally Inconsistent**

### **(Significant Control Weakness)**

We recommend that the County Executive Office evaluate the business travel policies and procedures and consider the benefits of the inclusion of thresholds or references to existing federal and state per diem rates as guidance and as a basis point for determining reasonable, necessary and business related expenses. The evaluation should also consider the merits of establishing some thresholds requiring a second review and approval outside of the originating department.

Current Status: **In-Process (Second Follow-Up Audit).** The County Executive Office is drafting revised business travel policies and procedures for the Board of Supervisors' review and approval. A review of the draft-in-process business travel policies and procedures disclosed that they are referencing the U.S. General Services (US GSA) per diem rates for domestic destinations. However, the revised business travel policies and procedures are in draft form and not yet completed.

Planned Action: The County Executive Office will present a proposed revision for the County's business travel policies and procedures to the Board of Supervisors. The process for proposing a revision will consider per diem thresholds, a second review, and approval outside of the originating department.

## **11. County Travel Policy is Ambiguous and Internally Inconsistent**

### **(Significant Control Weakness)**

We recommend that the County Executive Office evaluate the business travel policies and Cal Card Policies and Procedures and assess whether the method of paying for lodging expenses should be consistent.

Current Status: **In-Process (Second Follow-Up Audit).** The County Executive Office and the County Procurement Office responsible for the Cal Card Program exchanged viewpoints on the method of paying for lodging expenses. The County Procurement Office has a draft agreement for Cal Card holder which now requires the employee to abide with the County of Orange Business Travel and Reimbursement of Related Expenses Procedure when utilizing the Cal Card while traveling on County business. However, the revised business travel policies and procedures are in draft form and not yet completed.

Planned Action: The County Executive Office will present a proposed revision for the County's business travel policies and procedures to the Board of Supervisors. The proposed revision will ensure the method of paying for lodging expenses is consistent with the Cal Card Policies and Procedures.

## **12. County Travel Policy is Ambiguous and Internally Inconsistent**

### **(Significant Control Weakness)**

We recommend that the County Executive Office evaluate the business travel policies and clarify whether the Auditor-Controller's review of travel expense claims is limited to verification of the department/agency head's signature for authorization as stated in Section 18.1.1 or meant to be an independent assessment of whether claims are adequately justified, necessary and reasonable per submitted documentation, as stated in Section 18.5.



**Current Status: In-Process (Second Follow-Up Audit).** The County Executive Office and the Auditor-Controller have exchanged viewpoints on the review of travel expense claims. The County Executive Office has also drafted an itemized travel expense form for County wide use. However, the revised business travel policies and procedures are in draft form and not yet completed.

**Planned Action:** The County Executive Office will present a proposed revision for the County's business travel policies and procedures to the Board of Supervisors. The proposed revision for the business travel policies and procedures will delineate the roles and responsibilities for review of travel expense claims.

### **13. Investment Authority was Reassigned (Control Finding)**

We recommend that the Treasurer-Tax Collector ensure that the annual cost allocation studies for Fiscal Years 2009/2010 and 2010/2011 are adjusted to account for the reassignment of investment authority.

**Current Status: Fully Implemented (First Follow-Up Audit).** The Treasurer-Tax Collector completed cost allocation studies for Fiscal Years 2009/2010 and 2010/2011 in June 2012. The Treasurer-Tax Collector apportioned expenses from salaries, benefits, services, and supplies to account for the reassigned investment authority held by the Chief Financial Officer during the cost study periods. Since the annual cost allocation studies were adjusted to account for the reassignment of investment authority, we consider this recommendation fully implemented.

We appreciate the assistance extended to us by the Treasurer-Tax Collector and County Executive Office during our Follow-Up Audit. If you have any questions, please contact me directly at 834-5475 or Alan Marcum, Senior Audit Manager at 834-4119.

#### Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Board of Supervisors  
Members, Audit Oversight Committee  
Paul Gorman, Chief Assistant Treasurer-Tax Collector  
Ginika Ezinwa, Accounting and Compliance Manager, Treasurer-Tax Collector  
Rob Richardson, Assistant County Executive Officer  
Michelle Zink, Manager, CEO Administration  
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Susan Novak, Clerk of the Board of Supervisors  
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