



INTERNAL AUDIT DEPARTMENT



Internal Control Audit: Auditor-Controller Fiduciary and Special Revenue Funds

For the Nine Months Ended
March 31, 2020

Audit No. 1818
Report Date: August 28, 2020

Number of Recommendations

0

Critical Control
Weaknesses

1

Significant Control
Weaknesses

3

Control Findings

OC Board of Supervisors

CHAIRWOMAN MICHELLE STEEL
2nd DISTRICT

VICE CHAIRMAN ANDREW DO
1st DISTRICT

SUPERVISOR DONALD P. WAGNER
3rd DISTRICT

SUPERVISOR DOUG CHAFFEE
4th DISTRICT

SUPERVISOR LISA A. BARTLETT
5th DISTRICT



INTERNAL AUDIT DEPARTMENT

Internal Control Audit:
Auditor-Controller Fiduciary and Special Revenue Funds

August 28, 2020

AUDIT HIGHLIGHTS

SCOPE OF WORK	Perform an Internal Control Audit of the Auditor-Controller's (A-C) fiduciary and special revenue funds process for the nine-month period ended March 31, 2020.	
RESULTS	<ul style="list-style-type: none"> We concluded that A-C's internal controls over the fiduciary and special revenue funds process is generally effective to ensure sources and uses of funds are proper and in compliance with County and departmental policy, procedures, laws, and government codes. We concluded that the fiduciary and special revenue process is generally efficient. 	
RISKS IDENTIFIED	<p>As a result of our findings, potential risks include:</p> <ul style="list-style-type: none"> Cyber security breaches, cybercrimes, and threats. Misunderstandings and miscommunication regarding rights, responsibilities, and authorized uses for a fund. Undetected errors, irregularities, or potential fraud that may not be detected or resolved timely. Errors or irregularities could go undetected. 	
NUMBER OF RECOMMENDATIONS	<p>Opportunities for enhancing internal control include:</p> <ul style="list-style-type: none"> Restricting Personally Identifiable Information. Ensuring all fiduciary and special revenue funds are supported with complete written documentation. Ensuring proper documentation for fund reconciliations. Completing reconciliations in a timely manner. 	
0	CRITICAL CONTROL WEAKNESSES	
1	SIGNIFICANT CONTROL WEAKNESSES	
3	CONTROL FINDINGS	

Report suspected fraud, or misuse of County resources by vendors, contractors, or County employees to 714.834.3608



INTERNAL AUDIT DEPARTMENT

Audit No. 1818

August 28, 2020

To: Frank Davies, CPA
Auditor-Controller

From: Aggie Alonso, CPA, CIA, CRMA
Internal Audit Department Director

Subject: Internal Control Audit: Auditor-Controller Fiduciary and Special Revenue Funds

We have completed an Internal Control Audit of the Auditor-Controller's (A-C) Fiduciary and Special Revenue process for the nine-month period ended March 31, 2020. Details of our results and recommendations immediately follow this letter. Additional information including background and our objectives, scope, and methodology are included in Appendix A.

The A-C concurred with all of our recommendations and the Internal Audit Department considers the A-C's management response appropriate to the recommendations in this report.

We will include the results of this audit in a future status report submitted quarterly to the Audit Oversight Committee and the Board of Supervisors. In addition, we will request your department complete a Customer Survey of Audit Services, which you will receive shortly after the distribution of our final report.

We appreciate the courtesy extended to us by A-C's personnel during our audit. If you have any questions regarding our audit, please contact me at 714.834.5442 or Assistant Director Scott Suzuki at 714.834.5509.

