

THE BOARD OF SUPERVISORS OF THE COUNTY OF STANISLAUS
ACTION AGENDA SUMMARY

Laura Hays
DEPT: Auditor-Controller

BOARD AGENDA # B-13

Urgent Routine *pk*
CEO Concurs with Recommendation YES NO
(Information Attached)

AGENDA DATE August 28, 2007

4/5 Vote Required YES NO

SUBJECT:

Acceptance of Internal Audit Reports Prepared by the Internal Audit Division of the Auditor-Controller's Office

STAFF RECOMMENDATIONS:

Accept Internal Audit Reports Prepared by the Internal Audit Division of the Auditor-Controller's Office

FISCAL IMPACT:

Auditing has become an integral element of government accountability. The internal audit function is critical to ensuring that policies and procedures adopted by the Board of Supervisors and County management are adhered to. Without an effective and comprehensive internal audit program, errors and irregularities could go undetected and the County's exposure to inefficiencies, loss and misuse of public funds would be increased.

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BOARD ACTION AS FOLLOWS:

No. 2007-680

On motion of Supervisor Mayfield, Seconded by Supervisor Monteith
and approved by the following vote,
Ayes: Supervisors: Mayfield, Grover, Monteith, DeMartini, and Chairman O'Brien
Noes: Supervisors: None
Excused or Absent: Supervisors: None
Abstaining: Supervisor: None

- 1) Approved as recommended
- 2) Denied
- 3) Approved as amended
- 4) Other:

MOTION:

Christine Ferraro

ATTEST: CHRISTINE FERRARO TALLMAN, Clerk

File No.

Acceptance of Internal Audit Reports Prepared by the Internal Audit Division of the Auditor-Controller's Office

FISCAL IMPACT (Continued):

The audits presented in the agenda item represent close to two years of services performed by the Internal Audit Division. During this time \$3,585,731 of assets and \$17,177,382 of revenue transactions were audited for required financial/compliance audits. The financial/compliance examinations consisted of examining \$18,293,468 of expense transactions along with an average of \$784,947,124 of Treasury Assets for six quarters were reviewed. Testing of internal control receipts included \$263,216 of cash receipts. In addition, \$486,716 of payroll reimbursement transactions and \$3,755,822 of purchasing card transactions were audited for compliance with the County Purchasing Card and Travel Policies. The cost to the County for services provided by the Internal Audit Division for this time period was \$640,616 in salaries. Included in the Internal Audit Division's services are engagements with no monetary value but are required by the State of California in terms of compliance with state law. The benefit of the services provided by the Internal Audit Division to the County clearly outweighs the costs for these services.

DISCUSSION:

The Internal Audit Division provides services to the County by evaluating the adequacy of controls and the efficiency and effectiveness of processes resulting in improvements for the County. The Internal Audit Division also performs, on a limited basis, financial audits of County Departments and related Agencies, along with mandated engagements and special requests.

During the course of our work we must remain objective and consistent in our treatment of the various audits and departments thereby ensuring the results of our audit reports are accurately determined. The Internal Audit Division follows professional standards promulgated by the American Institute of Certified Public Accountants (AICPA), and the Government Accounting Office (GAO).

Sixty-four engagements are presented today as follows:

- Nine financial and/or compliance audits
- Seven financial and/or compliance examinations
- Seven financial and/or compliance reviews
- Seven non-audit engagements of internal controls over cash receipts
- One non-audit engagement of internal controls over cash receipts and disbursements
- Twenty-one payroll reimbursement engagements
- Twelve purchase card engagements

Additional Work Performed

The Internal Audit Division completed seven audits for Agencies either having separate governing bodies or were presented to the Board of Supervisors at an earlier date. These seven audits were completed in addition to the sixty-four engagements presented in this report. The seven audits are listed below.

Acceptance of Internal Audit Reports Prepared by the Internal Audit Division of the Auditor-Controller's Office

DISCUSSION (Continued):

The Internal Audit Division has completed two financial/compliance audits of another Agency that was presented to their Governing Committee. These audits consisted of the Stanislaus Drug Enforcement Agency as of June 30, 2003 and a separate audit report as of June 30, 2004.

Two financial/compliance audits were completed for the Children and Families Commission as of June 30, 2005 and a separate report issued as of June 30, 2006. Both of these audits were presented to the Commission by Management.

The Redevelopment Agency financial/compliance audit as of June 30, 2006 was completed by the Internal Audit Division and presented to the Board of Supervisors by the Agency on December 12, 2006.

