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INTERNAL AUDIT DEPARTMENT

COUNTY OF ORANGE

INTERNAL CONTROL REVIEW OF HEALTH CARE AGENCY CONTRACT ADMINISTRATION AND CASH DISBURSEMENTS

For the Period
May 1, 2004 through April 30, 2005

AUDIT NUMBER: 2530

REPORT DATE: October 20, 2005

Audit Director:	Peter Hughes, Ph.D., CPA
Deputy Director:	Eli Littner, CPA, CIA
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**Internal Control Review of Health Care Agency
Contract Administration and Cash Disbursements**

**For the Period
May 1, 2004 through April 30, 2005**

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Transmittal Letter

Audit No. 2530

October 20, 2005

TO: Juliette A. Poulson, Director
Health Care Agency

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

SUBJECT: Internal Control Review of Health Care Agency
Contract Administration and Cash Disbursements

We have completed an Internal Control Review of the Health Care Agency contract administration and cash disbursements processes for the period May 1, 2004 through April 30, 2005. The final **Internal Auditor's 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 no later than 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 and implemented.

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.

We have attached a Follow-Up Audit Report Form. Your agency 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 need to obtain the completed document to facilitate our review.

As the Director of the Internal Audit Department, I now make a monthly audit status presentation to the BOS where I detail any material and significant audit findings released in reports during the prior month, the implementation status of audit recommendations as disclosed by our Follow-Up Audits, any pressing audit or resource issues; as well as, respond to inquiries from the BOS. Therefore, the results of this audit will be included in a future summary to the BOS.

As always, the Internal Audit Department is available to partner with you so that you can successfully implement or mitigate difficult audit recommendations. Please feel free to call me should you wish to discuss any aspect of our audit report or recommendations.

Additionally, we will request your agency to complete a Customer Survey of Audit Services. You will receive the survey shortly after the distribution of our final audit report.

Attachment

Other recipients of this report:

Members, Board of Supervisors

Members, Audit Oversight Committee

Thomas G. Mauk, County Executive Officer

William D. Mahoney, Deputy CEO/Government & Public Services

Steve Franks, Deputy Agency Director, HCA/Financial & Administrative Services

Teri Schultz, Division Manager, HCA/Contract Development & Management

David E. Sundstrom, Auditor-Controller

Bill Castro, Assistant Auditor-Controller, Satellite Accounting Operations

Alice Sworder, Manager, HCA/Accounting Services

Foreman, Grand Jury

Darlene J. Bloom, Clerk of the Board of Supervisors



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INTERNAL AUDITOR'S REPORT

Audit No. 2530

October 20, 2005

Juliette A. Poulson, Director
Health Care Agency
405 West Fifth Street
Santa Ana, CA 92701

We have completed a review of internal controls over contract administration and cash disbursements at Health Care Agency (HCA) for the period May 1, 2004 through April 30, 2005. Our audit was performed in accordance with professional standards established by the Institute of Internal Auditors.

Management of HCA 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 of Orange Accounting Manual No. S-2 – *Internal Control Systems* prescribes the policies and standards the departments/agencies should follow in establishing and maintaining internal control systems. Our review enhances and complements, but does not substitute for, HCA's 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. 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 that the degree of compliance with the procedures may deteriorate. Accordingly, our review performed for the limited purpose described above would not necessarily disclose all weaknesses in HCA's operating procedures, accounting practices, and compliance with County policy.

Based upon our audit, **no material weaknesses were identified**. However, we did identify one area that we consider as a **Significant Issue** with four recommendations, and four other Control Findings resulting in a total of **eight recommendations** to improve controls and processes as noted in the Detailed Observations, Recommendations and Management Responses section of this report.

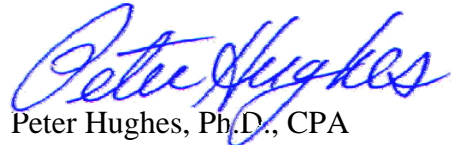
The Significant Issue relates to HCA's process for monitoring contractors, and the four Control Findings relate to the amount and timeliness of contractor payments, supporting documentation for validating contractor services, and HCA's written policies and procedures for contract administration and fiscal monitoring.

