

# Internal Audit Department

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

## Internal Control Audit:

### HEALTH CARE AGENCY CONTRACT DEVELOPMENT AND MANAGEMENT PAYMENT APPROVAL AND FISCAL MONITORING

For the Period April 1, 2010  
through March 31, 2011

**High  
Impact  
Audit**

During Fiscal Year 2010-11, the Health Care Agency Contract Development and Management section administered 496 human services contracts; approved over \$198 million in contract payments; and administered external, independent financial and compliance audits of HCA contractors and service providers.

We audited Health Care Agency Contract Development and Management (HCA/CDM) to evaluate the adequacy of internal controls for approving contract payments to ensure they are valid, supported, authorized, timely, and comply with contract terms and with County and HCA/CDM policies. We also evaluated fiscal monitoring process administered in CDM and performed by external audit firms. In addition, we evaluated efficiency and effectiveness of HCA/CDM's payment approval and fiscal monitoring processes.

Our audit found internal controls over HCA/CDM's payment approval and fiscal monitoring processes are adequate, with some exceptions, and provide reasonable assurance that contract payments are valid, supported, authorized, timely, and comply with contract terms and with County and HCA/CDM's policies. We found that fiscal monitoring audits are performed on contractors to ensure the propriety of program expenditures; however, these are conducted after the contract period ends. We identified **nine (9) Control Findings** to improve controls with regards to processing and approving invoices for payment, and for enhancing the fiscal monitoring process to ensure the proper use of County funds. HCA/CDM management agreed with all of the findings and recommendations.

AUDIT NO: 1030

REPORT DATE: SEPTEMBER 15, 2011

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**Deputy Director:** Eli Littner, CPA, CIA  
**Senior Audit Manager:** Michael Goodwin, CPA, CIA  
**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**

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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. 1030 September 15, 2011**

**TO:** David L. Riley, Director  
Health Care Agency

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

**SUBJECT:** Internal Control Audit: Health Care Agency  
Contract Development and Management  
Payment Approval and Fiscal Monitoring

We have completed an Internal Control Audit of the Health Care Agency Contract Development and Management Payment Approval and Fiscal Monitoring processes for the period April 1, 2010 through March 31, 2011. We performed this audit in accordance with our *FY 2010-11 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and the Board of Supervisors. Our final report is attached for your review.

Please note we have a structured and rigorous **Follow-Up Audit** process in response to recommendations and suggestions made by the Audit Oversight Committee (AOC) and the Board of Supervisors (BOS). Our **first Follow-Up Audit** will begin at 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. At the request of the AOC, we are to bring to their attention any audit recommendations we find still not implemented or mitigated after the second Follow-Up Audit. The AOC requests that such open issues appear on the agenda at their next scheduled meeting for discussion.

We have attached a **Follow-Up Audit Report Form**. Your agency should complete this template as our audit recommendations are implemented. When we perform our first Follow-Up Audit approximately six months from the date of this report, we will need to obtain the completed document to facilitate our review.

Each month I submit an **Audit Status Report** to the BOS where I detail any 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 BOS.

As always, the Internal Audit Department is available to partner with your staff so that they can successfully implement or mitigate difficult audit recommendations. Please feel free to call me should you wish to discuss any aspect of our audit report or recommendations. Additionally, we will request your department complete a **Customer Survey** of Audit Services. You will receive the survey shortly after the distribution of our final report.

### ATTACHMENTS

Other recipients of this report are listed on the **OC Internal Auditor's Report** on page 7.

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Health Care Agency  
Contract Development and Management  
Payment Approval and Fiscal Monitoring  
Audit No. 1030*

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Audit No. 1030

September 15, 2011

TO: David L. Riley, Director  
Health Care Agency

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

SUBJECT: Internal Control Audit: Health Care Agency  
Contract Development and Management  
Payment Approval and Fiscal Monitoring

## Audit Highlight

### Successes

HCA's Contract and Development Management (CDM) Division is responsible for developing, soliciting, negotiating, and administering human services contracts for HCA. During the audit period, CDM administered 496 contracts, many of which contain multiple funding sources and distinctly different programs. These human services contracts include public health, behavioral health, and medical and institutional health services. Contract providers include hospitals, clinics, educational institutions, and both for-profit and non-profit community based programs.

CDM's objective is to provide for the fiscal and operational integrity of HCA by utilizing the competitive bidding process to obtain the most cost effective services; providing effective and efficient contract development and administration; and providing oversight of contract services to safeguard the County's financial resources.

We identified **nine (9) Control Findings** to improve controls with regards to processing and approving contractor payments, and for enhancing the fiscal monitoring of contractors currently conducted by external audit firms.

## OBJECTIVES

In accordance with our *FY 2010-11 Audit Plan and Risk Assessment* approved by the Audit Oversight Committee and the Board of Supervisors, the Internal Audit Department conducted an Internal Control Audit of the Health Care Agency Contract Development and Management (HCA/CDM) Payment Approval and Fiscal Monitoring processes. Our audit included an evaluation of internal controls, testing compliance with HCA/CDM and County policies; and evaluating process efficiencies and effectiveness. Our audit was conducted in conformance with professional standards established by the Institute of Internal Auditors. The objectives of this audit were to:

1. Evaluate internal controls and processes for approving and contract disbursements to ensure payments are valid, supported, authorized, timely, and comply with contract terms and County and HCA/CDM policies.
2. Evaluate fiscal monitoring processes administered in HCA/CDM and performed by external firms for financial and compliance audits of program expenditures incurred by contractors using HCA funds.
3. Determine if the payment approval and fiscal monitoring processes 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 HCA/CDM's payment approval process are adequate, with some exceptions, and provide reasonable assurance that contract payments are valid, supported, authorized, timely, and comply with contract terms and with County and HCA/CDM policies. We identified **seven (7) Control Findings** to enhance controls over the payment approval process.

