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## INTERNAL AUDIT DEPARTMENT

File No. 2222

November 27, 2002

TO: Michael Schumacher, Ph.D.  
County Executive Officer

SUBJECT: Department Control Review of CEO/Employee Benefits Division  
Cash Receipting and Cash Disbursing Processes

Attached is a copy of our audit report on CEO/Employee Benefits Division Cash Receipting and Cash Disbursing Processes as of March 31, 2002. If you have any questions, please call me or Eli Littner, Deputy Director, at 834-5899, or Michael Goodwin, Audit Manager at 834-6066.

Respectfully submitted,

Dr. Peter Hughes, CPA  
Director, Internal Audit

### Attachment

#### Other recipients of this audit report:

- Members, Board of Supervisors
- Members, Audit Oversight Committee
- Foreman, Grand Jury
- Darlene J. Bloom, Clerk of the Board of Supervisors
- Jan Walden, Assistant CEO, Office of Human Resources
- Patricia Gilbert, Manager, CEO/HR/Employee Benefits
- Renee Catanzariti, Assistant Manager, CEO/HR/Employee Benefits

**DEPARTMENT CONTROL REVIEW  
COUNTY EXECUTIVE OFFICE  
OFFICE OF HUMAN RESOURCES  
EMPLOYEE BENEFITS DIVISION  
CASH RECEIPTS  
AND  
CASH DISBURSEMENTS**

**FOR THE PERIOD FROM JANUARY 1, 2001 THROUGH MARCH 31, 2002**

**REPORT DATE:  
NOVEMBER 27, 2002**

**Audit Number #2222**

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<b>Audit Director:</b>	<b>Dr. Peter Hughes, CPA</b>
<b>Deputy Director:</b>	<b>Eli Littner, CPA</b>
<b>Audit Manager:</b>	<b>Michael Goodwin, CPA</b>
<b>Senior Auditors:</b>	<b>Lily Chin, CPA</b>
	<b>James Santer, CIA</b>



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**INTERNAL AUDIT DEPARTMENT  
COUNTY OF ORANGE**

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## APPENDIX: MANAGEMENT'S RESPONSES



PETER HUGHES, Ph.D., CPA, CIA, CFE, CITP  
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Santa Ana, California 92701-4521

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## INTERNAL AUDIT DEPARTMENT

Audit No. 2222

November 27, 2002

## INTERNAL AUDITOR'S REPORT

Michael Schumacher, Ph.D.  
County Executive Officer  
10 Civic Center Plaza  
Santa Ana, CA 92701

We have completed a review of internal controls over cash receipts and cash disbursements in the County Executive Office/Human Resources/Employee Benefits Division (Employee Benefits) for the period from January 1, 2001 through March 31, 2002. Our review was made in accordance with professional standards established by the Institute of Internal Auditors for the purpose of evaluating the adequacy of internal controls in the areas noted above. We believe our review provides a reasonable basis for our opinion.

Management of Employee Benefits is responsible for establishing and maintaining a system of internal controls. The objectives of an internal control system are to provide management with reasonable, but not absolute assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly. County Accounting Procedure (CAP) No. 33 - *Internal Control Systems* - prescribes the policies and standards to be followed by departments/agencies in establishing and maintaining internal control systems. Our review enhances and complements, but does not substitute for the Employee Benefits' continuing emphasis on control activities and self-assessment of control risks.

Because of inherent limitations in any system of internal controls, errors or irregularities may nevertheless occur and not be detected. 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 that the degree of compliance with the procedures may deteriorate. Accordingly, our review made for the limited purpose described above would not necessarily disclose all weaknesses in the Employee Benefits' operating procedures, accounting practices and compliance with County policy.

Based upon our review, it is our opinion that internal controls are generally adequate to ensure cash receipts are properly collected, deposited, recorded and safeguarded; cash disbursements are authorized, accurate and supported; and transactions are processed in accordance with management's authorization and direction. Our substantive testing did not disclose any instances of monetary loss or misappropriation; however, we did observe opportunities where internal controls could be enhanced as detailed in the Observations, Recommendations, and Management Responses section of this report. Responses from Employee Benefits have been included for each recommendation and the complete text of responses has been appended to the report.

We appreciate the courtesy and cooperation extended to us by the personnel of the Employee Benefits during our review. If we can be of further assistance, please contact me directly or Eli Littner, Deputy Director at (714) 834-5899 or Michael Goodwin, Audit Manager at (714) 834-6066.

