



Orange County Auditor-Controller Internal Audit



Internal Control Audit
OC Public Works/OC Flood
Special Revenue Funds

Year Ended April 30, 2015

Audit Number 1421
Report Date: August 8, 2016



O R A N G E C O U N T Y
AUDITOR-CONTROLLER
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Transmittal Letter

Audit No. 1421

August 8, 2016

TO: Shane Silsby, Director
OC Public Works

SUBJECT: Internal Control Audit:
OC Public Works/OC Flood Special Revenue Funds

We have completed our Internal Control Audit over special revenue funds in OC Public Works/OC Flood for the year ended April 30, 2015. Our final report is attached for your review.

I submit an **Audit Status Report** quarterly to the Audit Oversight Committee (AOC) and a monthly report to the Board of Supervisors (BOS) where I detail any critical 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 AOC and BOS.

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

Toni Smart, CPA, Director
Auditor-Controller Internal Audit Division

Attachments

Other recipients of this report:

- Members, Board of Supervisors
- Members, Audit Oversight Committee
- Eric Woolery, Auditor-Controller
- Frank Kim, County Executive Officer
- Mark Denny, Chief Operating Officer
- Jessica Witt, Deputy Chief Operating Officer
- Robin Uptegraff, Assistant Director, OCPW
- Becky Juliano, Deputy Director, OCPW Administrative Services
- Randy Dunlap, Administrative Manager II, OCPW Centralized Quality Assurance
- Jackie Cadotte, Compliance Manager, OCPW Central Quality Assurance
- Tonya Riley, Director of Satellite Accounting Operations, Auditor-Controller
- Howard Thomas, Accounting Manager III, OCPW Accounting Services
- Foreperson, Grand Jury
- Robin Stieler, Clerk of the Board of Supervisors
- Macias Gini & O'Connell LLP, County External Auditor



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OC Public Works/OC Flood
Special Revenue Funds
Audit No. 1421*

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Internal Auditor's Report

Audit No. 1421

August 8, 2016

TO: Shane Silsby, Director
OC Public Works

FROM: Toni Smart, CPA, Director
Auditor-Controller Internal Audit Division

SUBJECT: Internal Control Audit:
OC Public Works/OC Flood Special Revenue Funds

OBJECTIVES

We completed our Internal Control Audit of special revenue funds in OC Public Works/OC Flood for the year ended April 30, 2015. We performed this audit in accordance with the *FY 15-16 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and the Board of Supervisors to ensure special revenue funds are properly administered and maintained in compliance with County policy and procedures, and are utilized in accordance with fund requirements. Our audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing prescribed by the Institute of Internal Auditors. The objectives of this audit were to:

1. Evaluate if internal controls are in place to ensure special revenue fund transactions are used for specific purposes.
2. Evaluate if internal controls are in place to ensure special revenue fund transactions are valid, adequately supported, processed timely, properly recorded, and that management reviews and approvals related to receiving, disbursing, reconciling, and claiming reimbursements of OC Flood funds are performed.
3. Determine if administration of OC Flood special revenue funds is effective and efficient (e.g., no backlogs, duplication of work, benefit in automating manual process).

RESULTS

Objective 1: Our audit found that internal controls are in place to ensure OC Flood's special revenue funds are used for specific purposes, with the following exceptions. We identified **one (1) Significant Control Weakness** concerning prior year encumbrance cancellations in OC Watersheds (in County General Fund 100) not being returned to OC Flood Fund 400 (Fund 400). Also, we identified **two (2) Control Findings** pertaining to a lack of sufficient documentation for the annual operating transfers from Fund 400 to OC Watersheds, and for creating and updating the Chart of Accounts (COFA) documents used for the establishment of Funds 400 and 404.

Objective 2: Our audit found that internal controls are in place to ensure special revenue fund transactions are valid, adequately supported, processed timely, properly recorded, and management reviews and approvals related to receiving, disbursing, reconciling, and claiming reimbursements of OC Flood funds are performed, with the following exception. We identified **one (1) Control Finding** regarding policies and procedures not in place to ensure all claims are submitted timely.