The Internal Audit Division has also completed the draft financial/compliance reports for the Consolidated Emergency Dispatch Agency for one audit report combining the years ending June 30, 2004 and 2005 and a separate audit report for the year ending June 30, 2006. These audit reports were presented to the Agency's Board of Commissioner's in May 2007.

External Quality Control Review

The Internal Audit Division underwent an External Quality Control Review for engagements completed during calendar year 2005. The review was conducted by the National Association of Local Government Auditors (NALGA). The review report determined the Internal Audit Division's internal quality control system was operating effectively to ensure reasonable compliance with Government Auditing Standards. The review report also included management comments to further strengthen the internal quality control system. The review report and management comments are included in this presentation for your review.

Financial/Compliance Audits

Eight of the nine financial/compliance audits were conducted in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards. One audit which was conducted in accordance with auditing standards generally accepted in the United States of America. An unqualified opinion was rendered for all nine audits.

Community Services Agency Program Services and Support Fund's Child Development Program

Financial Statements for the year ended June 30, 2005 along with a separate audit report for the year ended June 30, 2006. These annual audits are required by the California Department of Education per California Government Code Section 18071. In addition to the auditing standards cited above both these audits required additional analysis as required by the U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and the *Audit Guide for Audits of Child Development and Nutrition Programs*. The June 30, 2005 audit report noted opportunities for strengthening internal controls communicated to management in the form of a management letter. The June 30, 2006 audit noted no management comments.

Office of the District Attorney Automobile Insurance Fraud Grant Financial Statements for the year ended June 30, 2005 along with a separate audit report for the year ended June 30, 2006. These annual audits are required by the California Department of Insurance. Separate management comments were issued

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DISCUSSION (Continued):

along with the audit report for both audit years as an opportunity for strengthening internal controls.

Office of the District Attorney Worker's Compensation Fraud Grant Financial Statements for the year ended June 30, 2005 along with a separate audit report for the year ended June 30, 2006. These annual audits are required by the California Department of Insurance. Separate management comments were issued along with the audit report for both audit years as an opportunity for strengthening internal controls.

Abandoned Vehicle Abatement Program Schedule of Revenues, Expenditures and Balance of Abandoned Vehicle Abatement Funds Financial Statements of the year ended June 30, 2005 along with a separate audit report for the year ended June 30, 2006. These annual audits are required California Government Code Section 6505 and administered by the California Highway Patrol. We noted no matters as opportunities for strengthening internal controls.

Stanislaus Emergency Dispatch County Radio Maintenance Fund Financial Statements for the years ending June 30, 2004 and 2005. This audit was requested to be performed by Management of the Consolidated Emergency Dispatch Agency who managed the fund during the period under audit. We noted no matters as opportunities for strengthening internal controls.

Financial/Compliance Examinations

Treasury Oversight Committee Compliance Examination for the year ended June 30, 2005 along with a separate report for the year ended June 30, 2006. This engagement is required by California Government Code Section 27134 on an annual basis to guarantee compliance with such code by the County Treasury Department. The June 30, 2005 engagement was performed in accordance with standards established by the American Institute of Certified Public Accountants while the June 30, 2006 engagement was performed in accordance with standards established by the American Institute of Certified Public Accountants and Government Auditing Standards.

Endowment Investment Fund Compliance Examination for the year ended June 30, 2005 along with a separate report for the year ended June 30, 2006. This engagement is required by the Investment Policy Securitization of the Tobacco Industry's Master Settlement Agreement and investment provisions to assure compliance with the investment policy as required by California Government Code Section 53601. The June 30, 2005 engagement was performed in accordance with standards established by the American Institute of Certified Public Accountants while the June 30, 2006 engagement was performed in accordance with standards established by the American Institute of Certified Public Accountants and Government Auditing Standards.

Property Tax Administration Fee Cost Calculations for the years ended June 30, 2004, 2005 and 2006 as separate reports for each year. The annual engagement is performed at the request of the Auditor-Controller in order to ensure an independent review of the appropriations and calculations listed in the report. The June 30, 2004 engagement was conducted in accordance with standards established by the American Institute of Certified Public Accountants and the June 30, 2005 and 2006 engagements was

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DISCUSSION (Continued):

performed in accordance with the American Institute of Certified Public Accountant and Government Auditing Standards.

Financial/Compliance Reviews

Assessor's AB589 Workload and Valuation Data for the year ending October 31, 2005. This engagement is required by Section 9 of the Agreement for State-County Property Tax Administration Program. We verified the grant funds were spent in accordance with the program requirements within a reasonable amount.

