



Orange County Auditor-Controller Internal Audit



Audit of Unearned Revenue:
OC Community Resources

For the Year Ended
June 30, 2016

Audit Number 1619-B
Report Date: May 30, 2017



O R A N G E C O U N T Y
AUDITOR-CONTROLLER
I N T E R N A L A U D I T

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ERIC H. WOOLERY, CPA
AUDITOR-CONTROLLER



Transmittal Letter

Audit No. 1619-B

May 30, 2017

TO: Dylan Wright, Director
OC Community Resources

SUBJECT: Audit of Unearned Revenue:
OC Community Resources

We have completed our audit of internal controls over the recording of unearned revenue by OC Community Resources (OCCR) for the year ended June 30, 2016. Our final report is attached for your review.

I submit an **Audit Status Report** quarterly to the Audit Oversight Committee (AOC) and a quarterly report to the Board of Supervisors (BOS) where I detail any critical and significant audit findings released in reports during the prior quarter 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
- Lilly Simmering, Deputy Chief Operating Officer
- Cymantha Atkinson, Deputy Director of OCCR
- Thea Bullock, Director of Compliance, OCCR
- Connie Chang, Financial Planning Manager, OCCR
- Brian Rayburn, Business Office Manager, OCCR
- Tonya Riley, Director of Satellite Accounting Operations, Auditor-Controller
- Win Swe, Accounting Manager III, Auditor-Controller/OCCR Accounting
- Foreperson, Grand Jury
- Robin Stieler, Clerk of the Board of Supervisors
- Macias Gini & O'Connell LLP, County External Auditor



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OC Community Resources
Audit No. 1619-B*

For the Year Ended June 30, 2016

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Internal Auditor's Report

Audit No. 1619-B

May 30, 2017

TO: Dylan Wright, Director
OC Community Resources

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

SUBJECT: Audit of Unearned Revenue:
OC Community Resources

OBJECTIVES

We have completed our audit of internal controls over the recording of unearned revenue by OC Community Resources (OCCR) for the year ended June 30, 2016. We performed this audit in accordance with the FY 2016-17 Audit Plan and Risk Assessment approved by the Audit Oversight Committee and the Board of Supervisors. The purpose of this audit is to support an initiative to partner with the County's external auditors to leverage audit resources. Our audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing prescribed by the Institute of Internal Auditors. Our audit objectives were to:

1. Evaluate if internal controls over recording of unearned revenue in the County's financial system are adequate to ensure transactions are complete, accurate, valid, and processed timely.
2. Assist the external auditor function with its evaluation of unearned revenue.
3. Determine if the County's procedures for recording unearned revenue are efficient and effective, (e.g., no backlogs, duplication of work, manual processes that could benefit from automation).

RESULTS

Objective #1: Our audit found internal controls over recording of unearned revenue in the County's financial system are adequate to ensure transactions are complete, accurate, valid, and processed timely, with the following exception. We identified **one (1) Control Finding** regarding revenue accrual for expenditures incurred was not recorded.

Objective #2: Our audit assisted the external auditor function with its evaluation of unearned revenue.

Objective #3: Our audit did not disclose any instances concerning backlogs, duplication of work, or manual processes needing automation.

BACKGROUND

OCCR's mission is "Connecting People & Resources." The department was created through Board of Supervisors approval on March 18, 2008 and is made up of OC Animal Care, OC Community Services, OC Parks, and OC Public Libraries.



Internal Auditor’s Report

OC Animal Care provides refuge for animals in the 18 contract cities and unincorporated areas of Orange County, adoption services, promotes community outreach and education on responsible pet ownership, and enforces Federal, State, and local animal control laws.

OC Community Services links eligible customers to a wide variety of community resources that will help them achieve self-sufficiency, seeks and secures alternate sources of funding, provides safe, affordable, and accessible housing and shelter opportunities, and provides comprehensive employment assistance and development services.

OC Parks ensures that residents and visitors benefit from the regional parks system, educates and encourages residents and visitors to discover the parks system, responsibly manages public funds and revenues, and acquires, maintains and preserves parkland. On September 13, 2010, OC Parks was moved from the OC Public Works Department to OCCR. On June 14, 2016, the Board of Supervisors adopted Resolution No. 16-049 to approve the reorganization of OC Dana Point Harbor into OC Parks.

OC Public Libraries provides safe and easy access to libraries for the community, offers a broad spectrum of materials in multiple formats, provides the community with the best access to the collection, and delivers knowledgeable, friendly and experienced staff to support the information needs of the community.

Unearned Revenue

A basis of accounting for governmental funds exists where revenue is recognized when amounts are earned, measurable, and available. Known as the modified accrual basis of accounting, receiving alone is not sufficient to recognize revenue (cash basis accounting) and revenue recognition can occur before amounts are actually received (accrual basis of accounting). Revenues **received in advance** of meeting all the earning requirements are a liability and require an entry to balance sheet account Unearned Revenue. It is a liability of resources obtained prior to revenue recognition. For the year ended June 30, 2016, unearned revenue for OCCR was **\$3,088,734**.

Table 1 – Unearned Revenue Account Codes

Account Code	Account Name
9540	Unearned Revenue Received
9543	Law Enforcement Services
9544	Support Services
9550	Billed Unearned Revenue

SCOPE AND METHODOLOGY

Our audit examined OCCR’s processing of unearned revenue and related internal controls for the year ended June 30, 2016. Our audit included inquiry, auditor observation, and limited testing for assessing the adequacy of internal controls and compliance with established County and departmental procedures.