Objective 3: Our audit did not disclose any instances concerning duplication of work, backlogs, or manual processes needing automation. **We have no findings under this objective.**



Internal Auditor's Report

BACKGROUND

The mission of OC Public Works (OCPW) is to “protect and enrich the community through efficient delivery and maintenance of public works infrastructure, planning, and development services.” OCPW is comprised of ten core service areas: OC Fleet Services, OC Development Services, Administrative Services, OC Facilities Design & Construction, OC Facilities Maintenance & CUF, OC Infrastructure Programs, OC Construction, OC Operations & Maintenance, OC Survey, and OC Environmental Resources. Under OC Infrastructure Programs is the OC Flood Division that is responsible for maintaining public safety through the planning and design of flood control facilities that protect the region from flooding. OC Flood Division consists of three sections:

- | |
|---|
| 1. Flood Control Programs: Programs that manage the County's floodplains and provide support to developers and other agencies, and for managing the Flood Control Capital Improvement Program. |
| 2. Santa Ana River Project: Responsible for planning support, engineering, real estate, legal, and administration of the Santa Ana River Project. |
| 3. Flood Control Design: Used for design and analysis of flood control capital improvement projects. |

Under the authorization of the Orange County Flood Control Act (Act), Chapter 723 of the State of California Statutes of 1927, the Orange County Flood Control District (OCFCD) was established on May 23, 1927. It was created to provide: control of flood and storm waters of the district and of streams flowing into the district (e.g., the Santa Ana River, San Juan Creek); to mitigate the effects of tides and waves; and to protect the harbors, waterways, public highways and property in the district from such waters. Subsequent to its formation, the Act was revised and its scope expanded to include water quality monitoring, investigations, and compliance with federal and state water pollution regulations. The OCFCD is governed by the Orange County Board of Supervisors and is administered by OCPW.

OC Flood Division Special Revenue Funds:

OC Flood Division operates using three special revenue funds: Fund 400 OC Flood, Fund 403 OC Santa Ana River, and Fund 404 OC Flood - Capital. The purpose of a special revenue fund is to establish accountability for general government financial resources that are restricted by law or contractual agreement to specific purposes other than debt service or major capital projects. OC Flood's revenue sources are primarily from property taxes and state and federal grants. The table below shows the establishment of the funds and respective activities during the audit period (as of April 30, 2015):

Fund	Authority for Fund Establishment	Operational Use	Expenditures	Revenues	Fund Balance
400 OC Flood	Unknown due to missing record, see Finding No. 3.	Provides for Countywide flood protection and for the operation and maintenance of the Orange County Flood Control District's 380 miles of flood control channels, 6 dams, 33 retarding basins, 13 pump stations, and other flood control infrastructure.	\$97,579,250	\$128,060,887	\$179,087,362
403 OC Santa Ana River	Established in 1973 to provide a method of accounting of monies received and disbursed in accordance with Agreement No. C732 entered into by the OC Flood Control District and the OC Water District on July 25, 1972.	Provides for the environmental enhancement of the Santa Ana River between Katella Avenue and Imperial Highway per agreement with Orange County Water District. (Note: There has been limited activity with this fund for some time now.)	\$54	\$5,042	\$68,120
404 OC Flood - Capital	Established in 1977 in accordance with Board of Supervisor's Ordinance No. 2992 to permit an accumulation of district funds for future construction of the proposed Santa Ana River Federal Project.	Used to account for activities to remove the flood threat in Orange County from the Santa Ana River.	\$39,197,006	\$41,736,661	\$183,895,623



Internal Auditor's Report

Note: Typically in special revenue funds when there are large ending fund balances, this represents funding available for projects or uses that are planned or in process. Special revenue funds are not supposed to accumulate large reserves unless the funding is earmarked for future projects. Our audit found that OC Flood has a seven-year plan of projects for which Funds 400 and 404 are intended for.

SCOPE AND METHODOLOGY

Our audit covered the year ended April 30, 2015, and included OCPW's administration of special revenue Funds 400 and 404. Our scope and methodology included:

1. Obtaining an understanding of the nature, purpose, and requirements concerning sources and uses of Funds 400 and 404 monies to ensure special revenue funds are used for specific purposes. We accomplished this by obtaining documentation from A-C General Accounting for the establishment of the funds, known as the Chart of Accounts (COFA) and reviewing the Orange County Flood Control Act.
2. Evaluating processes and internal controls over the OCPW's administration of Funds 400 and 404 to ensure compliance with County, OCPW, and OC Flood District's policies and procedures. Our scope was limited to reviewing accounting practices and management reviews/approvals of Funds 400 and 404 transactions to ensure sources and uses are in compliance with each established fund purpose.
3. Reviewing a sample of Funds 400 and 404 revenues and expenditures to determine if the transactions are accurate, valid, adequately supported, properly recorded, processed timely, and in accordance with the established purposes of the special revenue funds.
4. Reviewing a sample of Funds 400 and 404 reimbursement claims and fund reconciliations to determine if they are performed accurately, completely, and timely in accordance with management expectations.

SCOPE EXCLUSIONS

Our audit did not include a review of Fund 403 – OC Santa Ana River due to low activity in the fund. Our audit also did not include OC Flood program compliance, performance measures, or reporting requirements of the Flood Control District, except if related to the administration and processing of special revenue fund transactions. This audit also did not evaluate the establishment, maintenance, or project management of OC Flood projects.

