



INTERNAL AUDIT DEPARTMENT
COUNTY OF ORANGE

*Integrity
Objectivity
Independence*

**INTERNAL CONTROL REVIEW
ORANGE COUNTY
DEVELOPMENT AGENCY
FUND EXPENDITURES**

For the Period
July 1, 2004 through December 31, 2004

AUDIT NUMBER: 2433

REPORT DATE: August 3, 2005

Audit Director:	Peter Hughes, Ph.D., CPA
Deputy Director:	Eli Littner, CPA
Audit Manager:	Alan Marcum, MBA, CPA
Senior Auditor:	Dan Melton, MT, CPA

**INTERNAL CONTROL REVIEW
ORANGE COUNTY DEVELOPMENT AGENCY
FUND EXPENDITURES**

For the Period July 1, 2004 through December 31, 2004

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**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) 834-2880


EMAIL: peter.hughes@ocgov.com
WEBSITE: www.oc.ca.gov/audit/

Transmittal Letter

Audit No. 2433

August 3, 2005

TO: Paula Burrier-Lund, Director
Housing and Community Services Department

FROM: Peter Hughes, Ph.D., CPA, Director
Internal Audit Department 

SUBJECT: Internal Control Review of Orange County Development Agency
Fund Expenditures

We have completed our audit of internal controls over agency fund expenditures of the Orange County Development Agency for the period July 1, 2004 through December 31, 2004. The final report is attached along with your responses to our recommendations.

Please note, beginning in January 2005, we implemented a more structured and rigorous follow-up audit process in response to recommendations and suggestions made by the Audit Oversight Committee (AOC) and the Board of Supervisors (BOS). As a matter of policy, our first Follow-Up Audit will now begin at six months upon the official release of the report. The AOC and BOS expect that audit recommendations will typically be implemented within six months and often sooner for significant and higher risk issues. Our second Follow-Up Audit will now begin at 12 months from the release of the original report, by which time all audit recommendations are expected to be addressed or implemented.

We have attached a Follow-Up Audit Tracking Document template. Your department should complete this template as our audit recommendations are implemented. When we perform our Follow-Up Audit approximately six months from the date of this report, we will request the completed document to facilitate our audit.

At the request of the AOC, we are to bring to their attention any audit recommendations we find still not implemented or mitigated after the second Follow-Up Audit. The AOC requests that such open issues appear on the agenda at their next scheduled meeting for discussion.

Because of these visible changes to our follow-up process, the Internal Audit Department is available to partner with all departments and agencies so that they can successfully implement or address difficult audit recommendations. Please feel free to call me should you wish to discuss any aspect of our audit report, recommendations or follow-up process.

Further, as the Director of the Internal Audit Department, effective December 14, 2004, I make a monthly audit status presentation to the BOS where I detail any significant and material audit findings released in reports during the prior month and the status of audit recommendations implementations as disclosed by Follow-Up Audits. Accordingly, the results of this review will be included in a future summary to the BOS.

Additionally, we will be submitting a Customer Survey of Audit Services to you shortly. Please complete the survey and return it to Renee Aragon, Executive Secretary, Internal Audit Department. We appreciate the courtesy and cooperation of your staff during our audit.

Attachment

Other recipients of this report:

- Members, Board of Supervisors
- Members, Audit Oversight Committee
- Thomas G. Mauk, County Executive Officer
- David Sundstrom, Auditor-Controller
- William D. Mahoney, Deputy CEO/Government and Public Services
- Paul Lanning, Program Manager, Orange County Development Agency, HCS
- Larry Stansifer, Chief of Community Services, HCS
- Mike Montijo, Accounting Manager, OCDA/Accounting Services
- Foreman, Grand Jury
- Darlene J. Bloom, Clerk of the Board of Supervisors



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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) 834-2880

EMAIL: peter.hughes@ocgov.com
WEBSITE: www.oc.ca.gov/audit/

INTERNAL AUDITOR'S REPORT

Audit No. 2433

August 3, 2005

Paula Burrier-Lund
Housing and Community Services Department
1770 N. Broadway
Santa Ana, CA 92706

We have completed a audit of internal controls over agency fund expenditures for the Orange County Development Agency (OCDA). The audit period was from July 1, 2004 through December 31, 2004. Our audit 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 area noted above. We believe our audit provides a reasonable basis for our opinion.

