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Internal Control Audit:

PUBLIC DEFENDER – REVOLVING FUNDS PROCESS

For the Year Ending February 28, 2011

High Impact Audit

During the audit period, the Public Defender expended approximately \$1.5 million via its Revolving Funds. The Public Defender maintains three separate revolving funds in the amounts of \$250,000, \$50,000 and \$5,000.

We audited the Public Defender Revolving Funds Process and determined that internal controls are in place to ensure revolving funds are adequately safeguarded; transactions are processed in accordance with County policy; and transactions are properly authorized, and recorded completely, accurately and processed timely.

However, we did identify two (2) Control Findings regarding the resolution of long-outstanding reconciling items on bank reconciliations and the frequency of revolving funds replenishment requests.

AUDIT NO: 1053 REPORT DATE: JUNE 16, 2011

Director: Dr. Peter Hughes, MBA, CPA, CIA
Deputy Director: Eli Littner, CPA, CIA
Senior Audit Manager: Alan Marcum, CPA, CIA
Audit Manager: Michael Dean, CPA, CIA
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RISK BASED AUDITING

GAO & IIA Peer Review Compliant - 2001, 2004, 2007, 2010

American Institute of Certified Public Accountants Award to Dr. Peter Hughes as 2010 Outstanding CPA of the Year for Local Government

2009 Association of Certified Fraud Examiners' Hubbard Award to Dr. Peter Hughes for the Most Outstanding Article of the Year – Ethics Pays

2008 Association of Local Government Auditors' Bronze Website Award





GAO & IIA Peer Review Compliant - 2001, 2004, 2007, 2010

Providing Facts and Perspectives Countywide

RISK BASED AUDITING

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To access and view audit reports or obtain additional information about the OC Internal Audit Department, visit our website: www.ocgov.com/audit



Letter from Dr. Peter Hughes, CPA





Transmittal Letter

Audit No.1053 June 16, 2011

TO: Deborah A. Kwast Public Defender

FROM: Dr. Peter Hughes, CPA, Director

Internal Audit Department

SUBJECT: Internal Control Audit: Public Defender

Revolving Funds Process

We have completed an Internal Control Audit of the Public Defender Revolving Funds Process for the period ending February 28, 2011. We performed this audit in accordance with our *FY 2010-11 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and the Board of Supervisors. Our final report is attached for your review.

Please note we have a 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). Our **first Follow-Up Audit** will begin at <u>six months</u> from the official release of the report. A copy of all our Follow-Up Audit reports is provided to the BOS as well as to all those individuals indicated on our standard routing distribution list.

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 begin at <u>six months</u> from the release of the first Follow-Up Audit 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 department should complete this template as our audit recommendations are implemented. When we perform our first Follow-Up Audit approximately six months from the date of this report, we will need to obtain the completed document to facilitate our review.

Each month I submit an Audit Status Report to the BOS where I detail any material and significant audit findings released in reports during the prior month and the implementation status of audit recommendations as disclosed by our Follow-Up Audits. Accordingly, the results of this audit will be included in a future status report to the BOS.

As always, the Internal Audit Department is available to partner with your staff so that they 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 department complete a **Customer Survey** of Audit Services. You will receive the survey shortly after the distribution of our final report.

ATTACHMENTS

Other recipients of this report are listed on the OC Internal Auditor's Report on page 3.

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Public Defender Revolving Funds Process
Audit No. 1053

For the Period March 1, 2010 through February 28, 2011

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OC Internal Auditor's Report



Audit No. 1053 June 16, 2011

TO: Deborah A. Kwast

Public Defender

FROM: Dr. Peter Hughes, CPA, Director,

Internal Audit Department

SUBJECT: Internal Control Audit: Public Defender

Revolving Funds Process

Audit Highlight

We audited the Public Defender Revolving Funds Process. The Public Defender maintains three revolving funds totaling \$305,000, and for yearending February 28, 2011, expended approximately \$1.5 million.

We found that internal controls are in place to ensure revolving funds are adequately safeguarded; transactions are processed in accordance with County policy; and transactions are properly authorized, and recorded completely, accurately and processed timely. However, we did indentify two (2) Control Findings regarding the resolution of longoutstanding reconciling items on bank reconciliations and the timeliness of revolving funds replenishment requests.

OBJECTIVES

In accordance with our *FY 2010-11 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and the Board of Supervisors, the Internal Audit Department conducted an Internal Control Audit of the Public Defender Revolving Funds Process. Our audit included an evaluation of the adequacy and integrity of internal controls, testing compliance with Public Defender and County policies; and evaluating process efficiencies and effectiveness. Our audit was conducted in conformance with professional standards established by the Institute of Internal Auditors. The objectives of this audit were to ensure:

- 1. Revolving funds are adequately safeguarded.
- 2. Revolving fund transactions are processed in accordance with applicable County Accounting Manual (CAM) procedures.
- 3. Revolving fund transactions are properly authorized, and recorded completely, accurately and processed timely.