FOLLOW-UP PROCESS

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 six months 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 six months from the release of the first Follow-Up Audit report, by which time **all** audit recommendations are expected to be addressed and implemented. We bring to the AOC's attention any audit recommendations we found still not implemented or mitigated after the second Follow-Up Audit. Such open issues will appear on the AOC agenda at their next scheduled meeting for discussion.



Internal Auditor's Report

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 form to facilitate our review.

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 OC Public Works' and OC Flood'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 OC Public Works' and OC Flood's operating procedures, accounting practices, and compliance with County policy.

The Auditor-Controller Internal Audit Division is available to partner with your staff so that they can successfully implement or mitigate difficult audit recommendations.

ACKNOWLEDGEMENT

We appreciate the courtesy extended to us by the personnel of OCPW, OCPW Accounting, and OC Flood during our audit. If you have any questions regarding our audit, please contact me directly at (714) 834-5442, or Scott Suzuki, Assistant Director at (714) 834-5509.



Detailed Findings, Recommendations, and Management Responses

Objective 1: Evaluate if internal controls are in place to ensure special revenue Funds 400 and 404 are used for specific purposes.

AUDIT STEPS AND RESULTS

To accomplish this objective, we performed the following audit steps:

- ✓ Reviewed County Accounting Manual (CAM) Procedure ~ F-3, Requesting Establishment/Deletion of Funds/Agencies for fund establishment.
- ✓ Obtained documentation showing the establishment and authorized uses of Funds 400 and 404 and gained an understanding of the nature, purpose, and requirements concerning sources and uses of Fund 400 and Fund 404 monies.
- ✓ Held meetings with OC Flood management, program, budget, and accounting personnel to obtain a general understanding of the operations pertaining to Funds 400 and 404, and reviewed relevant documentation provided by staff responsible for administration of the funds.
- ✓ Reviewed financial data to gain an understanding of the actual activities and uses of Funds 400 and 404 during our audit period.

CONCLUSION

Our audit found OCPW has controls in place to ensure that special revenue Funds 400 and 404 are used for specific purposes, with the following exceptions. We identified **one (1) Significant Control Weakness** regarding a policy is not in place to ensure all OC Watersheds' programs prior period encumbrance cancellations are refunded to Fund 400 instead of reverting back to the County General Fund. We also identified **two (2) Control Findings** pertaining to a lack of sufficient documentation for the annual operating transfers from Fund 400 to OC Watersheds, and for creating and updating the Chart of Accounts (COFA) documents used for the establishment of Funds 400 and 404. The three (3) findings and recommendations are discussed below.

Finding No. 1 – Policy and Procedures Not in Place to Ensure All Prior Year OC Watersheds' Encumbrance Cancellations are Refunded to OC Flood Fund 400 (Significant Control Weakness)

Criteria

Fund 400 is a special revenue fund restricted for allowable uses as stated in the Flood Control Act (Act). The Act was subsequently amended to broaden the scope that Flood Funds can also be expended for water quality monitoring, investigations, and compliance with federal and state water pollution regulations. Therefore, funds are transferred from Fund 400 to support OC Watersheds' programs in Fund 100/034, annually. Since it provides funding to Fund 100/034 via operating transfers, any unused monies in OC Watersheds should be returned to Fund 400.

Details

Actual expenditures and encumbrances for OC Watersheds' programs are recorded and posted in Fund 100/034. Encumbrances are anticipated expenditures in the form of purchase orders, contracts, and other commitments authorizing the delivery of merchandise or rendering of services. An encumbrance reserves appropriations (available funding) until an obligation is paid, cancelled, or has expired.



Detailed Findings, Recommendations, and Management Responses

The County has a procedure for encumbering appropriations. As a payment is processed, it is made against the purchase order/contract from which the encumbrance was created and an equal amount of encumbrance is reversed. When the obligation is fulfilled or has expired, the encumbrance will be cancelled and the remaining encumbrance balance is reversed and made available for other use in the fund where it was created. At fiscal year-end, any unused open encumbrances are carried forward to the new fiscal year as prior year encumbrances in the accounting system. Expenditures charged to these prior year encumbrances are referred to as prior year expenditures and they do not impact current year budget appropriations.

Since OC Watersheds' programs receive funding from Fund 400 via operating transfers, total appropriations are a critical element in determining the amount to be transferred. The amount encumbered in a prior year, but cancelled subsequently, has already been included in the total appropriations for the year that it was created and has received funding for it. Therefore, a transfer from OC Watersheds or County General Fund is needed to refund the money back to OC Flood.

