

# Internal Audit Department

O R A N G E C O U N T Y  
6<sup>th</sup> Largest County in the USA

**FINAL CLOSE-OUT  
FIRST FOLLOW-UP:**

## ANNUAL AUDIT OF TREASURER'S INVESTMENT COMPLIANCE FOR YEAR ENDED DECEMBER 31, 2010

**AS OF MARCH 31, 2013**

Our First Follow-Up Audit found the Treasurer fully implemented all four (4) recommendations from our original audit report dated May 7, 2012.

During the original audit period, investments held at fair value by the Treasurer were \$7.28 billion.

AUDIT NO: 1218-C  
(ORIGINAL AUDIT NO. 1013)

REPORT DATE: MAY 23, 2013

**Director:** Dr. Peter Hughes, MBA, CPA, CIA  
Senior Audit Manager: Alan Marcum, CPA, CIA  
Audit Manager: Lisette Free, CPA, CFE  
Senior Internal Auditor: Abdul Khan, CPA, CIA

### 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

GRC (Government, Risk & Compliance) Group 2010 Award to IAD as MVP in Risk Management



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



2005 Institute of Internal Auditors' Award to IAD for Recognition of Commitment to Professional Excellence, Quality, and Outreach



ORANGE COUNTY BOARD OF SUPERVISORS'  
**Internal Audit Department**

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

*Providing Facts and Perspectives Countywide*

**RISK BASED AUDITING**

**Dr. Peter Hughes** **Ph.D., MBA, CPA, CCEP, CITP, CIA, CFE, CFF, CGMA**  
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Certified Information Technology Professional (CITP)  
Certified Internal Auditor (CIA)  
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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](http://www.ocgov.com/audit)



**OC Fraud Hotline (714) 834-3608**



## Transmittal Letter



**Audit No. 1218-C May 23, 2013**

**TO:** Members, Treasury Oversight Committee

**FROM:** Dr. Peter Hughes, CPA, Director  
Internal Audit Department

**SUBJECT:** **First and Final Close-Out** Follow-Up:  
Annual Audit of Treasurer's Investment  
Compliance For the Year Ended December  
31, 2010, Original Audit No. 1013, Issued  
May 7, 2012

We have completed a First Follow-Up Audit of Treasurer's Investment Compliance for the year ended December 31, 2010. Our audit was limited to reviewing, as of March 31, 2013, actions taken to implement the **four (4) recommendations** from our original audit report dated May 7, 2012. We conducted this First Follow-Up Audit in accordance with the *FY 12-13 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and Board of Supervisors (BOS).

The results of our First Follow-Up Audit are discussed in the **OC Internal Auditor's Report** following this transmittal letter. Because satisfactory corrective action has been taken for the four (4) recommendations, **this report represents the final close-out of the original audit.**

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.

Other recipients of this report are listed on the **OC Internal Auditor's Report** on page 4.

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Annual Audit of Treasurer's Investment Compliance  
For the Year Ended December 31, 2010  
Audit No. 1218-C***

As of March 31, 2013

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# OC Internal Auditor's Report



**Audit No. 1218-C**

**May 23, 2013**

TO: Members, Treasury Oversight Committee

FROM: Dr. Peter Hughes, CPA, Director  
Internal Audit Department

SUBJECT: **First and Final Close-Out** Follow-Up: Annual Audit of Treasurer's Investment Compliance for the Year Ended December 31, 2010, Original Audit No. 1013, Issued May 7, 2012

## Scope of Review

We have completed a First Follow-Up Audit of Treasurer's Investment Compliance for the year ended December 31, 2010. Our audit was limited to reviewing actions taken, as of March 31, 2013, to implement the **four (4) recommendations** from our original audit report dated May 7, 2012.

## Background

We conducted an examination of the Treasurer's Investment Compliance for the year ended December 31, 2010 in accordance with the attestation standards established by the American Institute of Certified Public Accountants. The original audit disclosed four (4) recommendations regarding areas where compliance and internal controls over compliance could be improved.

California Government Code Sections 27000.1, 27000.3, and 53600.3 grant a county board of supervisors, not a county treasurer, with authority for investing public funds. Thus, under California law, county boards of supervisors generally have primary responsibility for investment of public funds in a county treasury. The authority of the board to invest or reinvest funds deposited in a county treasury may be delegated for a one-year period by the board. Subject to review, such a delegation may be renewed annually (Government Code Section 53607). It is common practice for the board of supervisors for counties in the State to delegate its investment responsibility.

California law requires the Treasurer to prepare an annual investment policy statement. The County's Investment Policy Statement (IPS) is reviewed and approved by the County's Treasury Oversight Committee (TOC) and the Board of Supervisors on an annual basis. The IPS, to the extent consistent with the restrictions of state law, establishes the legal parameters by which the Treasurer, or other qualified party to which investment authority is delegated, may invest monies deposited and held within the County treasury.

Historically, the Board of Supervisors performs an annual review of the Treasurer's performance and has delegated its investment authority to the County Treasurer. The most recent renewal of investment authority was January 8, 2013 for calendar year 2013.

On February 2, 2010, the Board of Supervisors directed the Internal Audit Department to conduct this examination to determine whether the treasury investments complied with both applicable California law and the IPS for the years ended December 31, 2009, 2010, and 2011. As the public stewards of \$7 billion of taxpayers' monies, compliance with the County's IPS is of the highest priority for the Board of Supervisors.



We are reminded that in 1995, a former Treasurer, unbeknownst to the Board of Supervisors, invested billions of County funds into extremely high risk and prohibited securities that resulted in a \$1.6 billion loss. The importance of having the Treasurer's office establish and practice sound internal controls ensures that the Treasurer's office is in full compliance with the applicable California Government Code and the IPS.