Scope Exclusions. Our audit did not include an audit of application controls over CAPS+ Financial and Purchasing System.



Internal Auditor's Report

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 generally 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 generally 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 find still not implemented or mitigated after the second Follow-Up Audit. Such open issues appear on the AOC 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 recommendation is 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 of the Treadway Commission (COSO) Internal Control – Integrated Framework. Our Internal Control Audit enhances and complements, but does not substitute for OCCR'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 control, 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 OCCR'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.



Internal Auditor's Report

ACKNOWLEDGEMENT

We appreciate the courtesy extended to us by the personnel of OCCR 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

Finding No. 1 – Errors Noted in Supplemental Schedules (Control Finding)

OCCR utilizes supplemental schedules to track the Office on Aging Area Plan program's activity, revenue recognition, and reconciliation. We identified the following errors in the Office on Aging's supplemental schedules used to record unearned revenue.

Table 2 – Review of Office on Aging Supplemental Schedules

Program Type	Amount	Observation
C1 – Federal	\$109,745	Incorrectly debited unearned revenue instead of a receivable since no funds were available.
C2 – Federal	\$68,225	Incorrectly debited unearned revenue instead of a receivable since no funds were available.
IIIB – Federal	\$64,257	Incorrectly debited a receivable instead of unearned revenue when funds are available.
IIIB – State	\$48,174	Incorrectly debited a receivable instead of unearned revenue when funds are available.
VIIA – Federal	\$16,140	Matching principle not met.
IIIE – Federal Direct	\$211,717	OCCR combined unearned revenue for IIE Direct (CA305, CA306 and Contractor Federal); however, if combined, matching principle is not met.

County Accounting Manual (CAM) Section 3.3, Governmental Funds, states, “Governmental Fund types (General Fund, Special Revenue Funds, Capital Projects Funds, Debt Service Funds and Permanent Funds) have different criteria for recognizing revenue under the modified accrual basis of accounting. Revenues that are not advance funded can only be considered “available” for accrual if the actual revenue is expected to be received within 60 days following the end of the fiscal year (on or before August 30). GASB 65 states that when revenue is unavailable, it should be recorded as a deferred inflow of resources until such time as the revenue becomes available.”

CAM J-2, Fiscal Year-End Procedures, Section 3, Revenue Accruals, states, “Revenues should be accrued for earned but uncollected revenues that equals or exceeds \$5,000. To record such accruals, an account receivable is recorded and revenue accounts are credited.”

There is a risk that information is not complete and financial statements are not accurate. An adjusting entry is not required as this amount is not material to the County's financial statements taken as a whole.

Recommendation No. 1:

We recommend OCCR ensure supplemental schedules are complete, accurate, and in conformity with management's authorization.



Detailed Findings, Recommendations, and Management Responses

OC Community Resources Management Response:

Concur. OCCR Accounting will use Departmental Balance Sheet Account (DBSA) in conjunction with Balance Sheet Account – Unearned Revenue Received (BSA 9540) in CAPS+ to account for advanced funds from each program. OCCR Accounting will reconcile the balance of BSA 9540 and each DBSA to supplemental schedules on a monthly basis. By recording advanced funds to the General Ledger by each program and reconciling monthly, there will be greater assurance that information is complete, accurate, and in conformity with management's authorization.



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: OC Community Resources Management Response



May 22, 2017

DYLAN WRIGHT
DIRECTOR
OC COMMUNITY RESOURCES

CYMANTHA ATKINSON
DEPUTY DIRECTOR
OC COMMUNITY RESOURCES

JENNIFER HAWKINS, DVM
DIRECTOR
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RENEE RAMIREZ
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JULIA BIDWELL
DIRECTOR
HOUSING & COMMUNITY
DEVELOPMENT & HOMELESS
PREVENTION

STACY BLACKWOOD
DIRECTOR
OC PARKS

HELEN FRIED
COUNTY LIBRARIAN
OC PUBLIC LIBRARIES

TO: Toni Smart, Director
Auditor-Controller, Internal Audit Division

RE: **AUDIT NO. 1619-B Audit of Unearned Revenue:
OC Community Resources**

The Auditor-Controller Internal Audit Division completed an audit of internal controls over the recording of unearned revenue by OC Community Resources as of June 30, 2016. Below are OC Community Resources' responses to the audit findings and recommendations, which have been reviewed and approved by the County Executive Office.

Finding No. 1 – Errors Noted in Supplemental Schedules (Control Finding)

Recommendation No. 1:

We recommend OCCR ensure supplemental schedules are complete, accurate, and in conformity with management's authorization.

OC Community Resources Management Response:

Concur - OCCR Accounting will use Departmental Balance Sheet Account (DBSA) in conjunction with Balance Sheet Account – Unearned Revenue Received (BSA 9540) in CAPS+ to account for advanced funds from each program. OCCR Accounting will reconcile the balance of BSA 9540 and each DBSA to supplemental schedules on a monthly basis. By recording advanced funds to the General Ledger by each program and reconciling monthly, there will be greater assurance that information is complete, accurate, and in conformity with management's authorization.

If you have any questions related to these responses, please contact Brian Rayburn, Business Office Manager, OC Community Resources at 714-480-2885.

Sincerely,

Signature

5/17/17

Date



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