OCPW Accounting informed us a prior year encumbrance cancellation for Fund 100/034 was not refunded to Fund 400. We researched and confirmed the cancellations were not returned to Fund 400. While OC Watersheds was not the subject of our audit, it is possible funds resulting from the cancellation could have been used for general purposes in General Fund 100 which is against the special revenue fund's restrictions. A policy should be in place to ensure any prior period encumbrance cancellations for OC Watersheds' programs are returned to Fund 400 for restricted use. During our audit period, total prior year encumbrances of \$110,406 were cancelled and not returned to Fund 400.

Recommendation No. 1:

OCPW/OC Flood partner with the County Budget Office and the Auditor-Controller to establish a policy to ensure OC Watersheds' prior period encumbrance cancellations are refunded to Fund 400. In addition, the total amount to refund Fund 400 should be determined and transferred back to Fund 400 since OC Watersheds is part of the General Fund and has been receiving funding from OC Flood.

OCPW/OC Flood Management Response:

Concur. During the audit OCPW Accounting staff recognized this deficiency and reported it to Internal Audit. Due to the fact that OCPW Accounting lacks a procedure, OCPW/OC Flood is currently working with the County Budget Office and OCPW Accounting to establish a procedure to ensure OC Watersheds' prior period encumbrance cancellations are refunded to Fund 400. Additionally, OCPW Accounting researched the total amount to be refunded to Fund 400 and transferred the funds back to Fund 400 in June 2016.

Finding No. 2 – Lack of Sufficient Supporting Records for Operating Transfers from OC Flood Fund 400 to OC Watersheds' Program (County General Fund 100/034) (Control Finding)

Criteria

OC Flood Fund 400 is a special revenue fund restricted to provide control of flood and storm waters, to conserve those waters for beneficial and useful purposes, and to protect from damage from those flood or storm waters, the harbors, waterways, public highways, and property in the district as stated in the Act. The Act was subsequently amended to broaden the scope that Flood Funds can also be expended for water quality monitoring, investigations, and ensuring compliance with federal and state water pollution regulations. Therefore, funds are transferred from Fund 400 to support OC Watersheds' programs in Fund 100/034, annually. The annual operating transfer is calculated based on the differences between total operating revenues and expenditures to support the operation of OC Watersheds' program.



Detailed Findings, Recommendations, and Management Responses

Since total expenditures for OC Watersheds' program are comprised of many projects and activities, sufficient records are required to indicate a nexus of the expenditure to the Flood Control restricted use.

Details

OC Watersheds' program in OCPW is part of the County's General Fund. Actual expenditures for the program are recorded and posted in Fund 100/034. Program funding includes Fund 400 and is made in the form of operating transfers once or twice a year. The transfer amount is calculated based on the difference between the operating revenues and expenditures for the fiscal year.

The use of Fund 400 for OC Watersheds' programs was based on the amended scope in the Act. Furthermore, we affirmed OC Watersheds' costs must have a connection to the Act or District in order to be funded from Fund 400. While OC Watersheds was not the subject of our audit, we found there are no written policies and procedures in OC Flood or OC Watersheds to ensure sufficient records are available to clearly support the operating transfers by indicating a nexus of the expenditure to the Flood Control restricted use.

Without documentation that clearly distinguishes OC Watersheds' projects that are allowable under the Act, there is a risk of using restricted special revenue funds for unallowable projects or expenditures. Since OC Watersheds' projects or operations may have evolved over time, OCPW should ensure continuity of legal compliance for special revenue fund use.

Recommendation No. 2:

OCPW/OC Flood establish a defined methodology to identify projects that specifically relate to the Act and establish policy and procedures to ensure sufficient supporting records for operating transfers from OC Flood Fund 400 to OC Watersheds' programs are available.

OCPW/OC Flood Management Response:

Do Not Concur. OCPW and CEO Budget do not concur with the finding as stated. OCPW Accounting included an overall reconciliation summary with all Journal Vouchers related to operating transfers from OC Flood Fund 400 to OC Watershed Budget 034. All operating transfers were consistent with the prior Board action and Annual Budgets approved by the Board of Supervisors. While OCPW/OC Flood Management recognizes that there can be improved documentation for the operating transfer, and will implement the recommendations provided, we believe that the support for the previous transfers was sufficient. Based on the Flood Control Act the District can expend funds for the monitoring and testing of waters within the District, carry on examinations and investigations pertaining to water quality, and establish compliance with all applicable laws and regulations relating to water pollution or the discharge of pollutants. These are precisely the activities that are performed by the OC Watersheds Service Area. Additionally, the Board of Supervisors approved the operating transfers from Fund 400 to cover OC Watersheds' program costs. Given this approval and the nature of OC Watersheds activities, OCPW is comfortable that the previous transfers were adequately supported.