Management of OCDA is responsible for establishing and maintaining a system of internal controls for program operations, while the County's Auditor-Controller (A-C) is responsible for establishing and maintaining an appropriate system of internal controls for the accounting functions. 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. S-2 – *Internal Control Systems* prescribes the policies and standards the departments/agencies should follow in establishing and maintaining internal control systems. Our audit enhances and complements, but does not substitute for, OCDA's and A-C's continuing emphasis on control activities, self-assessment of control risks and correction or mitigation of control risks identified.

Because of inherent limitations in any system of internal controls, errors or irregularities may nevertheless occur and not be detected. In addition, 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 audit made for the limited purpose described above would not necessarily disclose all weaknesses in OCDA's or the Auditor-Controller's operating procedures, accounting practices, and compliance with County policy.

Based upon our audit, it is our opinion that internal controls are generally effective to ensure agency fund expenditures are accurate, authorized, and supported in accordance with management's authorization and direction. No material weaknesses or significant issues were identified. However, we identified three reportable conditions related to internal controls that are noted in the Observations, Recommendations and Management Responses section of this report. See Attachment A for a description of report item classifications.

An expectation of the Board of Supervisors is that departments and agencies will view this report as a "lessons learned" opportunity to guide them in proactively self-assessing other similar operations. Therefore, where our observations are directly applicable, the department/agency should implement the recommendations in other funds that they find as applicable to them.

We appreciate the courtesy and cooperation extended to us by the personnel of OCDA, HCS, and Auditor-Controller. If you have any questions regarding our audit or if we can be of further assistance, please contact me directly or Eli Littner, Deputy Director at (714) 834-5899 or Alan Marcum, Audit Manager at (714) 834-4119.

Respectfully submitted,



Peter Hughes, Ph.D., CPA
Director, Internal Audit

Distribution: Pursuant to Audit Oversight Committee Procedure No. 1
Members, Board of Supervisors
Members, Audit Oversight Committee
Thomas G. Mauk, County Executive Officer
David Sundstrom, Auditor-Controller
William D. Mahoney, Deputy CEO/Government and Public Services
Paul Lanning, Program Manager, OC Development Agency, HCS
Larry Stansifer, Chief of Community Services, HCS
Mike Montijo, Accounting Manager, OCDA/Accounting Services
Foreman, Grand Jury
Darlene J. Bloom, Clerk of the Board of Supervisors

EXECUTIVE SUMMARY

OBJECTIVES

The Internal Audit Department conducted an internal control audit of the Orange County Development Agency (OCDA) to evaluate the effectiveness of internal controls over expenditures to ensure that the expenditures were accurate, valid, processed timely, properly recorded and authorized, and processed in compliance with management directives.

BACKGROUND

OCDA is an agency which operates as a legal entity separate and distinct from the County and is broadly empowered to engage in the general economic revitalization and redevelopment of the County through acquisition and development of property, public improvements, and revitalization activities. OCDA currently administers the redevelopment project know as The Santa Ana Heights Project and the Neighborhood Development and Preservation Project. OCDA utilizes bond proceeds and tax increment set-aside to rehabilitate housing, construct infrastructure and public facilities, and provide affordable housing. During our period of audit, expenditures for OCDA totaled \$2,958,785.18. In addition, OCDA maintains a notes receivable on its balance sheet for loans made for the development of low-income affordable housing projects. As of the ending of our audit period, the outstanding principal for notes receivable was \$12,157,891.82.