While our report indicates the specific areas of human services contracts where our observations are directly applicable, **HCA should implement the recommendations in other contract processes they find as applicable to them.** 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 or processes.

We appreciate the courtesy and cooperation extended to us by the personnel of HCA/Contracts and HCA/Accounting Services during our review. As we identified issues during the review, personnel were responsive in taking corrective actions.

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,



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
William D. Mahoney, Deputy CEO/Government & Public Services
Steve Franks, Deputy Agency Director, HCA/Financial & Administrative Services
Teri Schultz, Division Manager, HCA/Contract Development & Management
David E. Sundstrom, Auditor-Controller
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Alice Sworder, Manager, HCA/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 review of contract administration and cash disbursement processes in the Health Care Agency. The objectives of our audit were to determine whether internal controls are in place and operating to ensure:

1. Cash disbursements related to human services contracts are processed completely, accurately, timely, and in accordance with management's authorization.
2. Cash disbursements for contracted services have adequate supporting documentation to justify payments made to contractors.
3. Fiscal monitoring/site review process confirms contractor expenditures are appropriately supported and allowable in accordance with contractual requirements.

Additionally, we will identify any ineffective or inefficient processes coming to our attention during the audit.

BACKGROUND

The mission of the Health Care Agency (HCA) is to protect the optimal health of individuals, families, and diverse communities through partnerships, community leadership, assessment of community needs, planning and policy development, and public services for prevention and education. Examples of these services include food protection, hazardous waste regulation, water quality monitoring, mental health services, alcohol and drug abuse services, coordinating emergency medical care, and contracting essential medical services.

Under HCA/Financial & Administrative Services is the Contract Development & Management Division (HCA/Contracts). HCA/Contracts develops, solicits, negotiates, and administers contracts for human services with external providers of alcohol, drug abuse, mental health, public health, and medical services. Administration of these contracts includes monitoring overall compliance with the terms of the agreement, analyzing invoices in relation to contract requirements, authorizing payment on billings for disbursement by the Auditor-Controller, and preparing written documentation of any contract performance issues that should be addressed. The Auditor-Controller has an outstationed accounting section (herein referred to as HCA Accounting) that provides a variety of accounting support functions to HCA and includes processing contractor payments.

There are two types of human services contracts:

- **Actual Cost Reimbursement.** HCA pays contractor for actual and allowable business expenses as indicated in the program budget up to the maximum contract obligation.
- **Fee for Service.** HCA pays contractor for actual services provided at a pre-determined rate (generally by hourly increments, sessions, or client) up to the maximum contract obligation.

In FY 2004-2005, the inventory of HCA human services contracts was 414 agreements with a budget totaling approximately \$180 million.



HCA/Contracts reviews and authorizes the invoices received from contract providers and forwards the payment requests to HCA/Accounting who also monitor contractor payments and ensures proper payment authorization. HCA/Contracts performs on-site reviews of contractors through Annual Site Visits and Fiscal and Administrative Reviews. Additionally, for some cost reimbursement contracts, they contract with external CPA firms to perform fiscal monitoring of program expenses, as these expenditures are self-reported by contractors, and some have received \$300,000 or more in funding from the Federal government and require an audit.

SCOPE

Our audit was limited to internal controls and processes over contract administration and cash disbursements for human services contracts for the period from May 1, 2004 to April 30, 2005. Our methodology included inquiry, auditor observation, and examination and testing of relevant documentation related to Actual Cost Reimbursement and Fee for Service contracts and HCA's review and monitoring processes. Our review did not include contract development and bidding processes, agreements with County departments/agencies (cost-applied), and an evaluation of information systems used in the contract administration and cash disbursement processes.

