2011-2012 GRAND JURY REPORT
Riverside County Auditor-Controller
Internal Audit Division

Background

The Riverside County Auditor-Controller is an independent, nonpartisan elected official. The Auditor-Controller is the chief accounting and disbursement officer responsible for budget control, disbursements and receipts, and financial reporting. This officer is responsible for audits of all departments and certain agencies within the County's jurisdiction. The office was established to provide various accounting and property tax administration services for Riverside County (County), special districts, schools, and cities. The key divisions of the Auditor-Controller include Administration, General Accounting and Reporting, Property Tax, Payroll, Information Technology, and Internal Audits/Specialized Accounting. The focus of this report is the Internal Audit/Specialized Accounting Division (Audit Division).

Focus / History

The Auditor-Controller is required by law to perform audits of all departments within the jurisdiction of the Riverside County Board of Supervisors (Board). California Government Code §25250 and Board Resolution 83-338 mandate that these audits be performed biennially.
When the staff of the Audit Division is drastically reduced, these risk-based audits are not pursued. Countywide duplicate vendor payments, Countywide Sheriff's Department overtime, and Countywide revenue generating leases, were three of Fiscal Year (FY) 2010/2011 audits omitted because of "lack of manpower," or were "not mandated" according to the Auditor-Controller.

The definition of a mandated audit per Board Resolution 83-338 is:

> *…The financial accounts and records of officers having responsibility for care, management, collection, disbursement of money belonging to the county, or money received or disbursed by them under authority of law shall be audited biennially…*

A document from the Auditor-Controller states:

> *Our interpretation includes all officers, either elected or appointed by the Board including all Department Heads of all departments of the county since they are appointed by the Board and have the responsibility for the care, management, collection, and disbursement of county funds. In addition, Government Code §25252 authorizes the Board to establish or abolish, those funds as are necessary for the proper transaction of the*

> *business of the county, and may transfer money from one fund to another, as the public interest requires. Since the Board of Supervisors reviews and adopts department's* [*sic*] *budgets and allocates funding as appropriate to each department, Government Code §25250 applies, whereas each department shall be audited biennially. Our goal and practice has been* [*sic*] *to audit an aspect of each department every two years, identifying these audits as 'mandated' on our annual audit plan.*

As reported by KPMG, an outside auditing firm, in 2001, the primary beneficiaries of these audits are the taxpayers of the County. Other beneficiaries are the Board and departments who benefit from the knowledge that assets and resources are safeguarded and that department operations are effective and efficient. The Auditor-Controller is responsible for ensuring that mandatory audits are performed as scheduled by either internal staff or contracted certified public

accountants. Examples of mandatory audits are special districts, County treasury, probation, child development, tax collector, and joint powers agencies.

Seven prior grand jury reports addressing the lack of adequate staffing in the Audit Division have been submitted to the Board. Serious staffing shortages have existed since 1990. Reports covering the staffing issues resulted in Board Resolution 440-8568 of October 19, 2004. This resolution increased the County budget over the following five years to bring authorized auditing positions to a total of twenty-four.

As a result of 2004 Board resolution, the number of audits increased from 41 per year to a high of 66 per year in FY 2007/2008 and averaging 54 per year through FY 2010/2011. At the time of this report, auditor positions have been reduced to seven. This leaves the Division with four vacant positions, leaving only three internal auditors. The present FY 2011/2012 audit plan is reduced to 37 audits, 26 of which are mandated or mandated follow-ups; an additional 11 are still in progress from FY 2010/2011.

The last Countywide risk assessment performed in 2001 by the accounting firm KPMG noted that with one audit manager (principal accountant) and three senior auditors, "…the downsizing of the Audit Division has limited the frequency of audits." One KPMG finding of this risk assessment was that due to resource limitations the internal audit function has been unable to conduct biennial audits. These audits are required by Board Resolution 83-338 and California Government Code §25250.

Findings

<u>Lack of Manpower</u>

1. Sworn testimony heard by the Grand Jury revealed that nine of the scheduled internal audits for FY 2010/2011 were not completed due to a <u>lack</u> <u>of</u> <u>manpower</u> and/or due to the fact that they were <u>not</u> <u>mandated</u>. Only one of these audits was carried over to the FY 2011/2012 Internal Audit Plan. Two of the internal audits in the FY 2010/2011 plan were prompted by employee complaints via the Countywide "Speak Out!" program that focuses on fraud, waste, and abuse.