Respectfully submitted,



Dr. Peter Hughes, CPA  
Director, Internal Audit

Attachment

Distribution: Pursuant to Audit Oversight Committee Procedure No. 1  
Members, Board of Supervisors  
Members, Audit Oversight Committee  
Foreman, Grand Jury  
Clerk of the Board of Supervisors  
Jan Walden, Assistant CEO, Office of Human Resources  
Patricia Gilbert, Manager, CEO/HR/Employee Benefits  
Renee Catanzariti, Assistant Manager, CEO/HR/Employee Benefits

## OVERVIEW

### OBJECTIVE

The Internal Audit Department conducted a review of the County Executive Office/Human Resources/Employee Benefits Division (Employee Benefits) for the purpose of evaluating internal controls and whether they are functioning adequately in the area of cash receipts and cash disbursements to ensure:

- ◆ Cash receipts are properly collected, recorded, deposited, and reconciled.
- ◆ Cash receipts are adequately safeguarded to minimize occurrence of loss or theft.
- ◆ Cash disbursements are authorized, accurate, supported and processed timely in accordance with management's authorization.

### BACKGROUND

Employee Benefits provides a comprehensive and competitive benefits package to County employees by offering a variety of benefit programs, such as five different health plans, health and dependent care reimbursement accounts, Employee Assistance Program, Deferred Compensation Program, tuition reimbursement program, etc. They also provide dental and salary continuance benefits for a portion of County employees. The five health plans consist of three self-funded Preferred Provider Organization plans (PPO) and two Health Maintenance Organization plans (HMO). The enrollment to any plan is processed in the County Accounting and Personnel System (CAPS)/Advantage Human Resources System (AHRS). The employees' shares of benefit costs are deducted through the County payroll process.

Cash receipts processed by Employee Benefits are primarily for health insurance premiums paid by employees on family leave, leave of absence (LOA), retirees, or separated employees qualifying under the Consolidated Omnibus Budget Reconciliation Act (COBRA) provision, and for refunds of claims. Employee Benefits collect and process the cash receipts and deposits the monies with the County Treasury. The Deposit Order is submitted to the Auditor-Controller for recording into the CAPS/Advantage Financial System (AFNS). The total cash receipts processed during the calendar year ended 12/31/2001 was approximately \$4.5 million.

Cash disbursements processed by Employee Benefits primarily include premiums for the HMO plans, life, and disability insurance; claims (medical, dental, prescription, salary continuance); flexible spending accounts (health and dependent care reimbursement); third party benefit administrator's service fees; and employee benefits consultant fees. Employee Benefits prepares payment requests, reviews invoices, authorizes payments, and submits them to the Auditor-Controller's office where the actual payment is disbursed. The self-insured medical and dental claims payments are paid to the third party administrator through the County Treasury using zero-balance account (ZBA), and Employee Benefits prepares a Journal Voucher to record these payments. The total cash disbursements processed by Employee Benefits was approximately \$103.8 million for the calendar year ended 12/31/2001.

## **SCOPE**

Our review was limited to cash receipts and cash disbursements occurring between January 1, 2001 and March 31, 2002. Our review included inquiry, auditor observation and testing of relevant documentation for the purpose of assessing the adequacy of internal controls over cash receipts and cash disbursements processed by Employee Benefits.

Our review did not include an evaluation of the CAPS information systems or system controls used in its cash receipting and cash disbursing processes or the controls in the Auditor-Controller's Claims & Disbursing Section. We did not review the benefit enrollment or payroll deduction processes, or the third party administrators' cash handling, claims review, and payment processes.

Employee Benefits is currently working with a contractor to administer the billing and collection of LOA and COBRA premium that will take effect in January 2003. Our recommendations pertaining to monitoring the third party administrator's collections and invoice review (Report Items IV. and VI.) would also be applicable to the new administrator.

## **CONCLUSION**

It is our opinion that internal controls over cash receipting and cash disbursing are generally adequate for Employee Benefits to ensure cash receipts are properly collected, recorded, deposited, and safeguarded, and cash disbursements are properly authorized, accurate, supported and processed timely in accordance with management's authorization. It should be noted that Employee Benefits has been responsive to our observations and recommendations and started implementing some of the recommendations during our fieldwork. Although our testing did not disclose significant problems within the areas of cash receipts and cash disbursements we reviewed, we did observe the following areas where internal controls should be enhanced:

- I. Accountability Over Cash Receipts
- II. Physical Safeguards
- III. Reconciliation
- IV. Monitoring Premium Collection
- V. Special Use Fund
- VI. Invoice Review

Our observations and recommendations are discussed in the Observations, Recommendations and Management Responses section of this report.