Furthermore, OCPW's current budget process requires OC Watersheds to identify revenue sources for each of its program costs. This is detailed in OCPW's internal budget system "BFAST". Whenever a cost is submitted for OC Watersheds the cost is compared to the budget details in BFAST to make sure that sufficient appropriations and matching revenue is aligned with the request and is part of the approved budget.



Detailed Findings, Recommendations, and Management Responses

That being said we do believe that our process can be improved. OCPW/OC Flood will establish a defined methodology to document projects as they relate to the Flood Control Act. OCPW/OC Flood will require that all new OC Watersheds' job numbers reference the Flood Control Act to prove that only Flood-related activities are being funded by Fund 400. OCPW/OC Flood has reviewed current OC Watersheds' job numbers representing 90% of total 034 costs to show that the underlying activities are covered under the Flood Control Act and will update the underlying documentation on these to reference the appropriate Flood Control Act section. It should be noted that after our review there have been no ineligible expenditures identified within OC Watersheds and no Funds need to be returned to Fund 400.

A-C/Internal Audit Rejoinder:

The objective of our recommendation was to improve the process for ensuring operating transfers (for allowable use) from the special revenue fund to the other operating fund (Fund 100/034) are properly documented. OCPW has acknowledged that its process can be improved and it will establish a defined methodology to document projects as they relate to the Flood Control Act. As such, although OCPW did not concur with our finding, we determined that the intent of our recommendation has been recognized and the management response has adequately addressed our concerns.

Finding No. 3 – COFA Documents for OC Flood Funds 400 and 404 Need to be Created and Updated (Control Finding)

Criteria

CAM F-3 - *Requesting Establishment/Deletion of Funds/Agencies*, Section 2.2.1 ~ Approvals for Establishment of Fund or Agency states:

“A new fund or agency which is required to be established by the Board, because the statute, regulation or other authority requires that the fund or agency be established by Board action, must be submitted to the Board on an Agenda Item Transmittal (AIT). The AIT must be submitted to the Auditor-Controller and to the CEO for review, and concurrence must be obtained from the CEO.”

Further, Section 2.3 ~ Request for Establishment: Required Information states:

“The AIT or request letter must contain the following information:

- (A) The legal authority for establishing the new fund or agency;*
- (B) If no legal authority, the policy/administrative reason or other authority for establishing the fund or agency;*
- (C) Whether or not the fund or agency is a budgeted fund or agency, and if available, the Activity Code to be used for this budget;*
- (D) A description of the revenue sources for the fund or agency, and the uses of the fund or agency;*
- (E) Any expiration date for the fund or agency;*
- (F) Whether the fund will earn its own interest, or if it does not, which other fund should receive the interest earned on balances in the new fund (this does not apply to new agencies);*

- (G) If the fund will not earn its own interest, the reason for the redirection of interest: legal or contractual provision, or management decision;*
- (H) The specific account codings and dollar amounts or appropriations and estimated revenues to be established for the fund or agency, if the fund or agency is being established pursuant to 2.2.3 above;*
- (I) The responsible controlling department for the new fund or new agency; and*
- (J) For funds with separate cash accounts, the planned disposition of any residual account balances when the fund is closed. Include legal or other authority for the distribution.”*



Detailed Findings, Recommendations, and Management Responses

Details

Chart of Accounts (COFA) are documents used to establish or modify various funds in the County. Our audit found no COFA for establishing Fund 400. Instead of a COFA, OCPW provided documents that support the program, such as Orange County Flood Control Act, California uncodified Water Code Act 5682, and a memo from 2010 to rename Fund 400 from Flood Control District to OC Flood.

Although the exact date for the establishment of Fund 400 is unknown, the state governor approved to create the OC Flood Control District effective July 29, 1927, which is prior to the implementation of the CAM ~ F-3. Therefore, the establishment of the fund could have met the criteria at that time. Currently, documents are not available to validate it and to include all required elements in CAM ~ F-3. In addition, the COFA document for establishing Fund 404 is available; however, elements required in the CAM ~ F-3, Section 2.3 are missing and have not been updated to be in compliance.

Auditor-Controller General Accounting is responsible for establishing and maintaining COFA documents. They are aware of the fact that some of the fund establishment documents are old and are not available. OCPW/OC Flood should work with the Auditor-Controller to update the COFAs.

The absence of the COFA document increases the risk of misunderstanding or miscommunication regarding rights and responsibilities for the controlling department. Also, it increases the risk of unallowable use of restricted funds.

Recommendation No. 3:

OCPW/OC Flood partner with the Auditor-Controller to establish a COFA for Fund 400 and to update the document for Fund 404 in the current COFA format.