**Objective #2:** Our audit found that fiscal monitoring audits are performed by external audit firms to help ensure the propriety of program expenditures. However, these audits are conducted after the contract period ends and do not provide timely monitoring. We identified **one (1) Control Finding** in regard to HCA/CDM's use of Audit Tracking Logs for monitoring the external audits.

**Objective #3:** Our audit found the payment approval process is efficient and effective (e.g., no backlogs, duplication of work, manual processes that could benefit from automation); however, we noted where fiscal monitoring can be enhanced by performing fiscal reviews during the contract period. We identified **one (1) Control Finding** to evaluate conducting additional fiscal monitoring.

# OC Internal Auditor's Report



The following *Summary of Findings and Recommendations* shows our findings and recommendations based for this audit. See further discussion in the *Detailed Findings, Recommendations and Management Responses* section of this report. See *Attachment A* for a description of Report Item Classifications.

Finding No.	Finding Classification - see Attachment A	Finding	Recommendation	Concurrence by Management?	Page No. in Audit Report
1.	<b>Control Finding</b>	Invoice payment authorization limits and supervisory reviews of high dollar payments were not in place.	Evaluate establishing dollar thresholds by which Contract Administrators can approve invoice payments, and enhance supervisory reviews to include approving high dollar payments.	Yes	8
2.	<b>Control Finding</b>	A process to verify authorized contractor signatures should be established.	Establish a list of authorized contractor signatures to be maintained in contract files.	Yes	9
3.	<b>Control Finding</b>	Exceptions were noted in timeframes for receiving and paying contractor invoices.	Maintain documentation in contract files explaining delays in receiving and paying contractor invoices.	Yes	10-11
4.	<b>Control Finding</b>	Exceptions were noted in date-stamping contractor invoices upon receipt.	Ensure invoices are consistently date-stamped.	Yes	10-11
5.	<b>Control Finding</b>	Exceptions were noted in CDM's invoice processing timeframes.	Evaluate policy for invoice processing timeframes and document exceptions.	Yes	10-11
6.	<b>Control Finding</b>	Exceptions were noted in verifying contractor services prior to approving payments.	Ensure that all Fee-for-Service invoices obtain documented approval from HCA programs.	Yes	10-11
7.	<b>Control Finding</b>	Written Policies and Procedures Need Updating	Review, update, and communicate policies and procedures to reflect current expectations of management and department practices.	Yes	12
8.	<b>Control Finding</b>	Audit Tracking Logs were not updated completely.	Ensure External and Single Audit Tracking Logs are updated completely and contain relevant information for tracking audit status.	Yes	13
9.	<b>Control Finding</b>	Fiscal Monitoring Audits are conducted after the contract ending date.	Evaluate the feasibility of conducting on-going fiscal monitoring by performing on-site reviews of program expenditures during the contract period.	Yes	14-15



## BACKGROUND

HCA's mission is dedicated to "protecting and promoting the optimal health of individuals, families, and communities through partnerships; community leadership; assessment of community needs; planning & policy development; prevention & education; and providing quality services." Within HCA, **Financial and Administrative Services** provide internal support to HCA's varied divisions and programs as well as interfacing with HCA's external community organizations, contractors, and stakeholders. Under Financial and Administrative services, the **Contract Development and Management (CDM)** Division is responsible for developing, soliciting, negotiating, and administering human services contracts for HCA. CDM also administers the solicitation and coordination of external audit firms to conduct fiscal monitoring audits of HCA contractors.

### Contract Administration and Payment Approval

The objective of CDM is to provide for the fiscal and operational integrity of HCA by utilizing the competitive bidding process to obtain the most effective services; providing effective and efficient contract development and administration; and providing oversight of contract services to safeguard the County's financial resources.

During the audit period, CDM was administering **496 human services contracts totaling \$271 million**, many of which contain multiple funding sources and distinctly different programs. These human services contracts include public health, behavioral health, and medical and institutional health services. Contract providers include hospitals, clinics, educational institutions, and both for-profit and non-profit community based programs. A summary of contracts administered by CDM for **Fiscal Year 2010-11** is shown below:

Contracts	No.	Contract Amount	Percentage	Expenditures	Percentage
Behavioral Health Services	180	\$144,433,130	53%	\$136,935,575	69%
Medical/Institutional Health Services	175	118,545,864	44%	55,069,570	28%
Public Health Services	141	8,086,904	3%	6,869,910	3%
<b>Total</b>	<b>496</b>	<b>\$271,065,898</b>	<b>100%</b>	<b>\$198,875,055</b>	<b>100%</b>

CDM has three types of human services contracts:

- **Actual Cost Reimbursement:** HCA pays contractors for actual costs incurred and allowable business expenses as indicated in the program budget up to the maximum contract obligation. Actual cost reimbursement contracts can contain provisional payments or no provisional payments based on actual costs and budgeted amounts (further discussion provided below).
- **Fee-for-Service:** HCA pays contractors for actual services provided at a pre-determined rate (generally by hourly increments, sessions, or client) up to the maximum contract obligation.
- **Negotiated Contracts:** HCA pays contractors for services provided at a pre-determined, fixed amount up to the maximum contract obligation.

**Contract Administrators** in CDM have responsibility to coordinate Requests for Proposal (RFP) for soliciting proposals for contracted services; negotiating contract terms and amounts; preparing contracts; monitoring and analyzing contractor expenditures, revenue, and performance; providing technical assistance to contractors in budgeting and fiscal management; coordinating compliance training for all contractors; authorizing payments to contractors; and making recommendations to renew, terminate or amend contracts.