CONCLUSION

No material weaknesses were identified. Eight recommendations are included in this report to improve processes and controls. Based upon our audit objectives, we found:

1. Controls and processes are in place to ensure cash disbursements are processed completely, accurately and in accordance with management's authorization. We noted two areas where enhancements are needed: (1) reducing the monthly contract provisional amount when the contractor's actual expenditures are less than the monthly contract payment; and (2) ensuring that contractor payments are paid within the 21 day timeframe as indicated in HCA's written procedures. These two items are considered as Control Findings (see Report Items entitled Payment Amounts and Timing of Payments).
2. For cost reimbursement contracts, contractors self-report their revenue and expenditures with their monthly invoices. While in accordance with contract requirements, we believe this supporting documentation by itself is not adequate to justify payments made to the contractors. HCA complements this process by contracting external audits and performing site reviews that additionally validate program expenditures. We note in our report where an enhancement in supporting documentation is needed to ensure HCA/Contracts verifies client referrals to the Fee for Service invoices from providers when processing payments. This item is considered a Control Finding (see Report Item entitled Supporting Documentation).
3. Fiscal and Administrative Reviews and Annual Site Visits are performed to ensure contractor expenditures are appropriately supported and allowable in accordance with contractual requirements. However, we noted where the timing, frequency and documentation of these reviews need improvement to be considered effective monitoring controls. Because site reviews are the means for HCA to verify the propriety of contractor expenditures, we consider this area as a **Significant Issue** (see Report Item entitled Fiscal Monitoring and Annual Site Visits).
4. Documented policies and procedures were not up-to-date to reflect current expectations of management and agency practices. This item is considered a Control Finding (see Report Item entitled Policies and Procedures).



DETAILED OBSERVATIONS, RECOMMENDATIONS AND MANAGEMENT RESPONSES

FISCAL MONITORING AND ANNUAL SITE VISITS (Significant Issue)

The on-going monitoring of cost reimbursement contracts by HCA principally relies on the contractor's self-reported financial results for providing human services. Before disbursing funds, HCA requires each contractor to self-report actual costs on a monthly basis by providing a Statement of Revenues and Expenditures along with the invoice for payment. After the contractor provides services within the agreed-upon term, the closeout process requires the contractor to do a final report on expenditures and revenues.

HCA/Contracts is responsible for conducting evaluations of compliance with contract requirements. To fulfill this responsibility, they developed monitoring processes to evaluate compliance with applicable laws, regulations, and contract performance. HCA's written operating policies and procedures provide guidelines for monitoring contractors. Our review of the policies disclosed that:

- **Annual Site Visits** are conducted by HCA Contract Administrators to review management control systems, inspect facilities and records, and follow-up on prior recommendations.
- **Fiscal and Administrative Reviews** are also conducted by HCA Contract Administrators to determine whether requirements were met following the completion of the contract. The goal is to conduct a Fiscal and Administrative Review of all contracts at least once every two to three years (33% to 50% of contracts within a fiscal year). A documented protocol work program with the scope of the examination is required to be completed by the review team.
- **Annual Site Visits differ from Fiscal and Administrative Reviews** in that Annual Site Visits have a broader scope and encourage an exchange of information between the provider and HCA. Financial records may be reviewed, but the evaluation will usually be for a limited purpose and is not considered a fiscal review of the contractor. Fiscal and Administrative Reviews have a greater emphasis on verifying the propriety of provider expenditures.

Because contractors self-report revenues and expenditures, we believe that HCA/Contracts cannot rely solely on supporting revenue and expenditure reports that accompany monthly invoices. It is critical that HCA/Contracts ensure adequate fiscal monitoring of the providers with an emphasis on reviewing the propriety of program expenditures. This can be accomplished by performing both Annual Site Visits and Fiscal and Administrative Reviews to determine contractor compliance, or by using external CPA firms to perform the reviews. As indicated below, we noted issues concerning the frequency and documentation of both types of HCA reviews. We consider this area to be a **Significant Issue** because of the number of contracts, the total funding provided for contracted services, and the potential risk of providers invoicing the County for unallowable expenditures.

Finding No. 1 – Frequency of Annual Site Visits

Controls and processes over Annual Site Visits did not ensure all contractors received an annual review. Our review of 20 contracts noted that in 14 instances, an Annual Site Visit was not conducted between May 1, 2004 and April 30, 2005 (Note: We were informed these site visits were performed before June 30, 2005, subsequent to the completion of audit fieldwork).