OCPW/OC Flood Management Response:

Concur. OCPW Accounting has completed Form 5201 (Request for Establishment, Deletion, Modification of Fund) requesting modification to the purpose and use of Funds 400 and 404. OCPW Accounting has submitted the Chart of Financial Accounts (COFA) Form 5201 to Auditor-Controller for approval.



Detailed Findings, Recommendations, and Management Responses

Objective 2: Evaluate if internal controls are in place to ensure special revenue fund transactions are valid, adequately supported, processed timely, properly recorded, and that management reviews and approvals related to receiving, disbursing, reconciling, and claiming reimbursements of OC Flood funds are performed.

AUDIT STEPS AND RESULTS

To accomplish this objective, we performed the following audit steps:

- ✓ Reviewed pertinent County Accounting Manual (CAM) Procedures, OCPW and Auditor-Controller's written policy and procedures for processing transactions in Fund 400 OC Flood and Fund 404 OC Flood - Capital.
- ✓ Reviewed OC Public Works' process to establish and use job codes specifically for OC Flood programs. This included a review of job cost system policy and procedures and training materials provided to staff.
- ✓ Reviewed the reconciliation process between job cost/labor reports and the General Ledger for identifying exceptions and researching transactions in which funds and job numbers do not agree.
- ✓ Performed review of transactions including **19 fund revenues totaling \$36 million and 31 disbursements totaling \$26 million** to determine if they were valid, adequately supported, processed timely, properly recorded, and management reviews and approvals were performed.
- ✓ Confirmed a sample of **six (6) claim reimbursements totaling \$21 million** to the corresponding claim report and to the Summary of Subvention Claims to verify the claim has been properly recorded.
- ✓ Reviewed the subvention claim reimbursement to the corresponding fund reconciliation to ensure a reconciliation was performed and reviewed prior to submittal.
- ✓ Reviewed **seven (7) claim reimbursements** to the Claims and Reports Checklist to ensure claims were properly reviewed prior to submitting for reimbursement.

CONCLUSION

Our audit found OCPW/OC Flood has controls in place to ensure special revenue fund transactions are valid, adequately supported, processed timely, properly recorded and management reviews and approvals related to receiving, disbursing, reconciling and claiming reimbursements of OC Flood funds are performed with the following exception. We identified **one (1) Control Finding** regarding establishing written policy and procedures over the claiming process that include claiming timeframes and review process in OCPW.

The finding and recommendation are discussed below:



Detailed Findings, Recommendations, and Management Responses

Finding No. 4 – Comprehensive Policy and Procedures Not in Place to Ensure Subvention Claims Are Submitted in a Timely Fashion (Control Finding)

Criteria

County Accounting Manual ~ S-2, Internal Control Systems, Section 4.3.1, Written Policies and Procedures, *“Establish written policies and procedures that supplement the policies and procedures in the Auditor-Controller’s County Accounting Procedures Manual, to assure intended functioning of internal control systems. These policies and procedures should set forth in writing the specific procedures to be followed, and should be communicated and made available to all employees.”*

Details

Pursuant to the California Water Code, the Santa Ana River Mainstem Project (recorded in Fund 404) is authorized to receive state financial assistance administered by the Department of Water Resources’ (DWR) Flood Control Subventions Program. The Orange County Flood Control District is a local sponsor and can request reimbursements for the project. The state’s share is 70% of the eligible project costs pertaining to land purchase, easements, rights of way, relocations, disposal, and 5% cash contribution for project construction. The sponsor is responsible for the remaining 30%. The DWR Guidelines do not provide specific deadlines for submitting a subvention claim; however, it is reimbursed based on a first-in, first-out policy. Submitting reimbursement claims on a regular and timely basis ensures eligible funds for the project are secured for continued operations. Also, there may be multiple claims for a specific project; a delay in submitting one claim would delay the submittal of subsequent claims. Lastly, the claim process should be shortened and be consistent to meet business needs.

We reviewed a sample of seven (7) subvention claims and found that they were submitted from nine (9) months to three (3) years from the respective reporting quarter end. See the table below for details:

Subvention Claim #	Claim Period	Claim Submittal Date	Time from the Quarter End
82A&B	April - June 2009	May 9, 2012	2 years & 11 months
86A&B	April - June 2010	June 3, 2013	3 years
89A&B	Jan - March 2011	Dec. 23, 2013	2 years & 9 months
94A&B	April - June 2012	Dec. 23, 2013	1 year & 6 months
97A&B	Jan - March 2013	August 11, 2014	1 year & 5 months
104A&B	Oct - Dec 2014	Sept. 22, 2015	9 months
105A&B	Jan - March 2015	Dec. 15, 2015	9 months

Since subvention claims are paid in the order received by the DWR, there is a risk when eligible costs have been incurred in OC Flood Control District, the state funding might be unavailable for replenishment due to fund depletion or legislative changes.