## CDM Payment Approval Process

Contract Administrators analyze monthly invoices/payment requests submitted by contractors in relation to current expenditures, make adjustments as required, and advise contract providers, program staff and the Supervisor Contract Administrator in CDM of concerns and/or budget trends. The Contract Administrator authorizes payment on monthly invoices and submits the approved invoices to HCA/Accounting for further review and processing. There are four different types of invoice payments that CDM receives and approves:

- Actual Cost with Provisional Payment Invoices  
Contractor is paid monthly, in arrears. First month's payment is at the provisional amount per the contract whereas, the following monthly payments are based on either the prior month's actual reported costs, the provisional amount, or a higher or lower amount at the Contract Administrator's discretion based on the monthly projection of budgeted amounts and actual costs incurred.
- Actual Cost with No Provisional Payment Invoices  
Contractor is paid monthly, in arrears. The monthly invoice for the preceding month is based on the contractor's actual costs and is paid up to the maximum contract obligation.
- Fee-for-Service Invoices  
Contractor is paid monthly, in arrears, based on services used and according to a service rate per the contract. For example, a contractor is paid based upon the number of services provided and authorized by HCA. In most instances, these invoices and supporting documentation are forwarded to HCA program staff for verification of services. Program staff approves the invoices and are returned to the Contract Administrator.
- Negotiated Contract Invoices  
Contractor is paid monthly based on a fixed negotiated amount per the contract.

## Contractor Expenditure and Revenue Reports

Contract Administrators are responsible for monitoring contractor expenditures, revenues, and productivity for their assigned contracts. In most cases, this is accomplished through preparation of a monthly Expenditure and Revenue Report. At the beginning of each fiscal year, a new Expenditure and Revenue Report is developed by the assigned Contract Administrator showing the following information:

- Expenditure, Revenue, and Contract Productivity/Workload consistent with contractual obligations.
- Monthly actual and projected amounts.
- Year to Date (YTD) amounts.
- Contract Budget.
- Variance (amount and percentage) of YTD Actual to Budget.
- Average Monthly Actual.
- Monthly Provisional Payment per contract (if applicable).
- Monthly Gross and Net Costs.
- Monthly Payment.
- YTD Variance of Monthly Cost and Monthly Payment.

The contractors complete the report monthly with actual information for line items. A copy of each monthly report is saved on the CDM server. No other supporting documents are required to be submitted by the contractors. Upon receipt of the reports from the contractors, Contract Administrators analyze information and discuss any concerns with the contractor for appropriate action/resolution; document notes and comments in the report; and revise projections, as appropriate. Upon completing their review of the Expenditure and Revenue Report and comparing the invoice to the terms and conditions of the contract, the Contract Administrators sign the invoices indicating their review and approval and send them to HCA Accounting. CDM's internal goal is to conduct review of monthly Expenditure and Revenue Report and approve payments within five (5) business days of the receipt of the contractor invoice.



Note that although most contracts have language requiring expenditure, revenue and productivity reports, not all contracts require this level of reporting. In those cases other types of reporting is required for monitoring the contractor cost and performance, such as Fee-for-Service contracts where reports of services provided are required.

## **Fiscal Monitoring**

HCA contracts for annual external independent audits for its human health services contract providers to ensure contract and fiscal compliance. CDM is responsible for procuring external audit services, developing a list of planned audits, tracking and monitoring the completion of external audits; ensuring follow-up on prior audit recommendations; and tracking audits that are performed on all contractors subject to the Single Audit Act (OMB Circular A-133).

The Internal Audit Department conducted an Internal Control Review of CDM in FY 2004-05 (Audit No. 2530). At that time, Contract Administrators were conducting Fiscal and Administrative Reviews in addition to contracting with external audit firms. The prior audit report contained recommendations concerning improvement needed in the timing, frequency and documentation of audits conducted by CDM staff. Subsequent to the audit, a decision was made to no longer have CDM staff perform Fiscal and Administrative Reviews. Instead, CDM has relied solely on external audit firms to conduct the fiscal reviews.

As part of enhancing contract monitoring, CDM established the Central Fiscal and Administrative Support (CFAS) Unit in December 2005. This unit was responsible for the coordination of external independent audits, as well as developing a tool and to provide staff training to conduct Fiscal and Administrative Reviews (FARs). FARs continued for approximately one year before they were discontinued in 2006. In 2007, CFAS was renamed as Audits, Reviews, Compliance, and HIPAA (ARCH). The ARCH Unit continued to procure external independent auditors to conduct financial and compliance audits of human health services contract providers. Audits are usually performed by one audit firm, but more than one may be used depending on need. Audit field work lasts from one to three days and a standard Audit Program is followed. Contractors are required to submit Final Cost Reports after 60 days of contract expiration. Audit work starts after receipt of the Final Cost Report and is used as a source to conduct the audit. It is the goal of ARCH Unit to conduct an independent audit of a contractor at least once every three years. Contracts contain language that authorizes these external audits. Information obtained from these audits is shared with Contract Administrators and program staff.

In addition, HCA is qualified as the recipient agency for State Department of Alcohol and Drug Program (ADP) funds. Alcohol and Drug Abuse Service (ADAS) contract providers are qualified sub-recipients of these funds. ADP requires all qualified sub recipients who satisfy the Single Audit requirements through the contract with the recipient agency, submit their Single Audits through the recipient agency. Therefore, ARCH Unit oversees the review of all Single Audits submitted by qualified sub-recipients and ensures reasonable follow up is conducted and that outcome is documented. All qualified sub-recipients subject to a Single Audit are identified at the beginning of the fiscal year and reminded of their submission requirements by end of each calendar year. Qualified sub-recipients under the Single Audit Act are organizations that receive in aggregate \$500,000 or more in federal award funds from any recipient agency.