RESULTS

<u>Objective #1:</u> Controls and processes are in place to ensure revolving funds are adequately safeguarded. We noted **two (2) Control Findings** regarding the resolution of long-outstanding reconciling items on bank reconciliations and the timeliness of revolving funds replenishment requests.

Objective #2: Controls and processes are in place to ensure revolving fund transactions are processed in accordance with applicable County Accounting Manual (CAM) procedures.

OC Internal Auditor's Report



Objective #3: Controls and processes are in place to ensure revolving fund transactions are properly authorized, and recorded completely, accurately and processed timely.

See further discussion in the Detailed Findings, Recommendations and Management Responses section of this report in Findings 1 and 2. See Attachment A for a description of Report Item Classifications.

BACKGROUND

The mission of the Office of the Public Defender is to provide high quality legal representation to clients in a cost-effective manner. The Orange County Public Defender provides legal representation to those unable to afford a lawyer in criminal, juvenile, mental health and dependency cases. First established in 1944, Orange County Deputy Public Defenders, Alternate Defenders and Associate Defenders, with the support of Investigators, Paralegals and Clerical staff, provide legal representation in approximately 81,000 cases annually. The Alternate Defenders and Associate Defenders are separate subsidiary offices handling cases in which the Public Defender declares a conflict of interest.

The Public Defender maintains three revolving funds:

- 1. **\$250,000** is the authorized amount for a Special Use Revolving Fund. This fund was recently established, May 2009 to pay for confidential invoices for client expenses.
- \$50,000 is the authorized amount for general operations (Fund 100/Agency 058). Of this amount, \$40,000 is allocated for use by the Public Defender and \$10,000 is allocated for use by the Alternate Defender. This fund is used for the purposes of departmental petty cash expenditures and travel cash advances.
- 3. **\$5,000** is the authorized amount for a Delta Special Revenue Fund (Fund 15N/Agency 15N). This fund did not have any activity during the audit period, and therefore, was not included within the scope of this assignment.

During the period under review, Public Defender incurred expenditures of approximately \$1.5 million. 97% of the revolving fund expenditures were from the Special Use Revolving Fund and 3% of the revolving fund expenditures were from the general operations revolving fund.

SCOPE AND METHODOLOGY

Our audit was limited to internal controls and processes over revolving funds for the period from March 1, 2010 through February 28, 2011. Our methodology included inquiry, auditor observation, and examination and testing of relevant documentation.

OC Internal Auditor's Report



Management's Responsibilities for Internal Controls

In accordance with the Auditor-Controller's County Accounting Manual section S-2 *Internal Control Systems*, "All County departments/agencies shall maintain effective internal control systems as an integral part of their management practices. This is because management has primary responsibility for establishing and maintaining the internal control system. All levels of management must be involved in assessing and strengthening internal controls." Control systems shall be continuously evaluated (by Management) and weaknesses, when detected, must be promptly corrected. The criteria for evaluating an entity's internal control structure is the Committee of Sponsoring Organizations (COSO) control framework. Our Internal Control Audit enhances and complements, but does not substitute for the Public Defender's continuing emphasis on control activities and self-assessment of control risks.

Inherent Limitations in Any System of Internal Control

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 the degree of compliance with the procedures may deteriorate. Accordingly, our audit would not necessarily disclose all weaknesses in the Public Defenders' operating procedures, accounting practices, and compliance with County policy.

Acknowledgment

We appreciate the courtesy extended to us by the Public Defender during our audit. If we can be of further assistance, please contact me directly or Eli Littner, Deputy Director at 834-5899 or Alan Marcum, Senior Audit Manager at 834-4119.

Attachments

Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Board of Supervisors
Members, Audit Oversight Committee
Thomas G. Mauk, County Executive Officer
Steve Dunivent, Deputy CEO, Government & Public Services
Becky Juliano, Director of Administration, Public Defender
Foreperson, Grand Jury
Darlene J. Bloom, Clerk of the Board of Supervisors

Detailed Results, Findings, Recommendations and Management Responses



Finding 1 – Long-Outstanding Reconciling Items – Public Defender Bank Reconciliations

Reconciling items on bank reconciliations need to be researched and resolved timely to help ensure errors and/or irregularities are detected timely. (Control Finding)

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. The revolving funds bank reconciliations help ensure the accuracy and completeness of revolving fund transactions. County Accounting Manual (CAM) No. C-7, *Revolving Cash Fund*, requires bank checking accounts to be reconciled monthly by an independent person with no revolving fund duties. In addition, the CAM states that the bank reconciliations should be reviewed, initialed, and dated by a supervisor.