Six Quarterly review of the Stanislaus County Treasurer's Statement of Assets in the Treasury for the quarters ending December 31, 2004, March 31, 2005, September 30, 2005, December 31, 2005, March 31, 2006, and September 30, 2006. Review reports for the quarter ending June 30th are not issued by the Internal Audit Division as the annual audit report for the entire County as of that date includes the Treasury asset amounts. These quarterly reviews are required under California Government Code Section 26920 and the Stanislaus County Investment Policy and were performed in accordance with standards established by the American Institute of Certified Public Accountants. Based on our reviews the assets held in the Treasury are in conformity with State Code and the County Policy.

Internal Controls Over Cash Receipts Engagements

We have identified twelve departments which we consider to have cash receipt transactions that are high risk. High risk was determined either by the volume and/or nature of these transactions and also if remote locations were involved. Various dates exist for the seven engagements of internal controls over cash receipts presented. We documented the procedures in place and identified control weaknesses and process improvements. We then tested on a sample basis the procedures and controls documented to ensure operations existed and were effective.

Major findings of these engagements consisted of the following:

- Too many employees have access to the safe, locked cash drawer and in some cases an unlocked box is used to hold the cash. In addition, in some departments, keys to safes are kept in unlocked drawers and the safe itself is kept unlocked during the day allowing anyone access to the safe.
- We noted in some cases weekly deposits are not made per written department procedures. In addition, one department does not prepare a deposit until \$30,000 has been accumulated, thereby increasing risk of theft and additionally a lack of available funds for expenditures or investment.
- Lack of segregation of duties.
- Lack of reconciling numerical sequence documents such as invoices, manual receipt books (multiple receipt books used).

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DISCUSSION (Continued):

- Duplication of work either through multiple software programs used, manual documents prepared when the software can generate these documents, numerous counts of the same monies, same information reported on different documents.
- Lack of sufficient written procedures or no written procedures.
- Checks are not restrictively endorsed immediately upon receipt.

The Internal Audit Division is continuing to work on this series of audits documenting and testing the cash receipts procedures and controls currently in place for the remaining five departments considered to be high risk.

Internal Controls Over Cash Receipts and Cash Disbursement Engagement

The period of this engagement was July 1, 2003 through June 30, 2005. The engagement was performed due to a request made by the Chief Executive Office which resulted from a Grand Jury investigation of complaints regarding various issues with the department, one of which was the accounting practices within the department. We documented the procedures in place and identified control weaknesses and process improvements. We then tested on a sample basis the procedures and controls documented to ensure operations existed and were effective.

Major findings of this engagement consisted of the following:

- Lack of segregation of duties.
- Too many employees have access to the safe, locked bank bags and blank check stock.
- Temporary employees were assigned cash handling duties.
- Six employees are authorized signers on the two outside checking accounts. Some of the employee's job duties include handling cash which is incompatible with being a signer on a checking account. There are also too many signers on the checking accounts.
- 17% of the deposits tested were not made on a daily basis.
- We noted various issues with the department's receipting system.

Payroll Reimbursement Engagements

The period of these engagements under review was July 1, 2002 through June 30, 2003. The payroll reimbursement transactions were reviewed 100% for this period except for four departments which were reviewed using a sample population. These engagements were based on compliance with the County Travel Policy and Payroll Reimbursement Requirements.

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DISCUSSION (Continued):

Our engagement procedures included but were not limited to determining the following:

- Supporting documentation exists for the reimbursements.
- Appropriate approval was obtained and documented for each reimbursement.
- Determination of duplicate payments through the payroll reimbursement process and the purchasing card process.
- If the department has their own policy, determine if the policy is more stringent than the County policy and if so determine if the department complies with their policy.
- Identify any items that may be an abuse of County policy such as the use of luxury hotels.

We have completed a review of payroll reimbursements for 25 departments out of a total of 30 departments. During the prior presentation 4 of the completed engagements were presented. The total number of transactions and amounts for the 21 departments completed for this presentation is 22,329 transactions and \$486,716. Three departments of the 21 departments presented today had no major findings. Of the 5 remaining engagements not completed as of this presentation, fieldwork has been performed and we are in the process of reviewing the results of the fieldwork and writing the reports.

Major findings for the 21 engagements currently presented:

- We noted missing signatures on time cards as follows, 1,111 missing supervisor signatures, 171 missing employee signatures and 344 missing signatures from both the supervisor and the employee. In addition to the missing signatures we also noted 154 time cards were not dated by the supervisor and employee.
- We noted 356 missing travel authorizations to support supervisorial approval, and clear business purpose.
- We found 2,283 missing destination codes. Destination codes help to support a clear County business purpose. Based on the employees job duties the reimbursements were related to County business.
- We also noted 226 transactions without a clear business purpose documented.