## **OBSERVATIONS, RECOMMENDATIONS AND MANAGEMENT RESPONSES**

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### **I. Accountability Over Cash Receipts**

Accountability over cash receipts should be established when monies are initially collected, and when transferred between employees during the collection and deposit process. This internal control practice helps ensure that all monies received are completely and properly deposited. We found certain controls were not in place and should be added to strengthen accountability over cash receipts.

1. Establish initial collection records by preparing a list of mail payments upon receipt by the employee opening the mail. This will also help management monitor whether cash receipts are deposited timely and accurately.
2. Stamp-endorse checks immediately upon opening the mail.
3. Ensure cash receipts transferred between employees are verified in the presence of both employees and the transfer of accountability is documented in writing.
4. Maintain a listing of payments received and not deposited for inclusion in the reconciliation of collection records to deposits.

#### **Recommendation No. 1**

Employee Benefits management take additional measures to ensure accountability is properly established during the collection and deposit process by preparing initial collection records, stamp endorsing checks immediately upon receipt, documenting transfer of accountability, and maintaining records of monies not deposited.

#### **Employee Benefits Response:**

**Concur.** Employee Benefits has now implemented all 4 of the recommended controls in Recommendation No. 1 above.

### **II. Physical Safeguards**

Assets such as cash receipts must be safeguarded against unauthorized acquisition, use, or disposition. Access controls help to safeguard these assets. The following are areas where controls can be enhanced to improve the physical safeguarding objective.

1. Cash receipts were kept in unlocked cash box in an unlocked file cabinet drawer.
2. Access to the key to the file cabinet where cash receipts are stored was not restricted to appropriate employees.

#### **Recommendation No. 2**

Employee Benefits management ensures controls are in place to safeguard cash receipts by keeping access to the monies restricted and cash safeguarded until they are deposited in the treasury.



**Employee Benefits Response:**

**Concur.** The cash box has been put in a locked cabinet drawer, and there are only two employees that have key access to the drawer: the person performing the deposits, and the Accounting Manager.

**III. Reconciliation**

Reconciliation is a comparison of one set of data to another, identifying and investigating differences, and taking corrective action when necessary to resolve those differences. This internal control activity helps ensure the accuracy and completeness of transactions. Reconciling monthly general ledger reports to departmental subsidiary records is an example of reconciling one set of data to another.

Employee Benefits uses trust funds to accumulate and disburse insurance premiums for HMO plans and Sheriff insurance plans (Fund 305), and for life insurance, and accidental death and dismemberment insurance (Fund 304). The following are areas where additional controls should be implemented:

1. Reconciliation of all validated Deposit Orders to collection records and to the general ledger should be performed monthly and documented. Differences should be investigated and resolved monthly.
2. Payment requests (e.g. Request for Check, invoice payment, electronic fund transfer) submitted to A-C should be reconciled monthly to the County financial reports (e.g. General Ledger, Expense to Budget Report) to ensure they were processed accurately in the financial system.
3. Trust funds 304 and 305 are not being reconciled to the General Ledger. Employee Benefits solely monitors the balances in the funds for reasonableness. We were informed that reconciling the funds would be difficult due to numerous automated payroll entries recorded into the funds and Employee Benefits not having access to support documentation for those automated entries. Efforts made in the past to reconcile the automated entries have not been successful.

In our opinion, there should be a reconciliation of fund deposits and payments to County financial records with some reliance being placed on the automated entries. While reconciliation is the objective, in the interim, the trust fund balances should be monitored to ensure they are adequate to meet the health and benefit plan disbursements.

**Recommendation No. 3:**

Employee Benefits management take appropriate measures to reconcile deposits and payments to financial reports monthly to ensure accuracy and completeness. Also, measures should be considered to ensure accuracy and completeness of trust fund activities and balances are adequate to meet the health and benefit plan obligations.

**Employee Benefits Response:**

**Concur.** Employee Benefits will develop appropriate procedures to verify payments and deposits against the monthly General Ledger to ensure accuracy and completeness. This procedure will be developed and implemented by February 28, 2003. Employee Benefits will gladly meet with representatives of the Internal Audit Department to discuss their

recommendation for the method of ongoing reconciliation of the Trust Funds. In the meantime, Employee Benefits will continue to monitor the monthly balance of the Trust Funds to ensure they reflect required funding levels.