Recommendation No. 1

HCA/Contracts perform timely Annual Site Visits of provider services to determine contract compliance.

Health Care Agency Management Response:

Concur with recommendation.

Action Plan: Senior Administrators will establish an annual site visit schedule with Contract Administrators to be updated at the beginning of each fiscal year. Quarterly Contract Activity Report documentation will include the date of scheduled site visits, completion dates, and findings or required follow-up as applicable. **The FY 2005-06 annual site visit schedule has been completed.**

Finding No. 2 – Documentation of Annual Site Visits

Our review of 20 contracts noted that the Annual Site Visit files did not always contain documented information to adequately support the examination and evaluation of the contractor. We noted the policies and procedures did not provide detailed guidelines for conducting the reviews and documenting the work performed. Annual Site Visits do not have an emphasis on reviewing program expenditures; yet, they are the only site review that HCA/Contracts performs (other than an external audit if applicable) while the contract is in effect.

Recommendation No. 2

HCA/Contracts enhance its policies and procedures to provide detailed guidelines on conducting Annual Site Visits. Greater emphasis on validating program expenditures should be considered when updating the policies. In addition, results of the site visits should be consistently documented in writing to support specific Annual Site Visit objectives.

Health Care Agency Management Response:

Concur with recommendation.

Action Plan: The Policy and Procedure for Annual Site Visits will be updated to provide detailed guidelines and formats, and include preparation of the annual site visit schedule. **The revision of the policy and procedure draft is in process, to be finalized by November 2005.**

Finding No. 3 – Frequency & Timing of Fiscal and Administrative Reviews

Fiscal and Administrative Reviews were not completed in accordance with operating policies, procedures and goals. During our evaluation of Fiscal and Administrative Reviews completed in **FY 2003-2004** for services provided in the prior period, we noted that:

- HCA/Contracts personnel completed six Fiscal and Administrative Reviews. HCA/Contracts also engaged an external auditor to perform mandated audits of 32 programs receiving Federal awards and seven program expenditure reviews based on agreed-upon procedures. The 45 program audits and reviews comprised 13% of the inventory totaling 337 contracts with a budget of \$127 million. The number of Fiscal and Administrative Reviews completed is not in accordance with expectations for frequency of reviews that are stated in the written procedures and operational goals.



- The six Fiscal and Administrative Reviews that were performed appeared to have a detailed examination of program expenditures and provided recommendations for corrective actions. However, the documentation of the work performed and conclusions reached was not consistently prepared, or sometimes not included, in the fiscal review file.
- Fiscal and Administrative Reviews are conducted the year following the completion of the contract. We believe that these fiscal reviews should be conducted during the contract period to provide a more timely assessment of contract compliance and expenditures.
- A Senior Staff Analyst is responsible for conducting these reviews. HCA should consider allocating additional resources to this area for purposes of cross-training other individuals and to have a dedicated team for consistently performing the reviews.

We believe it is critical that HCA/Contracts provide timely Fiscal and Administrative Reviews of contractors. As an option, HCA/Contracts could expand its use of external auditors to provide coverage of its contractors. If HCA/Contracts continues to perform Fiscal and Administrative Reviews, controls and processes need to be strengthened in order for the reviews to be effective.

Recommendation No. 3

HCA evaluate the Fiscal and Administrative Review process and determine an appropriate level of staffing and frequency for the reviews. HCA/Contracts could determine the frequency of reviews (based on staffing resources) by prioritizing contracts by dollar amount and other risk factors. HCA should also consider performing the Fiscal and Administrative Reviews during the contract period instead of after the completion of the contract.

Health Care Agency Management Response:

Partially concur with recommendation.

Action Plan: The Policy and Procedure for Fiscal and Administrative Review will be updated to provide detailed guidelines of expectations, establish protocol for contracts exempt from the procedure, format for reports, follow-up requirements, and related timelines. **The revision of the policy and procedure draft is in process, to be completed by November 2005.**

A new centralized unit within CDM is being created using existing resources. The unit will be responsible for oversight of fiscal audit reviews, establishment of annual fiscal and administrative review schedules, approval of exemption requests with appropriate justification, coordination of external audits, monitoring compliance relative to the goal of achieving 33-50% completion annually, and provision of Contract Administrator training. **The Agency is currently recruiting for an Administrative Manager to supervise the new unit. The position is expected to be filled by December 2005.**

Comment: The recommendation to perform reviews during the contract period would not allow the audit to compare units of service performed during the contract. This is a critical factor of the review and can only be done when the fiscal year has been completed. This approach allows corrective action in future contract years, if applicable. The Agency will establish performance of timely audit reviews as a priority.