During FY 2009-10, there were **102 external audits** planned to be conducted and that were completed. During FY 2010-11, there are **95 external audits** planned to be conducted. As of our audit fieldwork, these external audits are in process of being completed by June 30, 2011. ARCH Unit utilizes an External Audit Tracking Log to monitor the progress of the planned audits, and a Single Audit Tracking Log to monitor the submission of Single Audits to CDM.



## SCOPE AND METHODOLOGY

Our audit covered the period April 1, 2010 through March 31, 2011 and included the following:

1. Evaluated whether internal controls are in place and adequate for approving and contract disbursements to ensure payments are valid, supported, authorized, timely, and comply with contract terms, County, and HCA/CDM policies. We tested forty (40) invoices from different contract types.
2. Evaluated fiscal monitoring processes administered in HCA/CDM and performed by external firms for financial and compliance audits of program expenditures incurred by contractors using HCA funds. We evaluated the lists of planned audits, the adequacy of audit programs used by external auditors, audit reports, follow-up and close-out of audits, and the tracking logs used by CDM to monitor the progress of external audits.
3. Evaluated the efficiency and effectiveness of the payment approval and fiscal monitoring processes, such as for instances of backlogs, duplication of work, manual processes that could benefit from automation, etc.

## SCOPE EXCLUSIONS

Our audit scope did not include controls, policies and processes used for approving and processing contract disbursements in HCA Accounting Services because we conducted a separate audit of HCA's Payment Approval Process (Audit No. 1025). We also did not audit Administrative Contracts and contract procurement processes in HCA/CDM.

## 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 HCA'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 HCA's operating procedures, accounting practices, and compliance with County policy.

## Acknowledgment

We appreciate the courtesy extended to us by the Health Care Agency during our audit. If we can be of further assistance, please contact me directly or Eli Littner, Deputy Director at 834-5899 or Michael Goodwin, Senior Audit Manager at 834-6066.

## Attachments



Distribution Pursuant to Audit Oversight Committee Procedure No. 1:

Members, Board of Supervisors  
Members, Audit Oversight Committee  
Thomas G. Mauk, County Executive Officer  
Vacant, Deputy CEO, Government & Public Services, CEO  
Bob Wilson, Assistant Agency Director, HCA  
Jeff Nagel, Ph.D., Deputy Agency Director & Chief Compliance Officer, HCA  
Alice Moore, Division Manager, Contract Development and Management, HCA  
Rebecca Siddiqui, Manager, Contract Development and Management, HCA  
Foreperson, Grand Jury  
Darlene J. Bloom, Clerk of the Board of Supervisors



**Objective #1:** Evaluate internal controls and processes for approving and contract disbursements to ensure payments are valid, supported, authorized, timely, and comply with contract terms, County and HCA/CDM policies.

## Finding 1 – Invoice Payment Authorization Limits and Supervisory Reviews

### Summary

Contract Administrators in HCA/CDM are authorized to approve contractor invoice payments regardless of dollar amount for contracts assigned to them. There is no limit on amounts the Contract Administrators can approve for payment, and there is no supervisory review and approval required for high dollar payments or of the Contract Administrator's role in approving invoice payments. **(Control Finding)**

### Details

Contract Administrators in HCA/CDM are responsible for reviewing and approving contractor invoices for payment prior to submitting the invoices to HCA Accounting Services for further processing. Contract Administrators review invoices to ensure they are valid, supported by the required contractor Expenditure and Revenue Report, and the invoice information and costs agree to the terms and conditions of the contract. Certain invoices also require verification from program staff (Fee-for-Service contracts).

Our audit noted that there is no dollar amount limitation for Contract Administrators in their role of approving invoice payments, which in our **testing of forty (40) invoices**, ranged from \$600 up to \$2.7 million, with several monthly payments between \$100,000 and \$500,000. We also noted there is no documented supervisory review and approval process over payment approvals by the Contract Administrators to ensure they are performing their required responsibilities.

Per best business practices, a dollar amount limitation should be applicable to individuals who authorize disbursements by requiring two or more approvals for disbursements over a certain threshold, for example greater than \$100,000. Also, documented supervisory Contract Administrator reviews should be conducted periodically to monitor performance and compliance with payment approval policy and procedures.

Having dollar thresholds for payment approval and supervisory reviews of Contract Administrator's payment approval process decreases the risk of errors and misappropriation occurring.

### Recommendation No. 1

HCA/CDM evaluate establishing dollar thresholds by which Contract Administrators can approve invoice payments, and enhance the supervisory review process to include approving higher dollar payments and monitoring the payment approval process by Contract Administrators.

### Health Care Agency Management Response:

**Concur.** CDM will evaluate establishing a dollar threshold for supervisory approval prior to invoice authorization. CDM will review existing County best practices pertaining to invoice review and approval and determine appropriate dollar threshold for supervisory approval. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.



## Finding 2 – Verification of Authorized Contractor Signatures

### Summary

Contract Administrators in HCA/CDM are responsible for reviewing and approving contractor invoices. Invoices are received in HCA/CDM and are signed by an authorized individual on behalf of the contractor. Our audit noted that there is not a process in place in HCA/CDM to verify the individual signing the invoice is authorized by the contractor. **(Control Finding)**

### Details

Contractor invoices submitted to HCA/CDM are required to be signed by an authorized contractor representative. While our testing of forty (40) invoices did not disclose any instances where invoices lacked an authorized contractor signature, we noted HCA/CDM does not always verify the signature is by an authorized individual. An Authorized Contractor Signature List is not maintained in contract files to verify authorized the contractor personnel approval on invoices.