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DISCUSSION (Continued):

- Two departments had significant mileage reimbursements for 6 employees who regularly travel as part of their job duties. One department spent over \$8,000 in mileage reimbursements for two employees and the other department spent \$4,000 for 4 employees. One department performed an analysis of the most cost effective and efficient mode of transportation and concluded that employee reimbursement was the best method. The other department now has their employees either receiving a vehicle allowance or using County vehicles assigned to their department.

In summary the findings listed above primarily relate to lack of documentation to support the reimbursements and proper approval of reimbursements as required by the Travel Policy.

We have begun the next series of payroll reimbursement engagements which covers the period July 1, 2004 through June 30, 2005. We will then continue to perform the engagement every other fiscal year. The transactions reviewed are based on a sampling population of approximately 30% of total reimbursements.

Purchase Card Engagements

The Board of Supervisors requested engagements to review employee purchasing card transactions to ascertain the purchases were made in compliance with the County Purchasing Card Policy. The period under review was July 1, 2002 through June 30, 2003. The purchase card transactions were reviewed 100% for this period.

Our engagement procedures included but were not limited to determining the following:

- Supporting documentation exists for the purchases.
- Examine the department's reconciliation of the monthly purchasing card statement.
- The purchasing card transactions are considered County business.
- Review purchasing card authorization for each card.
- If the department has their own policy, determine if the policy is more stringent than the County policy and if so determine if the department complies with their policy.
- Identify any items that may be an abuse of County policy such as purchase of personal items.

We have completed a review of purchase card transactions for 30 departments out of a total of 33 departments. During prior presentations 18 of the completed engagements were presented. The total number of transactions and amounts for the 12 departments completed for this presentation is 18,848 transactions and \$3,755,882. One department of the 12 departments presented today had no major findings. Of the 3 remaining engagements not completed, fieldwork has been performed and we are in the process of reviewing the results of the fieldwork and writing the reports.

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DISCUSSION (Continued):

Major findings for the 12 engagements currently presented:

- We noted 50 transactions that were incurred that were inappropriate County expenditures resulting in \$4,338 of additional costs to the County. The types of transactions were flowers, hotel accommodations, rental car upgrades, valet parking, personal phone calls and movie rentals. The departments obtained \$1,539 in reimbursements from County employees. Some departments attempted to collect further reimbursements however many of the employees involved have since left County employment.
- We noted 85 missing travel authorizations to support supervisorial approval, and clear business purpose.
- We also noted 73 transactions for in-county meals in the amount of \$3,947 were associated with department meetings and/or training sessions for one department.
- We noted 3 transactions were unresolved disputed items in the amount of \$1,286.

Of the transactions tested 306 or 1.62% of the total transactions were considered major findings. In summary, the major findings primarily consisted of departments lacking sufficient procedures and controls, in some cases, to monitor the appropriateness of the purchase card transactions.

Currently, the division has completed engagement fieldwork for 23 departments out of a total of 33 departments for the next series of purchase card engagements. The next series of engagements consists of combining Fiscal Year's 2003-2004 and 2004-2005 in to one report, per department. Also, we are testing on a sample basis of roughly 30% to 35% rather than 100% as in the Fiscal Year 2002-2003 engagements mentioned above.

Policy Issue

Per Government Section Code 26833, the Board of Supervisors shall have the power to require that the County Auditor-Controller shall audit the accounts and records of any department, office, board or institute under its control.

The Internal Audit Division helps to determine whether financial and operating information is accurate and reliable; risks are identified and minimized; policies and procedures are followed; resources are used efficiently and effectively; and objectives are effectively achieved.

The work performed by the Internal Audit Division provides accountability to the Board of Supervisors and the public. In addition, the work performed by the Internal Audit Division is in alignment with the Board's priority of ensuring efficient delivery of public services.

Acceptance of Internal Audit Reports Prepared by the Internal Audit Division of the Auditor-Controller's Office

DISCUSSION (Continued):

The division is committed to issuing reports on a timely basis. In order to continue to improve on the timing of the issuance of reports and the overall efficiency of the division, the Internal Audit Division presentations to the Board of Supervisors will be performed on a bi-annual basis.

STAFFING IMPACT:

The Internal Audit Division currently consists of the Internal Audit Manager and four Internal Auditors. At this time, three of the five employees are Certified Public Accountants. We also employ a full time temporary worker to help with the demands of the division giving us a total of six Internal Auditors. During the past few years the division has experienced significant recruitment challenges and until recently was not fully staffed.

ATTACHMENTS AVAILABLE
FROM PUBLIC ACCESS