#### **IV. Monitoring Premium Collections**

Employee Benefits contracts with a third party administrator (Delta Health Systems) to administer the billing and collection of insurance premiums for LOA and COBRA. Employee Benefits receives a check monthly from the administrator for the premiums collected. The administrator sends a spreadsheet summarizing the total premiums collected applicable to each health plan by type of collection, such as Family Leave, LOA, and COBRA. All of collections are paid to the County except for the HMO premium collected from the COBRA participants. They are sent directly to the two HMO carriers – Kaiser Permanente and CIGNA. The payment amounts are also included in the spreadsheet summary.

When a third party such as Delta performs a business process, monitoring controls become important to ensure the control objective is met. We noted the following areas where monitoring controls should be improved to ensure correct amounts are received:

1. Employee Benefits should receive a detail report from the administrator to verify the accuracy of cash receipts summary spreadsheet. This could have detected an error made by administrator where cash receipts were overpaid to the County by \$15,438 for the February 2002 collection.
2. A difference often exists when the administrator's check total is compared to the grand total of each health plan's premium amounts collected. This variance pertains to the difference between the COBRA HMO collection and amount paid to the HMO carriers where the collected amount is greater. This excess is included in the administrator's monthly check. Employee Benefits resolved the difference by allocating it between the two HMO carriers (one-third Kaiser and two-thirds CIGNA) and depositing it as a COBRA premium. However, there was no support for this allocation method. Employee Benefits should resolve the difference with adequate investigation and supporting documentation submitted by the administrator. Documentation such as administrator's system report supporting the spreadsheet amounts will help to identify the difference so that actual overages are calculated.
3. Employee Benefits provides the administrator a list of employees on Family Leave, LOA, and COBRA to help process billings and collections. The administrator updates the list noting the amount collected and sends it back to Employee Benefits. Employee Benefits should reconcile the updated list to the actual cash receipts to ensure appropriate amounts are received.

#### **Recommendation No. 4:**

Employee Benefits management take appropriate measures to monitor cash receipts collected by the administrator for accuracy and completeness, and resolve any differences with adequate research and support documentation.

**Employee Benefits Response:**

**Concur.** Employee Benefits now verifies supporting documentation for the cash receipts spreadsheet provided with the monthly remittance to the County. Proper actions have been taken to correct the overpayment to the County. In addition, the administrator has modified its spreadsheet to allocate appropriately to each health plan the exact difference between premium paid and premium collected. The administrator still performs the calculations by taking the difference between the amount collected and the amounts paid to COBRA HMO carriers, however there is no longer a need for an allocation of one-third to Kaiser and two-thirds to CIGNA. We now know exactly how much to allocate to each plan. Lastly, starting in January 2003, Employee Benefits will implement a reconciliation process with the new administrator to reconcile premiums collected to reports of those in a billing status for COBRA, Leave of Absence, or Family Leave. This new procedure will be finalized by March 31, 2003.

**V. Special Use Revolving Fund**

Employee Benefits maintains a special use revolving fund with an authorized amount of \$50,000 for the purpose of paying salary continuance to management and attorney employees. Employee Benefits controls the special use bank account and receives monthly bank statements showing activity in the fund. A third party administrator (Standard Insurance) draws from the fund via electronic fund transfers and provides support documentation to Employee Benefits for the claims paid. Employee Benefits replenishes the account monthly or when the balance is below \$20,000.

**A. Bank Reconciliation**

Employee Benefits did not prepare a formal reconciliation between the bank statement and the revolving fund. Employee Benefits did not maintain a record showing all activities in the account, which would help in the monthly bank reconciliation. An analysis of disbursements based on the monthly bank statement and administrator's supporting documents is prepared to support the payment request with the Auditor-Controller, but it only included the disbursements and not the deposits or credits into the account.

**Recommendation No. 5a:**

Employee Benefits establish a register recording complete account activities and prepare a monthly bank reconciliation to ensure that all monies are accounted for and identified. Any differences should be investigated, resolved and documented.

**Employee Benefits Response:**

**Concur.** Employee Benefits has developed a reconciliation report and records weekly balances from the bank, so that differences will be identified and resolved on a monthly basis.

**B. Fund Reconciliation**

Employee Benefits did not reconcile the special use revolving fund to the authorized fund amount. Funds should be reconciled monthly to the authorized amount to account for the usage of the funds. Our testing revealed that the actual funded amount exceeded the authorized amount by an average of \$2,800.