On November 2, 2010, a new County Treasurer-Tax Collector, Shari L. Freidenrich, was elected; and on December 14, 2010 the Board of Supervisors delegated investment authority, effective January 14, 2011, to the new County Treasurer-Tax Collector.

## Results

Our First Follow-Up Audit indicated the Treasurer **implemented all four (4) recommendations. As such, this report represents the final close-out of the original audit.** Based on our First Follow-Up Audit, the following is the implementation status of the four (4) original recommendations:

1. **Finding No. 1 – Amendments to the Treasury Oversight Committee Bylaws and Rules of Procedures Were Not Forwarded to the Board of Supervisors for Approval in a Timely Manner – Noncompliance with the Bylaws and Rules of Procedures of the County of Orange Treasury Oversight Committee Section VI – Miscellaneous Provisions**

### Recommendation No. 1

We recommend that the Treasurer-Tax Collector (T-TC) ensure changes/amendments to the Bylaws and Rules of Procedures of the County of Orange Treasury Oversight Committee are forwarded to the BOS for approval in a timely manner.

Current Status: **Implemented.** The Treasurer-Tax Collector implemented a new Administration Section in the Investment Policy Compliance Summary chart, which is included in the Treasurer's Monthly Investment Report, and it is included as a separate agenda item in the quarterly TOC meeting. The Administration Section has a new line item to report on "TOC Bylaws Changes – TOC Review and Board of Supervisor's Approval." This new line item provides a reminder to help ensure that changes/amendments to the Bylaws and Rules of Procedures of the County of Orange Treasury Oversight Committee are forwarded to the BOS for approval in a timely manner.

We tested all 2011 changes/amendments to the Bylaws and Rules of Procedures of the County of Orange Treasury Oversight Committee and found that they were forwarded to the BOS for approval in a timely manner.



## 2. **Finding No. 2 – Treasurer-Tax Collector Review of Qualified Institutions was not Complete and Approved In a Timely Manner – Noncompliance with IPS Section XI – Authorized Financial Dealers and Qualified Institutions**

### **Recommendation No. 2**

We recommend that the Treasurer-Tax Collector ensure the review of financial dealers and qualified institutions by staff is performed and approved in a timely manner and the policies and procedures are revised to include the steps to be taken in the event of noncompliance.

**Current Status: Implemented.** The Treasurer-Tax Collector's written procedures for the review of authorized dealers and qualified institutions were updated to include steps to be taken in the event of noncompliance and the required supervisory review and approval by the Chief Assistant Treasurer-Tax Collector.

In compliance with the Investment Policy Statement (IPS), approved by the BOS on January 10, 2012, the Treasurer shall conduct an annual review of each Qualified Institution's financial condition and registrations to determine whether it should remain on the approved list and require annual audited financial statements to be on file for each company. Furthermore, an Administration Section has been added to Investment Policy Compliance Summary chart included in the Treasurer's Monthly Investment Report to report on the "Annual Broker/Dealer Review."

We tested the T-TC dealer annual reviews for the year ended December 31, 2011 and found that it was completed and reviewed in a timely manner.

## 3. **Finding No. 3 – Investment Policy Statement is Less Restrictive than Government Code Section 53601(h)**

### **Recommendation No. 3**

We recommend the Treasurer-Tax Collector amend the IPS to ensure compliance with the Government Code. In addition, the revised Investment Policy Statement should be submitted to the Treasury Oversight Committee and Board of Supervisors for review and approval.

**Current Status: Implemented.** The Treasurer-Tax Collector revised the Investment Policy Statement to achieve compliance with California Government Code 53601(h), submitted the IPS for review to the Treasury Oversight Committee on October 26, 2011, and the Board of Supervisors approved the revised IPS at their regular meeting on January 10, 2012.

In addition, an Administration Section has been added to Investment Policy Compliance Summary chart included in the Treasurer's Monthly Investment Report and the quarterly TOC meeting to report on the "Annual IPS Approval."



## 4. Finding No. 4 – Internal Controls Over Issuer Analyses Needs Improvement

### Recommendation No. 4

We recommend Treasurer-Tax Collector amend its issuer analyses process to include a direct correlation with compliance requirements in the Government Code and Investment Policy Statement.

**Current Status: Implemented.** The Treasurer-Tax Collector amended its issuer analyses process to document a direct correlation with compliance requirements in the Investment Policy Statement and the Government Code. The Treasurer-Tax Collector implemented daily monitoring of all issuers, weekly Investment Credit Committee meetings to discuss any potential new issuers, and a quarterly review process of all issuers.

We appreciate the assistance extended to us by the Treasurer-Tax Collector during our Follow-Up Audit. If you have any questions, please contact me directly at 834-5475 or Alan Marcum, Senior Audit Manager at 834-4119.

### Members, Treasury Oversight Committee Distribution List:

Hon. Dr. Al Mijares, County Superintendent, OC Department of Education  
Jan Grimes, Auditor-Controller  
Michael B. Giancola, County Executive Officer  
William "Andy" Dunn, Public Member  
Laura Parisi, Public Member

### Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Board of Supervisors  
Members, Audit Oversight Committee  
Shari L. Freidenrich, Treasurer-Tax Collector  
Paul C. Gorman, Chief Assistant Treasurer-Tax Collector  
Paul Cocking, Assistant Treasurer-Tax Collector  
Michael B. Giancola, County Executive Officer  
Frank Kim, Chief Financial Officer  
Foreperson, Grand Jury  
Susan Novak, Clerk of the Board of Supervisors  
Vavrinek, Trine, Day, and Co., LLP, County External Auditor