Attachments

Other recipients of this report:

- Members, Board of Supervisors
- Members, Audit Oversight Committee
- Auditor-Controller Distribution
- Foreperson, Grand Jury
- Robin Stieler, Clerk of the Board of Supervisors
- Eide Bailly LLP, County External Auditor

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RESULTS

BUSINESS PROCESS & INTERNAL CONTROL STRENGTHS

Business process and internal control strengths noted during our audit include:

- ✓ Fiduciary and special revenue funds use has been authorized in the form of an agreement, statutory requirement, Board resolution, or by specific responsibilities of A-C.
- ✓ County Accounting Manuals and detailed desk procedures are used to perform fund duties.
- ✓ Adequate supporting documentation for fund receipts and disbursements is maintained.
- ✓ Fund policy and procedures are established and well-documented, including notes on identifying common reconciliation differences for some funds.
- ✓ For applicable funds, adequate interest reserves are maintained before disbursing interest payments to cities to avoid any potential cash deficit as occurred in prior years.
- ✓ An internal fund closure checklist is completed before deleting/closing funds.

FINDING NO. 1

Personally Identifiable Information

Fund transaction support included personally identifiable information (PII). Specifically, we reviewed all 19 cash receipts for Funds 290 and 292 that were related to “separated employee premium payments” and noted all 19 (100%) of the receipts included employee PII. While this information was restricted to employees granted access to the County’s financial images, the unredacted PII could potentially be accessed by an authorized user without an appropriate business need.

CATEGORY

Significant Control Weakness

RISK

Inadequate security over PII could result in identity theft, embarrassment, or blackmail. The impact to the County could include loss of the public’s trust, legal liability, and remediation costs.

RECOMMENDATION

A-C redact PII from fund transaction supporting documentation.

MANAGEMENT RESPONSE

Concur. AC has begun redacting PII as recommended.



INTERNAL AUDIT DEPARTMENT

FINDING No. 2	Fiduciary Fund Documentation <p>Seven of sixteen funds reviewed (44%) were not adequately supported with Chart of Account (COFA) documentation.</p> <p>The COFA elements are required to be entered into CAPS+ for the establishment of any new funds. A-C indicated there was no supporting documentation because the funds were established prior to the implementation of CAPS+.</p> <p>County COFA documentation is maintained for fund establishment, modification, and deletion, which supports the fund's purpose, nature of revenue sources, permitted expenditures, expiration date, and planned disposition of residual balances at closing.</p>
CATEGORY	Control Finding
RISK	Absence of complete written fund documentation may increase the risk of misunderstandings or miscommunication regarding rights, responsibilities, and authorized uses for a fund.
RECOMMENDATION	A-C ensure that all fiduciary and special revenue funds are fully supported with complete written documentation in compliance with department policy.
MANAGEMENT RESPONSE	Concur. AC will update these COFAs to the current policy standard by February 2021.

FINDING No. 3	Reconciliation Documentation <p>A-C Payroll Funds 290 and 292 did not have adequate documentation to show the following fund reconciliations:</p> <ul style="list-style-type: none">• General ledger, expense report, and revenue report to the department's records• Bank statements to the provider benefit statements <p>While there are procedures and workpaper documents that indicate performance of reconciliations, we found the procedures are missing a mechanism for providing appropriate proof that all fund activity has been reviewed and reconciled. For example, the documentation provided did not include the individuals preparing and reviewing the reconciliation or the completion date.</p>
CATEGORY	Control Finding



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RISK	Inadequate reconciliation documentation increases the risk of undetected errors, irregularities, or potential fraud that may not be detected or resolved timely.
RECOMMENDATION	A-C Payroll should properly document Funds 290 and 292 reconciliations including preparer and reviewer signatures, completion dates, and support for noted differences in reconciliations.
MANAGEMENT RESPONSE	Concur. Additional documentation steps have been implemented for all reconciliations on a prospective basis.

FINDING NO. 4	<p>Timeliness of Fund 216 Reconciliations</p> <p>A-C Property Tax Fund 216 reconciliations were not performed on a monthly basis as required by County policy. A-C indicated the delays were a result of limited staffing.</p> <p>We noted that, as of May 2020, the most recently performed reconciliation by A-C Property Tax unit was for the period of January 2020. Upon further review we noted that the periods of July to December 2019 had not been reconciled until February 2020.</p>
CATEGORY	Control Finding
RISK	Delays and backlogs in monthly reconciliations increases the potential risk of errors or irregularities going undetected.
RECOMMENDATION	A-C Property Tax unit ensure fund reconciliations are completed on a monthly basis.
MANAGEMENT RESPONSE	Concur. All reconciliations are now current and will be monitored for monthly completion.