We were informed OCPW Accounting was unable to process subvention claims timely due to limited resources at the time; however, OCPW Accounting was in the process of catching up with submitting outstanding claims during our audit period and this is evidenced by the most recent claims being completed and submitted within nine (9) months from the respective reporting quarter end.



Detailed Findings, Recommendations, and Management Responses

Each subvention claim requires a review by OC Flood and OCPW Accounting. While an A-C Claims and Reports Checklist used to process claims does not include any specific timing requirements, we found that OCPW Accounting has a practice requiring a claim review to be completed in OCPW Accounting and forwarded to OC Flood within 90 days. Separately, OC Flood management informed us that the processing time to submit a claim is determined to be six to 12 months; however, there are no documented procedures for Program's review of claims prepared by OCPW Accounting. If OCPW determines these are the standards for claim processing and review in OCPW Accounting and OC Flood, written policy and procedures should be adopted and approved by management to address the specific requirements in OCPW Accounting and the overall claim process in OCPW. Alternatively, this could be accomplished by modifying the A-C Claims and Reports Checklist to accommodate Program procedures and general timeframes.

Recommendation No. 4:

OCPW/OC Flood adopt written policy and procedures to address the general timeframes for submitting subvention and/or other reimbursable claims and ensure the policy is communicated and made available to all employees.

OCPW/OC Flood Management Response:

Concur. We concur that OCPW will adopt a timeframe for review. We will incorporate the OCPW review process in our overall submission timelines.

<p>Objective 3: Determine if administration of OC Flood special revenue funds is effective and efficient (e.g., no backlogs, duplication of work, benefit in automating manual process).</p>

CONCLUSION

Based on our audit, we did not observe any instances of backlogs, duplicated work or manual processes that could be automated in OCPW/OC Flood's or OCPW Accounting Services' processes and administration of Funds 400 and 404. As such, we have no findings under this objective.



Detailed Findings, Recommendations, and Management Responses

ATTACHMENT A: Report Item Classifications

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

▶ **Critical Control Weaknesses:**

These are Audit Findings or a combination of Auditing Findings that represent critical exceptions to the audit objective(s) and/or business goals. Such conditions may involve either actual or potential large dollar errors or be of such a nature as to compromise the Department's or County's reputation for integrity. Management is expected to address Critical Control Weaknesses brought to their attention immediately.

▶ **Significant Control Weaknesses:**

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

▶ **Control Findings:**

These are Audit Findings concerning internal controls, compliance issues, or efficiency/effectiveness issues 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 Findings, Recommendations, and Management Responses

ATTACHMENT B: OCPW/OC Flood Management Responses



July 13, 2016

To: Ms. Toni Smart, CPA, Director
Auditor-Controller Internal Audit Division
12 Civic Center Plaza, Room 200
Santa Ana, CA 92701

Subject: Response to Draft Report – Audit No. 1421, OC Public Works/OC Flood Special Revenue Funds

Dear Ms. Smart:

OC Public Works has received and reviewed in draft form, the Internal Audit Department's Review of the OC Public Works/OC Flood Special Revenue Funds.

OC Public Works understands the primary purpose of the Internal Audit Department's review was to ensure special revenue funds are properly administered and maintained in compliance with County policy and procedures, and are utilized in accordance with fund requirements.

OC Public Works hereby provides the following responses to the Internal Audit Department's Recommendations.

Recommendation No. 1: OCPW/OC Flood partner with the County Budget Office and the Auditor-Controller to establish a policy to ensure OC Watersheds' prior period encumbrance cancellations are refunded to Fund 400. In addition, the total amount to refund Fund 400 should be determined and transferred back to Fund 400 since OC Watersheds is part of the General Fund and has been receiving funding from OC Flood.

OC Public Works' Response: Concur

During the audit OCPW Accounting staff recognized this deficiency and reported it to Internal Audit. Due to the fact that OCPW Accounting lacks a procedure, OCPW/OC Flood is currently working with the County Budget Office and OCPW Accounting to establish a procedure to ensure OC Watersheds' prior period encumbrance cancellations are refunded to Fund 400. Additionally, OCPW Accounting researched the total amount to be refunded to Fund 400 and transferred the funds back to Fund 400 in June 2016.

Recommendation No. 2: OCPW/OC Flood establish a defined methodology to identify projects that specifically relate to the Act and establish policy and procedures to ensure sufficient supporting records for operating transfers from OC Flood Fund 400 to OC Watersheds' Program are available.