Best business practices include maintaining an updated list of authorized signatures for the purpose of verifying contractor personnel signatures placed on invoices requesting payment for services. This can be accomplished by identifying those individuals who can authorize invoices and including their names and signatures in the contract file.

Having a list of authorized individuals from contractors who can sign invoices and that Contract Administrators can verify against decreases the risk of unauthorized invoices being processed.

### Recommendation No. 2

HCA/CDM evaluate establishing a list of authorized contractor signatures to be maintained in contract files to help Contract Administrators verify the propriety of contractor signatures on invoices.

### Health Care Agency Management Response:

**Concur.** HCA/CDM will evaluate the need to establish a list of authorized contractor signatures, including identifying any risks with existing process. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.



## Findings 3-6 – Invoice Processing: Receipt, Date-Stamping, Processing Timeframes, and Verification of Services

### Summary

Our testing of forty (40) contractor invoices found that most invoices were processed in accordance with established procedures; however, we noted seven (7) were submitted late by the contractor without an explanation of the delay; three (3) were not date-stamped per procedures; six (6) invoices were not processed within HCA/CDM's goal of five business days; and three (3) invoices did not obtain HCA program verification. **(Control Finding)**

### Details

**Receipt of Invoices from Contractors.** Contracts in HCA/CDM generally have a provision whereby the contractor is paid monthly, in arrears. Monthly invoices for the preceding month are due on designated day of the current month depending on the type of contract (e.g., a January invoice is due to HCA/CDM by February 10<sup>th</sup>). Our testing of forty (40) contractor invoices found that seven (7) were submitted late by the contractor (from 2 to 44 days) after the required due date. There was no documentation explaining why the invoice was submitted late either on the invoice or in the contract file.

Late submission of invoices without an explanation of the delay results in non-compliance with contract terms and delays payments to the contractors. We did not see any other consequences for late submission of invoices by contractors. Although it is not in HCA/CDM's control when contractors submit invoices, they should ensure there is documentation for the delay.

**Date-Stamping of Invoices.** The Front Office support staff in HCA/CDM receives invoices, date stamps and forwards them to the assigned Contract Administrator for review and signature. After the Contract Administrator's approval, the invoices are submitted back to the Front Office. The Front Office date stamps the invoices with date of delivery to HCA/Accounting. Our testing of forty (40) invoices found most were properly date-stamped; however, three (3) were not date-stamped due to oversight by staff. Lack of date-stamping does not enable HCA/CDM to determine if they are processing invoices within their goal of five (5) business days upon receipt of the invoices.

**Invoice Processing Timeframes.** HCA/CDM's unwritten policy is to process invoices within five (5) business days after receipt. This allows time for the Contract Administrators to verify the invoice with the terms of the contract and to review the contractor's Expenditure and Revenue Report. Sometimes verification from programs is required for "Fee-for Service" contracts. Our testing found six (6) of forty (40) invoices reviewed were not processed within five business days, and there was no documentation in the contract file on why processing was delayed.

**Verification of Fee-for-Service Invoices.** Upon receipt of invoices that involve a fee-for-service contract, the Contract Administrator verifies the invoiced amount with appropriate HCA program staff who signs the invoice specifying confirmation of the receipt of goods/services with program's database and that the billing is correct. Our testing of ten (10) fee-for-service invoices found two (2) that did not have program verification of services provided. Verifying the services provided helps prevent errors and misappropriation of funds by contractors.



### **Recommendation No. 3**

HCA/CDM ensure there is documentation maintained in the contract files explaining the delay in receiving contractor invoices after the required due date.

#### **Health Care Agency Management Response:**

**Concur.** HCA/CDM will review existing contract language and will propose to change contract language to clarify that invoices are due on the 10<sup>th</sup> of each month, and are late by the 30<sup>th</sup> of each month. Contract Administrators will document in contract file when invoices are not received by the 30<sup>th</sup> of the month. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.

### **Recommendation No. 4**

HCA/CDM ensure invoices are consistently date-stamped upon receipt from the contractor and when submitted to HCA Accounting Services.

#### **Health Care Agency Management Response:**

**Concur.** HCA/CDM will ensure that invoices are consistently date-stamped upon receipt from contractor and when submitted to HCA Accounting. Staff will ensure desk procedures are up-to-date and staff is trained by September 30, 2011. The desk procedure will be reviewed and updated, if needed, by October 30, 2011 to ensure compliance with recommendation. Any update will be shared with staff within 15 days of desk procedure update and during new employee training.

### **Recommendation No. 5**

HCA/CDM evaluate its invoice processing timeframe policy and ensure that exceptions are documented accordingly in contract files.

#### **Health Care Agency Management Response:**

**Concur.** HCA/CDM will review invoice processing and update the policy and procedure to reflect a formal protocol for reviewing invoices and documenting delays in invoice processing. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.

### **Recommendation No. 6**

HCA/CDM ensure that all Fee-for-Service invoices document approval from HCA programs. In instances where program verification is not needed, there should be documentation maintained in the contract files explaining why program verification was not needed.

#### **Health Care Agency Management Response:**

**Concur.** HCA/CDM will ensure all Fee-For-Service invoices requiring approval from HCA Program staff are documented on the invoice. File documentation will be maintained in contract file for those that do not require Program verification. Any applicable policy and procedure will be in place no later than January 30, 2012.