The bank reconciliations contained various long-outstanding items. The Special Use Revolving Fund reconciliation for February 2011 contained four outstanding checks dating from February 2010 through July 2010. The Public Defender reconciliation for February 2011 contained two outstanding checks dating from May 2010 and June 2010. During the audit, Public Defender staff requested a "stop payment" to be applied to the long-outstanding checks.

Recommendation No. 1

We recommend the Public Defender ensure long-outstanding items on bank reconciliations are researched and resolved timely.

Public Defender Management Response:

Concur. All long-outstanding items have been canceled. Staff has been counseled to complete bank reconciliations within 30 days of the activity.

Finding 2 – Revolving Funds Replenishment Frequency Needs to be Improved

Our testing of the Alternate Defender portion of the regular revolving fund (\$10,000 of \$50,000 Fund 100/Agency 058 revolving fund) disclosed that three replenishment requests were submitted to the Auditor-Controller in March 2011 for \$3,973.27 for transactions occurring from July 2010 through March 2011. (Control Finding)

Recommendation No. 2

We recommend the Public Defender ensure that revolving fund replenishment requests are submitted for reimbursement on a regular basis.

Public Defender Management Response:

Concur. A reminder of the procedures has been distributed to staff and staff has been counseled regarding the process. The Director of Administration will work with staff to ensure the replenishments are completed regularly.

Detailed Results, Findings, Recommendations and Management Responses



ATTACHMENT A: Report Item Classifications

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

Critical Control Weaknesses:

Serious audit findings or a combination of Significant Control Weaknesses that represent critical exceptions to the audit objective(s) and/or business goals. Management is expected to address Critical Control Weaknesses brought to their attention immediately.

Significant Control Weaknesses:

Audit findings or a combination of Control Findings that represent a significant deficiency in the design or operation of internal controls. Significant Control Weaknesses generally will require prompt corrective actions.

Control Findings:

Audit findings concerning <u>internal controls</u>, <u>compliance issues</u>, or <u>efficiency/effectiveness issues</u> 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.

Detailed Results, Findings, Recommendations and Management Responses



DENISE M. GRAGG R ASSISTANT PUBLIC DEFI

FRANK OSPINO SENIOR ASSISTANT PUBLIC DEFENDER

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ATTACHMENT B: Public Defender Management Responses

LAW OFFICES

ORANGE COUNTY PUBLIC DEFENDER

DEBORAH A. KWAST PUBLIC DEFENDER

JEAN M. WILKINSON



14 CIVIC CENTER PLAZA SANTA ANA, CA 92701-4029 (714) 834-2144 FAX: (714) 834-2729 www.pubdef.ocgov.com

June 14, 2011

TO: Peter Hughes, Ph.D., CPA, Director

Internal Audit Department

SUBJECT: Response to Internal Control Review of the Offices of the Public Defender

Revolving Funds Process Audit Number 1053

I am providing the Public Defender's response to the Internal Control Review for the Revolving Fund Process recently completed by the Internal Audit Department. Our response has been reviewed by the County Executive Office on June 14, 2011.

I would like to express my appreciation for the professionalism and support provided by the Internal Audit Department in conducting this audit.

The following are the responses to the audit report recommendations.

BANK RECONCILIATION AND REPLENISHMENT

Recommendation No. 1 Public Defender Response:

Concur. All long-outstanding items have been cancelled. Staff has been counseled to complete bank reconciliations within 30 days of the activity.

Recommendation No. 2 Public Defender Response:

Concur. A reminder of all procedures has been distributed to staff and staff has been counseled regarding the process. The Director of Administration will work with staff to ensure the replenishments are completed regularly.

Again, thank you for this opportunity to improve services within our offices.

Respectfully Submitted,

Deborah A. Kwast Public Defender

CENTRAL OFFICE | HARBOR OFFICE | JUVENILE OFFICE | MENTAL HEALTH | NORTH OFFICE | 600 W. Santa Ana Blvd. | 4601 Jambore Rd. | 341 City Drive S. | 901 Civic Center Dr. | 1440 N. Harbor Blvd. | Suite 101 | Suite 307 | Suite 300 | 1440 N. | 1470 Plvd. | 1 SOUTH OFFICE SUPERIOR 901 WEST OFFICE 00 W. Santa Ana Blvd. Suite 111 Santa Ana, CA 92701 (714) 568-4860 901 Civic Center Dr Suite 200 Santa Ana, CA 92703 5001H OFFICE 5000 Birch St. Suite 5700 Newport Beach, CA 92660 (949) 757-7660 901 Civic Center Dr. Suite 200 Santa Ana, CA 92703 4601 Jamboree Rd. Suite 101 Suite 200 Westminster, CA 92683 Newport Beach, CA 92660 Fuller on. CA Orange, CA 92868 92835 (949) 476-4888 (714) 935-7578 (714) 796-8200 (714) 626-3700 (714) 796-8100 (714) 896-7281