AUDIT TEAM	Scott Suzuki, CPA, CIA, CISA, CFE Michael Dean, CPA, CIA, CISA Zan Zaman, CPA, CIA, CISA Gabriela Cabrera Stephany Pantigoso	Assistant Director Senior Audit Manager Audit Manager Senior Auditor Senior Auditor
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APPENDIX A: ADDITIONAL INFORMATION

OBJECTIVES	<p>Our audit objectives were to:</p> <ol style="list-style-type: none">1. Evaluate the effectiveness of internal control over fiduciary or special revenue funds to ensure sources and uses of funds are proper and in compliance with County and departmental policy, procedures, laws, and government codes.2. Review the fiduciary and special revenue funds process for efficiency.
SCOPE & METHODOLOGY	<p>Our audit scope was limited to internal control over A-C fiduciary and special revenue funds process for the nine-month period ended March 31, 2020. Our methodology included inquiry and examination of documentation.</p> <p>Our audit included a review of the following Funds: 15Q, 211, 212, 213, 216, 249, 290, 292, 309, and 353. See Appendix C for additional fund information.</p>
EXCLUSIONS	<p>Our audit scope did not include a review of the information technology controls for any of the Auditor-Controller's systems used in the administration of fiduciary and special revenue funds. In addition, we did not review compliance with GASB 84 "Fiduciary Activities," which was initially effective in FY 19-20, and subsequently extended for one year.</p>
PRIOR AUDIT COVERAGE	<p>An audit with similar scope, Internal Control Audit: Auditor-Controller Fiduciary (Agency) and Special Revenue Funds for the Period July 1, 2013 through December 31, 2014, Audit No. 1337, was issued on May 21, 2015.</p>



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BACKGROUND

Auditor-Controller's Central Accounting Operations include the Claims and Disbursing Unit, Payroll Unit, Financial Reporting Unit, General Accounting Unit, Cost, Revenue and Budget Unit, and Property Tax Unit to provide core services that are traditionally associated with the Auditor-Controller's Office such as: accounts payable services, financial reporting, and maintenance of the property tax rolls.

Fiduciary funds are separate funds that are used to record assets held by departments in a trustee capacity or as an agent for individuals, private organizations, or other governmental agencies. Therefore, the assets of fiduciary funds cannot be used to support the County's own programs. Fiduciary funds are classified into four different types:

- Pension Trust Funds – used to report resources that are required to be held in trust for the members and beneficiaries of defined benefit pension plan, defined contribution plans, other postemployment benefit plans, or other employee benefit plans (i.e., Fund 167-Extra Help Retirement Plan).
- Investment Trust Funds – used to report the external portion of investment pools reported by a sponsoring government.
- Private-Purpose Trust Funds – used to report all other trust arrangements under which principal and income benefit individuals, private organizations, or other governments. (i.e., Fund 164 & 165 – DA Public Administrator Estate Fund and Public Guardian Trust).
- Agency Funds – used to report resources held by the County in a purely custodial capacity. Agency funds typically involve only the receipt, temporary investment, and remittance of fiduciary resources to individuals, private organizations, or other governments. (i.e., funds held by departments in Fund 300 series that are held before distribution to non-County third parties).

Special revenue funds are used to account for the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments or for major capital projects) that are legally restricted to expenditure for specified purposes.