## Finding 7 – Written Policies and Procedures Need Updating

### Summary

HCA/CDM has written procedures describing the responsibilities of Contract Administrators and for HCA/CDM's responsibilities with external audit firms to provide fiscal monitoring and Single Audits of contractors. Although the existing procedures are detailed and provide guidance to staff, we noted some of the procedures are "draft" versions and/or were not updated to reflect current processes. **(Control Finding)**

### Details

Based on our review of HCA/CDM's written policy and procedures, we noted the following:

- The policy and procedure for *Contract Administrator Responsibilities* is not updated to reflect current processes. The procedures were last revised in October 2005 when contract administrators were involved in performing fiscal monitoring audits. They no longer perform fiscal monitoring themselves; instead it is done by external audit firms.
- The policy and procedure for *Expenditure/Revenue Report & Invoice Processing* is not updated to reflect current processes. It was last revised in October 2005 and only includes procedures for processing invoices for 'Actual Cost with Provisional Payments' and not other types of contract invoices.

Also concerning the monthly Expenditure and Revenue Reports received from contractors, we noted the variance calculation is not shown correctly in the reports. The positive variance between actual payment and actual costs should be reported as "overpayment" whereas, a negative variance should be reported as "underpayment." Currently, the Expenditure and Revenue Report labels positive variance as "underpayment" and negative variance as "overpayment." This should be evaluated and clarified in the policy.

- The policy and procedures for *External Independent Audits* and *Contract Provider's Single Audit Review* are in draft form, and have not been dated or approved by management.

Current written procedures help provide guidance to new staff and ensure consistency in work performed. Written procedures should be periodically reviewed and updated to ensure they are relevant and useful.

### Recommendation No. 7

HCA/CDM review, update, and communicate policies and procedures as needed that reflect current expectations of management and department practices. This includes evaluating how the variance calculations are reported in the Expenditure and Revenue Reports.

### Health Care Agency Management Response:

**Concur.** HCA/CDM staff will review, update, and communicate policies and procedures that reflect current departmental practices. Any applicable policy and procedure will be in place no later than January 30, 2012. The variance calculation will be correctly labeled on FY 2011-12 Expenditure and Revenue Reports no later than October 30, 2011.



**Objective #2:** Evaluate fiscal monitoring processes administered in HCA/CDM and performed by external firms for financial and compliance audits of program expenditures incurred by contractors using HCA funds.

## Finding 8 – Completion of Audit Tracking Logs

### Summary

HCA/CDM contracts with external audit firms to conduct fiscal monitoring of its contractors. Additionally, they track and monitor all Single Audits required of its contractors that are conducted by external auditors. The ARCH Unit in HCA/CDM utilizes External and Single Audit Tracking Logs in administering the external audits for purposes of tracking planned and completed audits, for identifying issues found during the external audits, and for submission of Single Audit Reports. While they can be an effective tool, we noted the Audit Tracking Logs were not completely updated, and lacked certain information about the audits, such as the entrance/exit meeting dates, audit completion and close-out dates, and follow-up status of prior findings. **(Control Finding)**

### Details

As part of enhancing contract monitoring, HCA/CDM established an Audits, Reviews, Compliance, and HIPAA (ARCH) Unit to provide additional oversight of contracted services. The ARCH Unit's responsibilities include procuring external independent auditors to conduct financial and compliance audits and monitoring the status of the external audits and Single Audits of contract providers.

It should be noted that when we last audited HCA/CDM in 2005, they had staff assigned to perform fiscal monitoring reviews of contractors in addition to hiring services of external audit firms to conduct financial and compliance audits. Sometime in 2007, a decision was made to no longer have HCA/CDM staff perform fiscal reviews. The ARCH Unit was established and developed External Audit and Single Audit Tracking Logs to monitor the completion of planned audits and submission of Single Audits for each fiscal year.

Our current audit noted that while the External Audit and Single Audit Tracking Logs contain detailed information to track audit status, some of the logs were not updated (such as the columns for entrance date, exit date); the logs showed no information as to when the audit was completed, when the report was issued, and the contract audit period was officially closed-out; and did not show when Single Audit reports were received by ARCH Unit and were sent to the State.

We commend HCA/CDM for using these Audit Tracking Logs as a tool to monitor the status of external and Single Audits, and believe they can be improved by completing all relevant information, including audit start and completion dates.

### Recommendation No. 8

HCA/CDM ensure its External and Single Audit Tracking Logs are updated completely and contain relevant information for tracking audit status, such as audit start dates, completion dates and follow-up status on prior audit findings.

### Health Care Agency Management Response:

**Concur.** HCA/CDM will ensure that tracking logs are updated no later than 60 days after the completion of an audit. Any applicable policy and procedure will be modified no later than January 30, 2012.



**Objective #3:** Determine if the payment approval and fiscal monitoring processes are efficient and effective (e.g., no backlogs, duplication of work, manual processes that could benefit from automation).

## Finding 9 – Timing of Fiscal Monitoring Audits

### Summary

Our audit found that external fiscal monitoring audits are conducted after the contract period ends, and after the contractor submits a Final Cost Report due 60 days after contract expiration. To ensure proper use of County funds, HCA/CDM should evaluate the feasibility of conducting fiscal monitoring reviews during the contract period instead of after contract expiration. Auditing contract expenditures after the contract period increases the risk that program funds could be misused and not be detected timely. **(Control Finding)**

### Details

HCA/CDM procures the services of external audit firms to conduct independent audits of contract providers to ensure compliance with contract requirements and for fiscal monitoring of expenditures using County funds. Fiscal monitoring audits can be performed by one audit firm, but more than one may be used depending on the need. HCA/CDM no longer conducts fiscal monitoring reviews.