**Recommendation No. 5b:**

Employee Benefits management should perform the fund reconciliation monthly and identify and resolve the differences appropriately, and limit the fund to the established \$50,000.

**Employee Benefits Response:**

**Concur.** We are developing procedures so that the fund will be reconciled on a monthly basis to prevent an excess in the balance. However because salaries have increased over the years, \$50,000 is no longer sufficient to fund the payments of salary continuance for County managers and attorneys, therefore Employee Benefits will work with Auditor Controller staff to investigate increasing the fund limit to an appropriate amount. A procedure will be implemented by March 31, 2003.

**VI. Invoice Review**

Invoices from third party administrators should be reviewed to ensure the accuracy in the number of participants, rates, calculations, and correct account coding. Employee Benefits pays service fees to the third party administrator (Delta Health Systems). Service fees are based on a rate per eligible participant. We noted that the total eligibility number on the invoice was not directly verified to Employee Benefits departmental records for accuracy. Our testing of four invoices disclosed the total eligibility number on the invoices were fewer than Employee Benefits' report total by a small variance, resulting in underpayments.

**Recommendation No. 6:**

Employee Benefits management ensure all information on third party administrator's invoices are verified for accuracy.

**Employee Benefits Response:**

**Concur.** Starting January 1, 2003 invoices to vendors for fees based on enrollment numbers will be paid directly from reports produced by the new County of Orange Benefits Center, ensuring accuracy of payments to actual enrollment.

**APPENDIX: MANAGEMENT'S RESPONSE**



*County of Orange*

**MEMO**

November 18, 2002

**To:** Dr. Peter Hughes, CPA, Director, Internal Audit  
**From:** Michael Schumacher, Ph.D., County Executive Officer  
**Subject:** **Audit of Internal Controls of the County Executive Office/Human Resources/Employee Benefits Division**

Attached please find our responses to the audit of the internal controls of the County Executive Office/Human Resources/Employee Benefits Division.

We appreciate the time and effort spent by your audit staff in reviewing the internal controls of the Employee Benefits Division.

Please contact me if you have any questions.

Thank you.

Attachment

**DEPARTMENT CONTROL REVIEW  
COUNTY EXECUTIVE OFFICE  
OFFICE OF HUMAN RESOURCES  
EMPLOYEE BENEFITS DIVISION  
CASH RECEIPTS  
AND  
CASH DISBURSEMENTS**

**FOR THE PERIOD FROM JANUARY 1, 2001 THROUGH MARCH 31, 2002**

**REPORT DATE:**

**Audit Number #2222**

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<b>Audit Director:</b>	<b>Dr. Peter Hughes, CPA</b>
<b>Deputy Director:</b>	<b>Eli Littner, CPA</b>
<b>Audit Manager:</b>	<b>Michael Goodwin, CPA</b>
<b>Senior Auditors:</b>	<b>Lily Chin, CPA James Santer, CIA</b>



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**INTERNAL AUDIT DEPARTMENT  
COUNTY OF ORANGE**

## **OVERVIEW**

### **OBJECTIVE**

The Internal Audit Department conducted a review of the County Executive Office/Human Resources/Employee Benefits Division (Employee Benefits) for the purpose of evaluating internal controls and whether they are functioning adequately in the area of cash receipts and cash disbursements to ensure:

- ◆ Cash receipts are properly collected, recorded, deposited, and reconciled.
- ◆ Cash receipts are adequately safeguarded to minimize occurrence of loss or theft.
- ◆ Cash disbursements are authorized, accurate, supported and processed timely in accordance with management's authorization.

### **BACKGROUND**

Employee Benefits provides a comprehensive and competitive benefits package to County employees by offering a variety of benefit programs, such as five different health plans, health and dependent care reimbursement accounts, Employee Assistance Program, Deferred Compensation Program, , etc. They also provide dental, life insurance, Accidental Death and Dismemberment (AD&D) insurance and salary continuance benefits for a portion of County employees. The five health plans consist of three self-funded Preferred Provider Organization plans (PPO) and two Health Maintenance Organization plans (HMO). The enrollment to any plan is processed in the County Accounting and Personnel System (CAPS)/Advantage Human Resources System (AHRS). The employees' shares of benefit costs are deducted through the County payroll process.