INTERNAL AUDIT DEPARTMENT

PURPOSE & AUTHORITY	We performed this audit in accordance with the FY 2019-20 Audit Plan and Risk Assessment approved by the Audit Oversight Committee (AOC) and Board of Supervisors (Board).
PROFESSIONAL STANDARDS	Our audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing issued by the International Internal Audit Standards Board.
FOLLOW-UP PROCESS	<p>In accordance with professional standards, the Internal Audit Department has a process to follow-up on its recommendations. A first follow-up audit will generally begin six months after release of the initial report.</p> <p>The AOC and Board expect that audit recommendations will typically be implemented within six months or sooner for significant and higher risk issues. A second follow-up audit will generally begin six months after release of the first follow-up audit report, by which time all audit recommendations are expected to be implemented. Any audit recommendations not implemented after the second follow-up audit will be brought to the attention of the AOC at its next scheduled meeting.</p> <p>A Follow-Up Audit Report Form is attached and is required to be returned to the Internal Audit Department approximately six months from the date of this report in order to facilitate the follow-up audit process.</p>
MANAGEMENT'S RESPONSIBILITY FOR INTERNAL CONTROL	In accordance with the Auditor-Controller's County Accounting Manual Section S-2 Internal Control Systems: "All County departments/agencies shall maintain effective internal control systems as an integral part of their management practices. This is because management has primary responsibility for establishing and maintaining the internal control system. All levels of management must be involved in assessing and strengthening internal controls." Control systems shall be continuously evaluated by Management and weaknesses, when detected, must be promptly corrected. The criteria for evaluating internal controls is the Committee of Sponsoring Organizations of the Treadway Commission (COSO) Internal Control – Integrated Framework. Our Internal Control Audit enhances and complements, but does not substitute for department management's continuing emphasis on control activities and monitoring of control risks.
INTERNAL CONTROL LIMITATIONS	Because of inherent limitations in any system of internal control, errors or irregularities may nevertheless occur and not be detected. Specific examples of limitations include, but are not limited to: resource constraints, unintentional errors, management override, circumvention by collusion, and poor judgment. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or the degree of compliance with the procedures may deteriorate. Accordingly, our audit would not necessarily disclose all weaknesses in the department's operating procedures, accounting practices, and compliance with County policy.



APPENDIX B: FINDING TYPE CLASSIFICATION

Critical Control Weakness	Significant Control Weakness	Control Finding
These are audit findings or a combination of audit findings that represent critical exceptions to the audit objective(s) and/or business goals. Such conditions may involve either actual or potential large dollar errors or be of such a nature as to compromise the department's or County's reputation for integrity. Management is expected to address Critical Control Weaknesses brought to its attention immediately.	These are audit findings or a combination of audit findings that represent a significant deficiency in the design or operation of internal controls. Significant Control Weaknesses require prompt corrective actions.	These are audit findings concerning the effectiveness of internal control, compliance issues, or efficiency issues that require management's corrective action to implement or enhance processes and internal control. Control Findings are expected to be addressed within our follow-up process of six months, but no later than twelve months.



INTERNAL AUDIT DEPARTMENT

APPENDIX C: FUND INFORMATION

Fund	Fund Name	Reason for Inclusion	Fund Balance at 3/31/2020
15Q	Pension Obligation Bond Amortization	High prepaid expenses balance of \$144M.	\$143,646,635
211	Supplemental Law Enforcement Services	High cash inflows of approximately \$23M and outflows of approximately \$19M.	\$11,089,282
212	Public Safety Augmentation	High cash inflows of approximately \$277M and outflows of approximately \$279M.	\$12,534
216	Vehicle License Fee (VLF) Property Tax Compensation	High cash inflows of approximately \$372M and outflows of approximately \$372M.	\$ 344,767
249	Retirement Contributions	High cash inflows of approximately \$549M and outflows of approximately \$559M.	\$ 328,961
290	Insurance Health Plans ISF	High cash inflows of approximately \$132M and outflows of approximately \$136M. A-C indicated fund management by CEO-HRS' Employee Benefits.	\$ 55,424,778
292	Self-Insured PPO Health Plans ISF	High Cash inflows of approximately \$51M and outflows of approximately \$57M. A-C indicated fund management by CEO-HRS' Employee Benefits.	\$ 6,622,879
309	Attached Salary (Auditor-Controller)	High Cash inflows of approximately \$276M and outflows of approximately \$282M.	\$389,420
213	Sales & Use Tax Compensation	Residual cents activity of \$0.02 to close fund in September 2019.	\$0
353	Auditor-Controller	No activity and fund closed 9/2019.	\$0