OC Public Works' Response: Do Not Concur

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Detailed Findings, Recommendations, and Management Responses

OCPW and CEO Budget do not concur with the finding as stated. OCPW Accounting included an overall reconciliation summary with all Journal Vouchers related to operating transfers from OC Flood Fund 400 to OC Watershed Budget 034. All operating transfers were consistent with the prior Board action and Annual Budgets approved by the Board of Supervisors. While OCPW/OC Flood Management recognizes that there can be improved documentation for the operating transfer, and will implement the recommendations provided, we believe that the support for the previous transfers was sufficient. Based on the Flood Control Act the District can expend funds for the monitoring and testing of waters within the District, carry on examinations and investigations pertaining to water quality, and establish compliance with all applicable laws and regulations relating to water pollution or the discharge of pollutants. These are precisely the activities that are performed by the OC Watersheds Service Area. Additionally, the Board of Supervisors approved the operating transfers from Fund 400 to cover OC Watersheds' program costs. Given this approval and the nature of OC Watersheds activities, OCPW is comfortable that the previous transfers were adequately supported.

Furthermore, OCPW's current budget process requires OC Watersheds to identify revenue sources for each of its program costs. This is detailed in OCPW's internal budget system "BFAST". Whenever a cost is submitted for OC Watersheds the cost is compared to the budget details in BFAST to make sure that sufficient appropriations and matching revenue is aligned with the request and is part of the approved budget.

That being said we do believe that our process can be improved. OCPW/OC Flood will establish a defined methodology to document projects as they relate to the Flood Control Act. OCPW/OC Flood will require that all new OC Watersheds' job numbers reference the Flood Control Act to prove that only Flood-related activities are being funded by Fund 400. OCPW/OC Flood has reviewed current OC Watersheds' job numbers representing 90% of total 034 costs to show that the underlying activities are covered under the Flood Control Act and will update the underlying documentation on these to reference the appropriate Flood Control Act section. It should be noted that after our review there have been no ineligible expenditures identified within OC Watersheds and no Funds need to be returned to Fund 400.

Recommendation No. 3: OCPW/OC Flood partner with the Auditor-Controller to establish a COFA for Fund 400 and to update the document for Fund 404 in the current COFA format.

OC Public Works' Response: Concur

OCPW Accounting has completed Form 5201 (Request for Establishment, Deletion, Modification of Fund) requesting modification to the purpose and use of Funds 400 and 404. OCPW Accounting has submitted the Chart of Financial Accounts (COFA) Form 5201 to Auditor-Controller for approval.

Recommendation No. 4: OCPW/OC Flood adopt written policy and procedures to address the general timeframes for submitting subvention and/or other reimbursable claims and ensure the policy is communicated and made available to all employees.

OC Public Works' Response: Concur

We concur that OCPW will adopt a timeframe for review. We will incorporate the OCPW review process in our overall submission timelines.

It is important to note that OCPW has been working on reducing the submission time for the SARMP claims for several years. Prior to the audit being conducted we had reduced submission time significantly while maintaining clean audits from the State Controller's Office. The statement that



Detailed Findings, Recommendations, and Management Responses

"During our audit period, OCPW was in the process of catching up with submitting outstanding claims" is true, however, during the time the audit was conducted the claims were caught up to our current standards. The claiming process is very involved and there are multiple levels of review as well as discussions with the State that delay official submission of the claims. Once Accounting prepares the claims for review, the review process can vary depending on the complexity of the underlying expenditures. Accounting developed the 90 day guideline to submit claims to OCPW for review because that process is largely routine and can be estimated within reason. This procedure was a directive communicated via email from the Satellite Accounting manager to the OCPW Accounting manager and subsequently to the SARMP Accounting manager.

As stated, the DWR Guidelines do not provide specific deadlines for submitting a subvention claim. There were no late claims during the audit period and there were no funds withheld from the County due to timeliness. OCPW/OC Flood staff work very closely with the Department of Water Resources (DWR) to ensure that claims are submitted in time to utilize available funding. Accounting, working in conjunction with OC Flood Staff, provides estimates to DWR via a five year projections progress report that outline upcoming claims that will be submitted to the State. DWR utilizes these reports to plan their funding of the claims among other uses. These progress reports are provided annually or more frequently if requested by DWR.

Thank you and should you have any questions, please contact Jackie Cadotte at OC Public Works at 714-667-3287.

Sincerely,

Signature: 
Shane L. Silsby
Director, OC Public Works

cc: Eric Woolery, Auditor-Controller
Jessica Witt, Assistant to the Chief Operating Officer
Robyn Uptegraff, Assistant Director, OCPW
Becky Juliano, Deputy Director, Administrative Services, OCPW
Randi Dunlap, Administrative Manager II, Centralized Quality Assurance, OCPW
Jackie Cadotte, Compliance Services Manager, Centralized Quality Assurance, OCPW
Tonya Riley, Director, Satellite Accounting Operations, A-C
Howard Thomas, Accounting Manager, OCPW Accounting