Finding No. 4 – Documentation of Fiscal and Administrative Reviews

The Fiscal and Administrative Review files did not contain adequate documentation describing the work performed to support the conclusions derived. In five of the six files, a protocol work program contained in HCA/Contract policies and procedures was not within the file documentation; instead, there were handwritten comments by the reviewer. One file did have the protocol work program included; however, several sections were not completed. Two of the six Fiscal and Administrative Reviews did not have a report prepared.

Recommendation No. 4

HCA/Contracts ensure that all required protocol work programs are utilized as intended in the Fiscal and Administrative Reviews. In addition, files should contain adequate and consistent documentation and reports to show the work performed and the conclusions reached.

Health Care Agency Management Response:

Concur with recommendation.

Action Plan: The policy and procedure will be revised to clearly define and provide a uniform format for performance of Fiscal and Administrative Reviews. In addition, a centralized unit has been established to provide better oversight and management of this critical function. **The Agency is currently in the process of recruiting for an Administrative Manager to supervise the new unit. The position is expected to be filled by December 2005.**

PAYMENT AMOUNTS

HCA Actual Cost Reimbursement contracts are based upon the provider's actual costs incurred. The payment terms are monthly at a fixed provisional installment per month. For example, a one-year contract for \$24,000 would have monthly provisional payments of \$2,000. Monthly installments are interim payments and subject to a final settlement between HCA and the contractor.

Contractors submit an Expenditure and Revenue Report to HCA in support of monthly billings. The Expenditure and Revenue Reports show the actual costs and revenues for the contractor's program. If, at any time, the contractor's Expenditure and Revenue Reports indicate that provisional amount payments exceed the actual costs of providing services, HCA may reduce payments to the contractor by an amount not to exceed the difference between the year-to-date provisional amount payments and the year-to-date actual costs incurred by the contractor.

Our testing disclosed that monthly provisional payments were not always being reduced when actual costs were less than the provisional payment amount. During our testing of 40 contract disbursements, we observed that eight payments (20%) were not reduced by the difference between the year-to-date provisional payment amount and the year-to-date actual cost. In the eight instances, the year-to-date provisional payment amount exceeded the year-to-date actual cost incurred ranging between \$10,221 and \$291,232.

HCA/Contracts management informed us that the year-to-date provisional amounts and actual costs incurred are reviewed throughout the fiscal year to determine whether subsequent payments require reduction. HCA indicated that the fixed provisional installment amounts permit contractors to strengthen their cash flow management and that adjustments are made later in the contract period. By doing so, the County is paying in advance for services not yet performed.



HCA/Contracts management indicated they would continue paying provisional amounts so as not to cause a hardship on the providers. If so, HCA/Contracts should consider classifying contracts by dollar amount and ensure that large dollar contracts have their provisional payments adjusted to actual costs on a more frequent basis.

Finding No. 5

Contractor payments were not always reduced by an amount not to exceed the difference between the year-to-date provisional amount and year-to-date actual cost incurred by the contractor.

Recommendation No. 5

HCA identify high dollar contracts and ensure that contractor provisional payments are reduced to reflect actual costs on a more frequent basis.

Health Care Agency Management Response:

Concur with recommendation.