SCOPE

Our audit was limited to internal controls over fund expenditures for the period from July 1, 2004 to December 31, 2004. Our audit included inquiry, auditor observation, and limited testing for assessing the adequacy of internal controls over OCDA expenditures. Our audit excluded controls over cash receipts, information systems and system controls. In addition, our examination excluded the audit of internal controls of other departments that journaled expenditures to OCDA controlled funds, and our audit excluded disbursements which were not classified as expenditures, such as loans made for the development of low-income affordable housing projects or for property improvements in redevelopment project areas. These loans are classified as notes receivable and appear on OCDA's balance sheet and not treated as agency expenses.

CONCLUSION

It is our opinion internal controls over OCDA fund expenditures are effective to ensure that these disbursements are properly authorized, accurate, supported and processed timely in accordance with management's authorization and direction. No material weaknesses or significant issues were identified. However, we identified three reportable conditions related to internal controls that are noted in the Observations, Recommendations and Management Responses section of this report.



DETAILED OBSERVATIONS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

Finding No. 1

We found that the OCDA Program Manager does not receive copies of all journal vouchers from the various departments/agencies for review that are charging his fund accounts.

In order for the Program Manager to more effectively administer OCDA fund accounts, he needs to have copies of all journal vouchers (JV) originated by the various departments/agencies for his review.

Recommendation No. 1

We recommend that the OCDA Program Manager work with the various departments/agencies to establish procedures to ensure that all journal vouchers are routed to him for review.

OCDA Response:

HCS concurs. In May, Budget & Support Services staff instructed the various departments and Auditor Controller staff that prepare JVs against OCDA funds to copy the Redevelopment Program Manager on all JVs. In addition, Budget & Support Services staff will monitor monthly "Expense Budget to Actual" reports and provide list of monthly JVs to Redevelopment Program Manager to ensure he has received all OCDA JVs.

Finding No. 2

We found that OCDA does not pre-approve JV's from other departments/agencies before they are processed by Auditor-Controller's General Ledger. Pre-approval of JV's prepared by other departments who seek reimbursement from OCDA could avoid both a misclassification of an expenditure and avoid an over budget condition.

Recommendation No. 2

We recommend that OCDA pre-approve JV's, material in amount, prepared by other departments/agencies for reimbursement from OCDA for costs incurred on their behalf.

OCDA Response:

HCS concurs. RDMD is responsible for the vast majority of Journal Vouchers that affect OCDA. In March 2005, RDMD/Planning signed an MOU with HCS to coordinate billings from RDMD to HCS for reimbursement of costs incurred during code enforcement. In the RDMD section of the MOU, the following is noted: "If an increase in the program cost is unavoidable, RDMD Planning will obtain HCS approval before incurring the costs." In addition, RDMD staff met with HCS staff and agreed that any JV billings will include detail regarding staff names, hours, and job titles as well as a summary of the total budget, current costs and cost to date, to ensure that budgets are not exceeded.

Finding No. 3

We found that OCDA is not reviewing invoices for mathematical accuracy. This type of review involves recalculating and confirming the accuracy of the charges on the invoice (example: multiplying the hours time the hourly rate or footing the invoice).



A reexamination of invoices for mathematical correctness functions as a control to detect invoice and billing errors before the payment to the vendor.

Recommendation No. 3

We recommend that OCDA assign a staff person to be responsible for reviewing invoices for mathematical accuracy before the invoices are approved for payment.

OCDA Response:

HCS concurs. In April 2005, HCS's Budget & Support Services Manager instructed the Office Specialist responsible for reviewing and processing invoices, to review and check all OCDA invoices for mathematical accuracy. The Office Specialist will now initial affected invoices next to calculated charges, to signify that the charges and math have been checked for accuracy. In addition, the position approving the invoice for payment (Staff Analyst or Budget and Support Services Manager) will ensure the invoice has been initialed before approving payment.



ATTACHMENT A: Report Item Classifications

For purposes of reporting our audit observations and recommendations, we have classified audit report items into three distinct categories:

Material Weaknesses:

Audit findings that can result in financial liability and exposure to a department/agency and to the County as a whole. Management is expected to address “Material Weaknesses” brought to their attention immediately.