Cash receipts processed by Employee Benefits are primarily for health insurance premiums paid by employees on family leave, leave of absence (LOA), retirees, or separated employees qualifying under the Consolidated Omnibus Budget Reconciliation Act (COBRA) provision, and for refunds of claims. Employee Benefits collect and process the cash receipts and deposits the monies with the County Treasury. The Deposit Order is submitted to the Auditor-Controller for recording into the CAPS/Advantage Financial System (AFNS). The total cash receipts processed during the calendar year ended 12/31/2001 was approximately \$4.5 million.

Cash disbursements processed by Employee Benefits primarily include premiums for the HMO plans, life, and disability insurance; claims (medical, dental, prescription, salary continuance); flexible spending accounts (health and dependent care reimbursement); third party benefit administrator's service fees; and employee benefits consultant fees. Employee Benefits prepares payment requests, reviews invoices, authorizes payments, and submits them to the Auditor-Controller's office where the actual payment is disbursed. The self-insured medical and dental claims payments are paid to the third party administrator through the County Treasury using zero-balance account (ZBA), and Employee Benefits prepares a Journal Voucher to record these payments. The total cash disbursements processed by Employee Benefits was approximately \$103.8 million for the calendar year ended 12/31/2001.

### **SCOPE**

Our review was limited to cash receipts and cash disbursements occurring between January 1, 2001 and March 31, 2002. Our review included inquiry, auditor observation and testing of relevant

## APPENDIX: MANAGEMENT'S RESPONSE (con't)

documentation for the purpose of assessing the adequacy of internal controls over cash receipts and cash disbursements processed by Employee Benefits.

Our review did not include an evaluation of the CAPS information systems or system controls used in its cash receipting and cash disbursing processes or the controls in the Auditor-Controller's Claims & Disbursing Section. We did not review the benefit enrollment or payroll deduction processes, or the third party administrators' cash handling, claims review, and payment processes.

Billing and collection of LOA and COBRA premiums is currently administered by Delta Health Systems under an existing contract. Starting January 1, 2003 billing and collection of LOA and COBRA premiums will be included in the County's contract with Mellon HR Solutions for benefits self service administration. . Our recommendations pertaining to monitoring the third party administrator's collections and invoice review (Report Items IV. and VI.) would also be applicable to the new administrator.

### CONCLUSION

It is our opinion that internal controls over cash receipting and cash disbursing are generally adequate for Employee Benefits to ensure cash receipts are properly collected, recorded, deposited, and safeguarded, and cash disbursements are properly authorized, accurate, supported and processed timely in accordance with management's authorization. It should be noted that Employee Benefits has been responsive to our observations and recommendations and started implementing some of the recommendations during our fieldwork. Although our testing did not disclose significant problems within the areas of cash receipts and cash disbursements we reviewed, we did observe the following areas where internal controls should be enhanced:

- I. Accountability Over Cash Receipts
- II. Physical Safeguards
- III. Reconciliation
- IV. Monitoring Premium Collection
- V. Special Use Fund
- VI. Invoice Review

Our observations and recommendations are discussed in the Observations, Recommendations and Management Responses section of this report.



**OBSERVATIONS, RECOMMENDATIONS AND MANAGEMENT RESPONSES**

**I. Accountability Over Cash Receipts**

Accountability over cash receipts should be established when monies are initially collected, and when transferred between employees during the collection and deposit process. This internal control practice helps ensure that all monies received are completely and properly deposited. We found certain controls were not in place and should be added to strengthen accountability over cash receipts.

1. Establish initial collection records by preparing a list of mail payments upon receipt by the employee opening the mail. This will also help management monitor whether cash receipts are deposited timely and accurately.
2. Stamp-endorse checks immediately upon opening the mail.
3. Ensure cash receipts transferred between employees are verified in the presence of both employees and the transfer of accountability is documented in writing.
4. Maintain a listing of payments received and not deposited for inclusion in the reconciliation of collection records to deposits.

**Recommendation No. 1**

Employee Benefits management take additional measures to ensure accountability is properly established during the collection and deposit process by preparing initial collection records, stamp endorsing checks immediately upon receipt, documenting transfer of accountability, and maintaining records of monies not deposited.

**Employee Benefits Response:**

**Concur**

Employee Benefits has now implemented all 4 of the recommended controls noted in Recommendation No. 1 above.

**II. Physical Safeguards**

Assets such as cash receipts must be safeguarded against unauthorized acquisition, use, or disposition. Access controls help to safeguard these assets. The following are areas where controls can be enhanced to improve the physical safeguarding objective.