Action Plan: A monthly Expenditure/Revenue analysis will be incorporated into each payment review, and adjustments will be made on next monthly payment for all variances in accordance with terms and conditions of contract. If necessary, variances and adjustments will be clearly documented in contract provider file. **This procedural change has been implemented.**

Policies and procedures related to provisional payments for Contract Administrators will be updated to analyze and adjust payments each month if appropriate, in accordance with the contract terms and conditions. **The update is expected to be completed by January 2006.**

TIMING OF PAYMENTS

Human services contracts state that the County should release payments no later than 21 days after receipt of the correctly completed billing form. Our testing of 40 contract disbursements disclosed that 5 payments (13%) were processed between 23 and 55 days after receipt of the contractor invoice. We noted that HCA/Accounting generally processes claims within two days upon receipt from HCA/Contracts. The delay in payments generally is from not getting the claims timely from HCA/Contracts. Untimely payments increase the risk of noncompliance with the terms of the contract.

Finding No. 6

Contractor payments were not always promptly paid in accordance with contract requirements.

Recommendation No. 6

HCA/Contracts strengthen controls to ensure timely contractor payments. HCA could revise its payment policy to reflect current practices or keep the existing policy and maintain notes in the case file for any exceptions.

Health Care Agency Management Response:

Concur with recommendation.



Action Plan: The policies and procedures will be revised to ensure processing of payments are tracked from time of invoice receipt to Auditor Controller submission, and when payments are delayed documentation will be noted accordingly in the contract provider file as to cause of any delays (i.e. missing data on invoices, calculation errors, missing signatures, lack of supporting documentation, etc.), as appropriate. **The updating of the policies and procedures has been completed and the procedural changes implemented.**

SUPPORTING DOCUMENTATION

Effective control over disbursements includes verification of provider services to determine whether invoices comply with contract provisions and authority existed to obtain the services. Documentation should be maintained to evidence authorizations and that services conform to the terms of the authorizations. An inspection of documents verifying authorization and services decreases the risk of errors and irregularities.

Our review disclosed that HCA program management inspects the records of certain fixed fee providers to verify authorized treatment and confirm services rendered. However, the results of the inspections were not forwarded to HCA/Contracts unless an exception was noted. HCA management indicated that results of future inspections would be appropriately distributed to HCA/Contracts who are responsible for approving the invoices for payment.

Finding No. 7

HCA/Contracts did not always ensure contract disbursements were supported by documented verification of services rendered from program management.

Recommendation No. 7

HCA strengthen controls to ensure officials with authority to approve invoices receive documented verification of services rendered from program management.

Health Care Agency Management Response:

Concur with recommendation.

Action Plan: The policies and procedures will be revised to require program verification of authorized services provided to support payment of invoice for Fee for Service providers. Verification of eligible services is to be clearly documented in the contract provider file. **This procedural change has been implemented.**

POLICIES AND PROCEDURES

We noted that the policies and procedures manual for HCA/Contracts was updated in May 2000, and does not reflect current practices based on existing staffing resources. For example, procedure number A.8 for *Reports* describes a monthly contract activity report identifying major issues and problems by a contract provider. However, procedure number A.16 for *Automated Quarterly Contract Activity Report* describes a quarterly distribution of a contract activity report without a superceding reference to any earlier operating statements. Another example is the procedures have operational goals for the frequency of Annual Site Visits and Fiscal and Administrative Reviews; however, as disclosed above in this report, current practices are less than the required frequency.



Finding No. 8

Documented policies and procedures were not up-to-date to reflect current expectations of management and department practices based on current staffing resources.

Recommendation No. 8

HCA review, update, and communicate policies and procedures that reflect current expectations of management and department practices.

Health Care Agency Management Response:

Concur with recommendation.

Action Plan: Contract Development and Management Policies and Procedures will be updated. The unit will perform all periodic reviews to ensure all remain current. **The updating of all policies and procedures will be completed by June 30, 2006.**



ATTACHMENT A: Report Item Classifications

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

- **Material Weaknesses:**

Audit findings or a combination of Significant Issues 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 or a combination of Control Findings that represent a significant deficiency in the design or operation of processes or internal controls. Significant Issues do not present a material exposure throughout the County. They generally will require prompt corrective actions.

- **Control Findings:**

Audit findings that require management’s corrective action to implement or enhance processes and internal controls. Control Findings are expected to be addressed within our follow-up process of six months, but no later than twelve months.