Significant Issues:

Audit findings that represent a deficiency in the design or operation of processes or internal controls. Significant issues do not present a material exposure throughout the County; yet generally will require more immediate attention and corrective action by management than expected with a “Reportable Condition.”

Reportable Conditions:

Audit findings that require management’s corrective action to implement or enhance processes and internal controls.



ATTACHMENT B: Housing and Community Services Management Responses



Housing & Community
Services Department
COUNTY OF ORANGE

RECEIVED
INTERNAL AUDIT DEPARTMENT
2005 JUL 29 AM 10:13

July 26, 2005

County of Orange
Attn: Peter Hughes, Ph.D., CPA
10 Civic Center Drive
Santa Ana, CA 92701

Subject: Audit Number 2433, for the period July 1, 2004 through December 31, 2004

Dear Dr. Hughes:

In response to the internal audit of the Orange County Development Agency (OCDA), dated April 20, 2005; the following are Housing and Community Services' (HCS) responses to the three findings:

Finding #1

We found that OCDA Program Manager does not receive copies of all journal vouchers from the various department /agencies for review that are charging his fund accounts. In order for the Program Manager to more effectively administer OCDA fund accounts, he needs to have copies of all journal vouchers (JV) originated by the various departments/agencies for his review.

Recommendation #1

We recommend that the OCDA Program Manager work with the various department/agencies to establish procedures to ensure all journal vouchers are routed to him for review.

HCS Response:

HCS concurs. In May, Budget & Support Services staff instructed the various departments and Auditor Controller staff that prepare JVs against OCDA funds to copy the Redevelopment Program Manager on all JVs. In addition, Budget & Support Services staff will monitor monthly "Expense Budget to Actual" reports and provide list of monthly JVs to Redevelopment Program Manager to ensure he has received all OCDA JVs.

Finding #2

We found that OCDA does not pre-approve JVs from other departments/agencies before they are processed by Auditor-Controller's General Ledger. Pre-approval of JV's prepared by other departments who seek reimbursement from OCDA could avoid both a misclassification of an expenditure and avoid an over budget condition.

Recommendation #2

We recommend that OCDA pre-approve JVs, material in amount, prepared by other departments/agencies for reimbursement from OCDA for costs incurred on their behalf.



**ATTACHMENT B: Housing and Community Services Management Responses
(con't)**

HCS Response:

HCS concurs. RDMD is responsible for the vast majority of Journal Vouchers that affect OCDA. In March 2005, RDMD/Planning signed an MOU with HCS to coordinate billings from RDMD to HCS for reimbursement of costs incurred during code enforcement. In the RDMD section of the MOU, the following is noted: "If an increase in the program cost is unavoidable, RDMD Planning will obtain HCS approval before incurring the costs." In addition, RDMD staff met with HCS staff and agreed that any JV billings will include detail regarding staff names, hours, and job titles as well as a summary of the total budget, current costs and cost to date, to ensure that budgets are not exceeded.

Finding #3

We found that OCDA is not reviewing invoices for mathematical accuracy. This type of review involves recalculating and confirming the accuracy of the charges on the invoice (example: multiplying the hours time the hourly rate or footing the invoice). A reexamination of invoices for mathematical correctness functions as a control to detect invoice and billing errors before the payment to the vendor.

Recommendation #3

We recommend that OCDA assign a staff person to be responsible for reviewing invoices for mathematical accuracy before the invoices are approved for payment.

HCS Response:

HCS concurs. In April 2005, HCS's Budget & Support Services Manager instructed the Office Specialist responsible for reviewing and processing invoices, to review and check all OCDA invoices for mathematical accuracy. The Office Specialist will now initial affected invoices next to calculated charges, to signify that the charges and math have been checked for accuracy. In addition, the position approving the invoice for payment (Staff Analyst or Budget and Support Services Manager) will ensure the invoice has been initialed before approving payment.

Please call me at (714) 480-2805 if you have any questions or need additional information.



Paula Burrier-Lund
Director

Encl: (1) Copy of Audit Number 2433

- C: Julia Bidwell
- Paul Lanning
- Dana Ohanesian
- Mike Montijo