1. Cash receipts were kept in unlocked cash box in an unlocked file cabinet drawer.
2. Access to the key to the file cabinet where cash receipts are stored was not restricted to appropriate employees.

**Recommendation No. 2**

Employee Benefits management ensures controls are in place to safeguard cash receipts by keeping access to the monies restricted and cash safeguarded until they are deposited in the treasury.

**Employee Benefits Response:**

Concur.

The cash box has been put in a locked cabinet drawer, and there are only two employees that have key access to the drawer, the person performing the deposits, and the Accounting Manager.

**III. Reconciliation**

Reconciliation is a comparison of one set of data to another, identifying and investigating differences, and taking corrective action when necessary to resolve those differences. This internal control activity helps ensure the accuracy and completeness of transactions. Reconciling monthly general ledger reports to departmental subsidiary records is an example of reconciling one set of data to another.

Employee Benefits uses trust funds to accumulate and disburse insurance premiums for HMO plans and Sheriff insurance plans (Fund 305), and for life insurance, and accidental death and dismemberment insurance (Fund 304). The following are areas where additional controls should be implemented:

1. Reconciliation of all validated Deposit Orders to collection records and to the general ledger should be performed monthly and documented. Differences should be investigated and resolved monthly.
2. Payment requests (e.g. Request for Check, invoice payment, electronic fund transfer) submitted to A-C should be reconciled monthly to the County financial reports (e.g. General Ledger, Expense to Budget Report) to ensure they were processed accurately in the financial system.
3. Trust funds 304 & 305 are not being reconciled to the General Ledger. Employee Benefits solely monitors the balances in the funds for reasonableness. We were informed that reconciling the funds would be difficult due to numerous automated payroll entries recorded into the funds and Employee Benefits not having access to support documentation for those automated entries. Efforts made in the past to reconcile the automated entries have not been successful.

In our opinion, there should be a reconciliation of fund deposits and payments to County financial records with some reliance being placed on the automated entries. While reconciliation is the objective, in the interim, the trust fund balances should be monitored to ensure they are adequate to meet the health and benefit plan disbursements.

**Recommendation No. 3:**

Employee Benefits management takes appropriate measures to reconcile deposits and payments to financial reports monthly to ensure accuracy and completeness. Also, measures should be considered to ensure accuracy and completeness of trust fund activities and balances are adequate to meet the health and benefit plan obligations.

**Employee Benefits Response:**

Concur.

Employee Benefits will develop appropriate procedures to verify payments and deposits against the monthly General Ledger to ensure accuracy and completeness. This procedure will be developed and implemented by February 28, 2003. Employee Benefits will gladly meet with

## APPENDIX: MANAGEMENT'S RESPONSE (con't)

representatives of the Internal Audit Department to discuss their recommendation for the method of ongoing reconciliation of the Trust Funds. In the meantime, Employee Benefits will continue to monitor the monthly balance of the Trust Funds to ensure they reflect required funding levels.

### IV. Monitoring Premium Collections

Employee Benefits contracts with a third party administrator (Delta Health Systems) to administer the billing and collection of insurance premiums for LOA and COBRA. Employee Benefits receives a check monthly from the administrator for the premiums collected. The administrator sends a spreadsheet summarizing the total premiums collected applicable to each health plan by type of collection, such as Family Leave, LOA, and COBRA. All of collections are paid to the County except for the HMO premium collected from the COBRA participants. They are sent directly to the two HMO carriers – Kaiser Permanente and CIGNA. The payment amounts are also included in the spreadsheet summary.

When a third party such as Delta performs a business process, monitoring controls become important to ensure the control objective is met. We noted the following areas where monitoring controls should be improved to ensure correct amounts are received:

1. Employee Benefits should receive a detail report from the administrator to verify the accuracy of cash receipts summary spreadsheet. This could have detected an error made by administrator where cash receipts were overpaid to the County by \$15,438 for the February 2002 collection.
2. A difference often exists when the administrator's check total is compared to the grand total of each health plan's premium amounts collected. This variance pertains to the difference between the COBRA HMO collection and amount paid to the HMO carriers where the collected amount is greater. This excess is included in the administrator's monthly check. Employee Benefits resolved the difference by allocating it between the two HMO carriers (one-third Kaiser and two-thirds CIGNA) and depositing it as a COBRA premium. However, there was no support for this allocation method. Employee Benefits should resolve the difference with adequate investigation and supporting documentation submitted by the administrator. Documentation such as administrator's system report supporting the spreadsheet amounts will help to identify the difference so that actual overages are calculated.
3. Employee Benefits provides the administrator a list of employees on Family Leave, LOA, and COBRA to help process billings and collections. The administrator updates the list noting the amount collected and sends it back to Employee Benefits. Employee Benefits should reconcile the updated list to the actual cash receipts to ensure appropriate amounts are received.