ATTACHMENT B: Health Care Agency Management Responses



*Excellence
Integrity
Service*

COUNTY OF ORANGE HEALTH CARE AGENCY

OFFICE OF THE DIRECTOR

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October 11, 2005

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

SUBJECT: Response to Draft Report on Internal Control Review of Health Care Agency
Contract Administration and Cash Disbursements Processes
Audit Number 2530

We have reviewed the draft audit report prepared by the Internal Audit Department covering HCA internal controls over contract administration and cash disbursement processes. Except as noted in our comments to Recommendation No. 3, the Health Care Agency concurs with the recommendations made in the audit and each of these have been or will be implemented.

In accordance with County procedure, we have submitted the response to the County Executive Officer for concurrence prior to submittal to Internal Audit.

Please call me at 834-6254, or Steve Franks at 834-5101, if you have any questions concerning this report.

C.C.

Juliette A. Poulson
Juliette A. Poulson, RN, MN
Director

Concurrence: *Thomas G. Mauk*
Thomas G. Mauk
County Executive Officer

JAP:sf

Attachments

cc: Thomas G. Mauk, CEO
William D. Mahoney, Deputy CEO
David L. Riley, Assistant Director, HCA
Steve Franks, HCA Financial & Administrative Services
Teri Schultz, HCA Contract Development and Management

RECEIVED

OCT 17 2005

INTERNAL AUDIT
DEPARTMENT



DRAFT REPORT
INTERNAL CONTROL REVIEW
HEALTH CARE AGENCY
CONTRACT ADMINISTRATION AND CASH DISBURSEMENTS PROCESSES
MANAGEMENT RESPONSE

Presented below are the Health Care Agency (HCA) responses to the Recommendations from the Draft Report dated August 17, 2005 regarding the Internal Control Review of Health Care Agency Contract Administration and Cash Disbursements Processes. As an outcome of this audit HCA has evaluated the effectiveness and structure of the Contract Development and Management (CDM) Unit. HCA is implementing a Central Fiscal and Administrative Support Unit to better allocate resources and improve performance outcomes within existing CDM resources to meet Agency expectations. This unit will be responsible for oversight of fiscal audit reviews, coordination of external audits, establish annual fiscal and administrative review schedule for management approval, update CDM Policies and Procedures, and provide Contract Administrator training to ensure contract provider accountability and ensure fiscal integrity is maintained to secure County resources. In addition, the current CDM Management structure will be streamlined to provide appropriate management and supervision and clearer organizational lines with an increased focus on areas of responsibility.

RECOMMENDATIONS

Recommendation No. 1

HCA/Contracts perform timely Annual Site Visits of provider services to determine contract compliance.

HCA Response:

Concur with recommendation.

Action Plan: Senior Administrators will establish an annual site visit schedule with Contract Administrators to be updated at the beginning of each fiscal year. Quarterly Contract Activity Report documentation will include the date of scheduled site visits, completion dates, and findings or required follow-up as applicable. **The FY 2005-06 annual site visit schedule has been completed.**

Recommendation No. 2

HCA/Contracts enhance its policies and procedures to provide detailed guidelines on conducting Annual Site Visits. Greater emphasis on validating program expenditures should be considered when updating the policies. In addition, results of the site visits should consistently documented in writing to support specific Annual Site Visit objectives.

HCA Response:

Concur with recommendation.

Action Plan: The Policy and Procedure for Annual Site Visits will be updated to provide detailed guidelines and formats, and include preparation of the annual site visit schedule. **The revision of the policy and procedure draft is in process, to be finalized by November 2005.**



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Recommendation No. 3

HCA evaluate the Fiscal and Administrative Review process and determine an appropriate level of staffing and frequency for the reviews. HCA/Contracts could determine the frequency of reviews (based on staffing resources) by prioritizing contracts by dollar amount and other risk factors. HCA should also consider performing the Fiscal and Administrative Reviews during the contract period instead of after the completion of the contract.

HCA Response:

Partially concur with recommendation.