During our audit period, HCA/CDM utilized four external audit firms to conduct fiscal monitoring audits. Audit fieldwork generally lasts from 1 to 3 days and a standard Audit Program is followed. Contractors are required to submit Final Cost Report after 60 days of contract expiration. Audit fieldwork starts after receipt of the Final Cost Report and used as a source to conduct the audit. It is the goal of the ARCH Unit to conduct an independent audit of a contractor at least once every three years. Contracts contain language that authorizes these external audits. Information obtained from these audits is shared with Contract Administrators and Program Staff for purposes of amending or renewing contracts with the service providers.

Our review of the external audit reports and Audit Tracking Logs found that the external audits have identified a variety of findings, but were audited and reported after the contract period had expired. Some of these contracts had been renewed, in which case there is recourse in the event any serious audit issues were identified. In FY 2009-10, there were 102 external audits planned to be conducted on FY 2008-09 and on earlier period contracts. All have been completed. In FY 2010-11, there are 95 external audits planned to be conducted on FY 2009-10 and earlier period contracts. As of our fieldwork, these external audits are in process to be completed by June 30, 2011.

Auditing contract expenditures after the contract period increases the risk that program funds could be misused and not be detected timely. There have been instances of past contractors not using funds in compliance with contract terms. Also, contractors generally do not submit any support documentation showing how program funds were used except for the monthly Expenditure and Revenue Report submitted with invoices.

HCA/CDM should evaluate the feasibility of conducting on-going fiscal monitoring, specifically to ensure the proper use of County funds, during the contract period. The scope of the fiscal monitoring during the contract period can be limited to testing expenditures, and could be performed during site visits by Contract Administrators. External audits, which have a broader audit scope and objectives, could still be performed after the contract period ends.

Because there is limited documentation submitted by the contractors with their monthly invoices, and contract terms can range up to three years, we believe it is important to perform on-going fiscal monitoring during the contract period to detect any significant findings.



## **Recommendation No. 9**

HCA/CDM evaluate the feasibility of conducting on-going fiscal monitoring by performing on-site reviews of program expenditures during the contract period in addition to the fiscal monitoring performed by external audits after the contract period ends.

### **Health Care Agency Management Response:**

**Concur.** HCA/CDM will evaluate the feasibility and resource impact of conducting on-going fiscal monitoring by performing a sample set of on-site reviews of contractor's expenditures during the contract period by February 12, 2012.



## ATTACHMENT A: Report Item Classifications

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

- ▶ **Critical Control Weaknesses:**  
Audit findings or a combination of Significant Control Weaknesses that represent serious exceptions to the audit objective(s) and/or business goals. Management is expected to address Critical Control Weaknesses brought to their attention immediately.
- ▶ **Significant Control Weaknesses:**  
Audit findings or a combination of Control Findings that represent a significant deficiency in the design or operation of internal controls. Significant Control Weaknesses require prompt corrective actions.
- ▶ **Control Findings:**  
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.



## ATTACHMENT B: Health Care Agency Management Responses



*Excellence  
Integrity  
Service*

### COUNTY OF ORANGE HEALTH CARE AGENCY

#### OFFICE OF THE DIRECTOR

DAVID L. RILEY  
DIRECTOR

BOB WILSON  
ASSISTANT DIRECTOR

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September 2, 2011

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

**SUBJECT:** Internal Control Audit: Health Care Agency/ Contract Development and Management  
Payment Approval and Fiscal Monitoring – Audit 1030 – Response  
Revisions to Finding and Recommendation No. 5

**ATTENTION:** Mike Goodwin, Senior Audit Manager

On August 31, 2011, the Health Care Agency (HCA) submitted its management responses to your department regarding HCA Contract Development and Management (CDM) Payment Approval and Fiscal Monitoring Audit 1030. Subsequent to this submittal, modifications to Finding No. 5 and its Recommendation were instituted. Below summarizes the revisions to the Control Finding and the Recommendation as we understand it, and a corresponding HCA revised Management Response. Please incorporate our response to the revised Recommendation #5 below into the final report as appropriate.

**Finding No. 5 - Invoice Processing Timeframes:** HCA/CDM's unwritten policy is to process invoices within five (5) business days after receipt. This allows time for the Contract Administrators to verify the invoice with the terms of the contract and to review the contractor's Expenditure and Revenue Report. Sometimes verification from programs is required for "Fee-for Service" contracts. Our testing found six (6) of forty (40) invoices reviewed were not processed within five business days, and there was no documentation in the contract file on why processing was delayed. Documenting reasons for delays establishes accountability and responsibility over invoice processing timeframes.

**Recommendation No. 5:**

HCA/CDM evaluate its invoice processing timeframe policy and ensure that expectations are documented accordingly in contract files.

**Health Care Agency Management Response: Concur.** HCA/CDM will review invoice processing and update the policy and procedure to reflect a formal protocol for reviewing invoices and documenting delays in invoice processing. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.

Should you have any further questions, please contact Alice Moore, HCA Contract Development and Management, at (714) 834-2848.

  
David L. Riley, Director

DLR:amo 11-078

cc: Thomas G. Mauk, County Executive Officer  
Bob Wilson, Assistant Director, HCA  
Jeff Nagel, Ph.D., Deputy Agency Director & Chief Compliance Officer, HCA  
Alice Moore, Division Manager, Contract Development and Management, HCA



## ATTACHMENT B: Health Care Agency Management Responses (continued)



*Excellence  
Integrity  
Service*

### COUNTY OF ORANGE HEALTH CARE AGENCY

OFFICE OF THE DIRECTOR

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August 30, 2011

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

**SUBJECT:** **Internal Control Audit: Health Care Agency  
Contract Development and Management  
Payment Approval and Fiscal Monitoring – Audit 1030 - Responses**

The Health Care Agency (HCA) has received the Internal Control Audit of the Health Care Agency Contract Development and Management Payment Approval and Fiscal Monitoring for the period of April 1, 2010 through March 31, 2011. As requested, below summarizes the nine (9) control finding and response from the Health Care Agency Management.