   A "Speak Out!" complaint, concerning the excessive use of overtime in the Sheriff's Department, prompted an investigative audit to be scheduled in FY 2010/2011. This audit, along with eight other scheduled audits, was eventually cancelled for either <u>lack</u> <u>of</u> <u>manpower</u> or because they were <u>not</u> <u>mandated</u>. It is the considered judgment of this Grand Jury that because it is law, <u>lack</u> <u>of</u> <u>manpower</u> is not an excuse for failure to perform these audits. Further, no concern about this failure has been expressed by the County Executive Office, Board, or the Auditor-Controller's Office.

   The decision to cancel planned audits due to <u>lack</u> <u>of</u> <u>manpower</u> or because they are <u>not</u> <u>mandated</u> may be construed as a disservice to the taxpayers, as well as to the Board and department directors.

<u>Special Districts</u>

2. Another function of the Audit Division is to ensure that all special districts in the County receive an annual financial audit. These audits are usually performed by public accounting firms. The Government Accounting Standards Board Statement No. 34 requires the inclusion of a Management Discussion and Analysis, which is a simple explanation of the results of the audit that can be easily understood. The Audit Division monitors and reviews these financial statements to ensure that they are conducted as required by Government Code §26909(a) and §6505(d).

   The Audit Division is not proactively pursuing delinquent audits of special districts, thereby placing at risk the fiduciary responsibility of these special district boards that are accountable to the taxpayers. The Audit Division has failed to review these special district audits in depth and ensure that recommended corrective actions were taken within a reasonable time frame. This results in the Auditor-Controller having no positive influence on the financial practices of special districts, a deficiency with unknown consequences.

   Certain special districts have been habitually delinquent, as much as two to five years, in conducting their mandated annual audits. In the case of one special district, Idyllwild Fire Protection District, the Management Discussion and Analysis was omitted from the report to the Audit Division at the request of the special district board. This omission violates Government Accounting Standard Board Statement No. 34, the rights of taxpayers to know the financial status of their district.

The Audit Division's present procedures require that reminder letters be sent to all special districts that are delinquent beyond twelve months after the end of the fiscal year. The timing of these letters, in effect, grants the delinquent special district an additional six months beyond the due date mandated by Government Code §26909(a)(2) and §6505(d).

Policies and Procedures

3. The Audit Division is operating with a draft copy of its policies and procedures, a document that has been dormant, in draft stage since July 2009. This deficiency was previously noted in a peer review report by the San Diego Auditor-Controller's Office in 2006. When an internal audit of a County department is initiated by the Audit Division, the first request is that the department provide a copy of its policies and procedures. If they are non-existent, it becomes a major finding.

Operational Review

4. In July 2011, the Auditor-Controller retained IntelliBridge Partners, an outside consulting firm, to perform an operational review of the Audit Division. The purpose of the review was to assess the County's efficiency and effectiveness in audit planning, execution, and reporting process, as well as to examine the Audit Division's organizational structure. This review was produced at a cost of $38,000. It was similar in content and recommendations to the peer review assessment of 2006 conducted by the San Diego Auditor-Controller's Office. The peer review cost nothing.

   The contracted consulting firm recommended:

   - working with the Board to revise Resolution 83-338 from auditing each County department every two years to auditing County departments based upon risk-based management criteria (e.g., high risks of fraud, waste, abuse or having a high potential to identify cost savings, or to enhance service delivery.)

   - hiring an audit chief executive from outside of the County that has experience in conducting all types of audits (e.g., internal, financial, performance, and compliance) and has a demonstrated track record of working with key stakeholders to produce cost savings and enhance service delivery. (Note: The Auditor-Controller did not follow this recommendation.)

- developing a comprehensive internal training program for all staff and new hires. (Note: IntelliBridge Partners that made the recommendation has now secured the contract to perform this training program.)

- conducting a formal Countywide risk assessment that identifies potential opportunities for cost savings, enhancements to service delivery, and increased compliance with local, state and federal requirements. (Note: IntelliBridge Partners made the recommendation and has now secured the contract to perform the Countywide risk assessment under a new contract.)