Action Plan: The Policy and Procedure for Fiscal and Administrative Review will be updated to provide detailed guidelines of expectations, establish protocol for contracts exempt from the procedure, format for reports, follow-up requirements, and related timelines. **The revision of the policy and procedure draft is in process, to be completed by November 2005.**

A new centralized unit within CDM is being created using existing resources. The unit will be responsible for oversight of fiscal audit reviews, establishment of annual fiscal and administrative review schedules, approval of exemption requests with appropriate justification, coordination of external audits, monitoring compliance relative to the goal of achieving 33-50% completion annually, and provision of Contract Administrator training. **The Agency is currently recruiting for an Administrative Manager to supervise the new unit. The position is expected to be filled by December 2005.**

Comment: The recommendation to perform reviews during the contract period would not allow the audit to compare units of service performed during the contract. This is a critical factor of the review and can only be done when the fiscal year has been completed. This approach allows corrective action in future contract years, if applicable. The Agency will establish performance of timely audit reviews as a priority.

Recommendation No. 4

HCA/Contracts ensure that all required protocol work programs are utilized as intended in the Fiscal and Administrative Reviews. In addition, files should contain adequate and consistent documentation and reports to show the work performed and the conclusions reached.

HCA Response:

Concur with recommendation.

Action Plan: The policy and procedure will be revised to clearly define and provide a uniform format for performance of Fiscal and Administrative Reviews. In addition, a centralized unit has been established to provide better oversight and management of this critical function. **The Agency is currently in the process of recruiting for an Administrative Manager to supervise the new unit. The position is expected to be filled by December 2005.**



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Recommendation No. 5

HCA identify high dollar contracts and ensure that contractor provisional payments are reduced to reflect actual costs on a more frequent basis.

HCA Response:

Concur with recommendation.

Action Plan: A monthly Expenditure/Revenue analysis will be incorporated into each payment review, and adjustments will be made on next monthly payment for all variances in accordance with terms and conditions of contract. If necessary, variances and adjustments will be clearly documented in contract provider file. **This procedural change has been implemented.**

Policies and procedures related to provisional payments for Contract Administrators will be updated to analyze and adjust payments each month if appropriate, in accordance with the contract terms and conditions. **The update is expected to be completed by January 2006.**

Recommendation No. 6

HCA/Contracts strengthen controls to ensure timely contractor payments. HCA could revise its payment policy to reflect current practices or keep the existing policy and maintain notes in the case file for any exceptions.

HCA Response:

Concur with recommendation.

Action Plan: The policies and procedures will be revised to ensure processing of payments are tracked from time of invoice receipt to Auditor Controller submission, and when payments are delayed documentation will be noted accordingly in the contract provider file as to cause of any delays (i.e. missing data on invoices, calculation errors, missing signatures, lack of supporting documentation, etc.), as appropriate. **The updating of the policies and procedures has been completed and the procedural changes implemented.**

Recommendation No. 7

HCA strengthen controls to ensure officials with authority to approve invoices receive documented verification of services rendered from program management.

HCA Response:

Concur with recommendation.

Action Plan: The policies and procedures will be revised to require program verification of authorized services provided to support payment of invoice for Fee for Service providers. Verification of eligible services is to be clearly documented in the contract provider file. **This procedural change has been implemented.**

Recommendation No. 8

HCA review, update, and communicate policies and procedures that reflect current expectations of management and department practices.

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HCA Response:

Concur with recommendation.

Action Plan: Contract Development and Management Policies and Procedures will be updated. The unit will perform all perform periodic reviews to ensure all remain current. **The updating of all policies and procedures will be completed by June 30, 2006.**



ATTACHMENT B: Health Care Agency Management Responses (con't)

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Goodwin, Mike

From: Villanueva, Diane

Sent: Monday, October 17, 2005 11:04 AM

To: Riley, David; Franks, Steve; Schultz, Teri; Hughes, Peter; Aragon, Renee (Audit); Goodwin, Mike; Daniels, Leslie

Subject: Interanl Audit #2530

The County Executive Office has reviewed and approved HCA response to Audit #2530, Internal Control Review of HCA Contract Administration and Cash Disbursements Processes. By copy of this email HCA is advised to submit their response to Internal Audit. Please call me if you have any questions.

Thank you,

Diane Villanueva
County Executive Office
(714) 834-3520
(714) 834-3555 fax

10/18/2005