#### Recommendation No. 4:

Employee Benefits management take appropriate measures to monitor cash receipts collected by the administrator for accuracy and completeness, and resolve any differences with adequate research and support documentation.

**Employee Benefits Response:**

Concur.

Employee Benefits now verifies supporting documentation for the cash receipts spreadsheet provided with the monthly remittance to the County. Proper actions have been taken to correct the overpayment to the County. In addition, the administrator has modified its spreadsheet to allocate appropriately to each health plan the exact difference between premium paid and premium collected. The administrator still performs the calculations by staking the difference between the amount collected and the amounts paid to COBRA HMO carriers, however there is no longer a need for an allocation of one-third to Kaiser and two-thirds to CIGNA. We now know exactly how much to allocate to each plan. Lastly, starting in January 2003, Employee Benefits will implement a reconciliation process with the new administrator to reconcile premiums collected to reports of those in a billing status for COBRA, Leave of Absence, or Family Leave. This new procedure will be finalized by March 31, 2003.

**V. Special Use Revolving Fund**

Employee Benefits maintains a special use revolving fund with an authorized amount of \$50,000 for the purpose of paying salary continuance to management and attorney employees. Employee Benefits controls the special use bank account and receives monthly bank statements showing activity in the fund. A third party administrator (Standard Insurance) draws from the fund via electronic fund transfers and provides support documentation to Employee Benefits for the claims paid. Employee Benefits replenishes the account monthly or when the balance is below \$20,000.

**A. Bank Reconciliation**

Employee Benefits did not prepare a formal reconciliation between the bank statement and the revolving fund. Employee Benefits did not maintain a record showing all activities in the account, which would help in the monthly bank reconciliation. An analysis of disbursements based on the monthly bank statement and administrator's supporting documents is prepared to support the payment request with the Auditor-Controller, but it only included the disbursements and not the deposits or credits into the account.

**Recommendation No. 5a:**

Employee Benefits establish a register recording complete account activities and prepare a monthly bank reconciliation to ensure that all monies are accounted for and identified. Any differences should be investigated, resolved and documented.

**Employee Benefits Response:**

Concur.

Employee Benefits has developed a reconciliation report and records weekly balances from the bank, so that differences will be identified and resolved on a monthly bases.

**B. Fund Reconciliation**

Employee Benefits did not reconcile the special use revolving fund to the authorized fund amount. Funds should be reconciled monthly to the authorized amount to account for the

**APPENDIX: MANAGEMENT'S RESPONSE (con't)**

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usage of the funds. Our testing revealed that the actual funded amount exceeded the authorized amount by an average of \$2,800.

**Recommendation No. 5b:**

Employee Benefits management should perform the fund reconciliation monthly and identify and resolve the differences appropriately, and limit the fund to the established \$50,000.

**Employee Benefits Response:**

Concur.

We are developing procedures so that the fund will be reconciled on a monthly basis to prevent an excess in the balance. However because salaries have increased over the years, \$50,000 is no longer sufficient to fund the payments of salary continuance for County managers and attorneys therefore Employee Benefits will work with Auditor Controller staff to investigate increasing the fund limit to an appropriate amount. A procedure will be implemented by March 31, 2003.

**VI. Invoice Review**

Invoices from third party administrators should be reviewed to ensure the accuracy in the number of participants, rates, calculations, and correct account coding. Employee Benefits pays service fees to the third party administrator (Delta Health Systems). Service fees are based on a rate per eligible participant. We noted that the total eligibility number on the invoice was not directly verified to Employee Benefits departmental records for accuracy. Our testing of four invoices disclosed the total eligibility number on the invoices were fewer than Employee Benefits' report total by a small variance, resulting in underpayments.

**Recommendation No. 6:**

Employee Benefits management ensure all information on third party administrator's invoices are verified for accuracy.

**Employee Benefits Response:**

Concur.

Starting January 1, 2003 invoices to vendors for fees based on enrollment numbers will be paid directly from reports produced by the new County of Orange Benefits Center, ensuring accuracy of payments to actual enrollment.

**APPENDIX: MANAGEMENT'S RESPONSES**

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