A request for proposal by the County was issued in 2011, (Internal Audit Risk Assessment Services RFP # ACARC-010), to conduct an internal audit risk assessment and to develop templates for enhanced reporting. IntelliBridge Partners performed the operational review and was selected to conduct the Countywide risk assessment and training that the firm had just recommended. Cost of this contract was $71,700.

<u>“Speak Out!” Program</u>

5. Prior to September, 2009 the County lacked a fraud policy and hotline. Such a policy is required by the American Institute of Certified Public Accountants (The Institute) and California Government Code §53087.6. The Institute issued two statements on Auditing Standards SAS 99 and SAS 115, which mandate the need to establish a fraud hotline. These requirements were noted as significant deficiencies by outside auditors in management letters in the years 2005 through 2008. As a result, in September 2009, Board Policy C-35 “Standards of Ethical Conduct” was adopted, which requires County employees to sign acknowledging receipt. This policy includes a program entitled “Speak Out!” which encourages County employees to report anonymously, if desired, any incident of fraud, waste, abuse, and other workplace incidents. This program could prompt an investigative audit of operations that might expose deficiencies in internal control, material weaknesses, and significant deficiencies. (In one instance it already has prompted an investigation.)

Sworn testimony to the Grand Jury revealed that reports received from County employees through “Speak Out!” had targeted two departments for wasteful usage of overtime. As a result, these departments were included in the FY 2010/2011 Audit Plan. Only one of these two audits was completed in November 2010, the aforementioned audit of overtime in the Department of Mental Health. The second scheduled audit involved potential overtime abuses in the Sheriff’s Department. This investigative audit was canceled due to <u>lack</u> <u>of</u> <u>manpower</u> or because it was <u>not</u> <u>mandated</u> by government code. It is the considered judgment of this Grand Jury that if either situation exists, the importance of asking County employees to identify fraud, waste, and abuse in County departments is negated.

Deficiencies

6. Sworn testimony given to the Grand Jury, as well as written documentation, were replete with issues involving Audit Division management:

- lack of training for auditors,
- turnover of personnel,
- tardiness of audits,
- insufficient number of auditors to cover Countywide obligations,
- auditors burdened with non-auditing responsibilities, and
- Audit Division intimidating work environment.

Recommendations

Riverside County Board of Supervisors
Riverside County Auditor-Controller
Riverside County Executive Office
Riverside County Human Resources Department

1. It is important that taxpayers know that County departments are managed without a waste of resources, especially during years where revenues have been seriously reduced. The Board must fund and authorize staffing levels commensurate with the tasks required by Board Resolution 83-338 and California Government Code §25250. The increased manpower must be provided in the FY 2012/2013 budget. In the interim, the Audit Division must prioritize tasks and reinstate the eight audits that were cancelled due to lack of manpower or not mandated. The Board and the Auditor/Controller must use whatever resources are necessary to comply with the California Government Code.

2. The Audit Division must accelerate issuance of reminder letters by initiating the first letter within six months after the end of the fiscal year. The second reminder shall be mailed in April and the final reminder shall be sent no later than June 15. This change in procedure would assure taxpayers that special districts serving them are in compliance with the requirements of California Government Code §26909(a)(2) and §6505(d).

The Auditor-Controller must review submitted audits from special districts and take the initiative to ensure that special district boards are taking corrective action on disclosed financial and performance deficiencies.

3. The Auditor-Controller must immediately finalize policies and procedures to guide the internal audit activity.

4. The Board and the Auditor-Controller must recognize that the July 2011, IntelliBridge Partners review was faulty in recommending that the Auditor-Controller work with the Board to replace Resolution 83-338. This resolution was passed to comply with California Government Code §25250, which mandates County departments be audited biennially. This policy delegates the mandated audit authority to the Auditor-Controller. The Auditor-Controller's Office, using only the risk assessment methodology proposed by IntelliBridge Partners, would be ignoring the biennial requirement of California law. The Board must reject this methodology.

5. The Auditor-Controller must perform investigative audits which are in the annual audit plan initiated by "Speak Out!" complaints.

6. Due to the seriousness of deficiencies in the Audit Division, the Board must immediately direct the Executive Office and Human Resources Department to form a special management committee to assess the scope and depth of the deficiencies and construct the means to eliminate or mitigate the potential damage.

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