SOURCE: CAPS+ Data Warehouse



APPENDIX D: AUDITOR-CONTROLLER MANAGEMENT RESPONSE



OFFICE OF THE
ORANGE COUNTY AUDITOR-CONTROLLER

FRANK DAVIES, CPA
AUDITOR-CONTROLLER

August 25, 2020

Aggie Alonzo, Director
Internal Audit Department

RE: Management Response to Audit 1818, Fiduciary and Special Revenue Funds

We have reviewed the audit report from your office dated July 15, 2020, titled Internal Control Audit: Auditor-Controller Fiduciary and Special Revenue Funds. We are pleased to provide the below responses to the audit findings and recommendations.

Finding No. 1 - Personally Identifiable Information

Fund transaction support included personally identifiable information (PII). Specifically, we reviewed all 19 cash receipts for Funds 290 and 292 that were related to "separated employee premium payments" and noted all 19 (100%) of the receipts included employee PII. While this information was restricted to employees granted access to the County's financial images, the unredacted PII could potentially be accessed by an authorized user without an appropriate business need.

Recommendation A-C redact PII from fund transaction supporting documentation.

Management Response:

Concur. AC has begun redacting PII as recommended.

Finding No. 2 - Fiduciary Fund Documentation

Seven of sixteen funds reviewed (44%) were not adequately supported with Chart of Account (COFA) documentation. The COFA elements are required to be entered into CAPS+ for the establishment of any new funds. A-C indicated there was no supporting documentation because the funds were established prior to the implementation of CAPS+. County COFA documentation is maintained for fund establishment, modification, and deletion, which supports the fund's purpose, nature of revenue sources, permitted expenditures, expiration date, and planned disposition of residual balances at closing.

Recommendation A-C ensure that all fiduciary and special revenue funds are fully supported with complete written documentation in compliance with department policy.

Management Response:

Concur. AC will update these COFAs to the current policy standard by February 2021.

Finding No. 3 - Reconciliation Documentation

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- General ledger, expense report, and revenue report to the department's records
- Bank statements to the provider benefit statements

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Management Response to Audit 1818, Fiduciary and Special Revenue Funds
August 25, 2020
Page 2 of 2

While there are procedures and workpaper documents that indicate performance of reconciliations, we found the procedures are missing a mechanism for providing appropriate proof that all fund activity has been reviewed and reconciled. For example, the documentation provided did not include the individuals preparing and reviewing the reconciliation or the completion date.

Recommendation A-C Payroll should properly document Funds 290 and 292 reconciliations including preparer and reviewer signatures, completion dates, and support for noted differences in reconciliations.

Management Response:

Concur. Additional documentation steps have been implemented for all reconciliations on a prospective basis.

Finding No. 4 - Timeliness of Fund 216 Reconciliations

A-C Property Tax Fund 216 reconciliations were not performed on a monthly basis as required by County policy. A-C indicated the delays were a result of limited staffing. We noted that, as of May 2020, the most recently performed reconciliation by A-C Property Tax unit was for the period of January 2020. Upon further review we noted that the periods of July to December 2019 had not been reconciled until February 2020.

Recommendation A-C Property Tax unit ensure fund reconciliations are completed on a monthly basis.

Management Response:

Concur. All reconciliations are now current and will be monitored for monthly completion.

If you have any questions or require additional information, please contact JC Squires, Director of Central Accounting Operations at (714) 834-5521.

Sincerely,



Frank Davies, CPA
Auditor-Controller

cc: Salvador Lopez, Chief Deputy Auditor-Controller
JC Squires, Director, Central Accounting Operations
Scott Suzuki, Assistant Director, Internal Audit Department