#### **Finding 1 – Invoice Payment Authorization Limits and Supervisory Reviews**

##### **Recommendation No. 1:**

HCA/CDM evaluate establishing dollar thresholds by which Contract Administrators can approve invoice payments, and enhance the supervisory review process to include approving higher dollar payments and monitoring the payment approval process by Contract Administrators.

**Health Care Agency Management Response: Concur.** CDM will evaluate establishing a dollar threshold for supervisory approval prior to invoice authorization. CDM will review existing County best practices pertaining to invoice review and approval and determine appropriate dollar threshold for supervisory approval. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.

#### **Finding 2 – Verification of Authorized Contractor Signatures**

##### **Recommendation No. 2:**

HCA/CDM evaluate establishing a list of authorized contractor signatures to be maintained in contract files to help Contract Administrators verify the propriety of contractor signatures on invoices.



## ATTACHMENT B: Health Care Agency Management Responses (continued)

Internal Control Audit: HCA Payment Approval and Fiscal Monitoring- Responses  
August 30, 2011  
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**Health Care Agency Management Response: Concur.** HCA/CDM will evaluate the need to establish a list of authorized contractor signatures, including identifying any risks with existing process. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.

### **Finding 3-6 – Invoice Processing: Receipt, Date-Stamping, Processing Time frames, and Verification of Services**

#### **Recommendation No. 3:**

HCA/CDM ensure there is documentation maintained in the contract files explaining the delay in receiving contractor invoices after the required due date.

**Health Care Agency Management Response: Concur.** HCA/CDM will review existing contract language and will propose to change contract language to clarify that invoices are due on the 10<sup>th</sup> of each month, and are late by the 30<sup>th</sup> of each month. Contract Administrators will document in contract file when invoices are not received by the 30<sup>th</sup> of the month. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.

#### **Recommendation No. 4:**

HCA/CDM ensure invoices are consistently date-stamped upon receipt from the contractor and when submitted to HCA Accounting Services.

**Health Care Agency Management Response: Concur.** HCA/CDM will ensure that invoices are consistency date-stamped upon receipt from contractor and when submitted to HCA Accounting. Staff will ensure desk procedures are up-to-date and staff are trained by September 30, 2011. The desk procedure will be reviewed and updated, if needed, by October 30, 2011 to ensure compliance with this recommendation. Any update will be shared with staff within 15 days of desk procedure update and during new employee training.

#### **Recommendation No. 5:**

HCA/CDM document explanations in contract files or on the invoices when the invoice processing time exceeds their goal of five business days.

**Health Care Agency Management Response: Partially Concur.** HCA/CDM will review invoice processing and update the policy and procedure to reflect a formal protocol for reviewing invoices and documenting delays in invoice processing. Any applicable policy and procedure will be created and/or modified to include this change no later than January 30, 2012.



## ATTACHMENT B: Health Care Agency Management Responses (continued)

Internal Control Audit: HCA Payment Approval and Fiscal Monitoring- Responses  
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**Recommendation No. 6:**

HCA/CDM ensure that all Fee-for-Service invoices document approval from HCA programs. In instances where program verification is not needed, there should be documentation maintained in the contract files explaining why program verification was not needed.

**Health Care Agency Management Response: Concur.** HCA/CDM will ensure all Fee-For-Service invoices requiring approval from HCA Program staff are documented on the invoice. File documentation will be maintained in contract file for those that do not require Program verification. Any applicable policy and procedure will be in place no later than January 30, 2012.

**Finding 7 – Written Policies and Procedures Need Updating**

**Recommendation No. 7:**

HCA/CDM review, update, and communicate policies and procedures as needed that reflect current expectations of management and department practices. This includes evaluating how the variance calculations are reported in the Expenditure and Revenue Reports.

**Health Care Agency Management Response: Concur.** HCA/CDM staff will review, update and communicate policies and procedures that reflect current departmental practices. Any applicable policy and procedure will be in place no later than January 30, 2012. The variance calculation will be correctly labeled on FY 2011-12 Expenditure and Revenue Reports no later than October 30, 2011.

**Finding 8 – Completion of Audit Tracking Logs**

**Recommendation No. 8:**

HCA/CDM ensure its External and Single Audit Tracking Logs are updated completely and contain relevant information for tracking audit status, such as audit start dates, completion dates and follow-up status on prior audit findings.

**Health Care Agency Management Response: Concur.** HCA/CDM will ensure that tracking logs are updated no later than 60 days after the completion of an audit. Any applicable policy and procedure will be modified no later than January 30, 2012.

**Finding 9 – Timing of Fiscal Monitoring Audits**

**Recommendation No. 9:**

HCA/CDM evaluate the feasibility of conducting on-going fiscal monitoring by performing on-site reviews of program expenditures during the contract period in addition to the fiscal monitoring performed by external audits after the contract period ends.

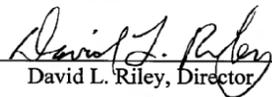


## ATTACHMENT B: Health Care Agency Management Responses (continued)

Internal Control Audit: HCA Payment Approval and Fiscal Monitoring- Responses  
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**Health Care Agency Management Response: Concur.** HCA/CDM will evaluate the feasibility and resource impact of conducting on-going fiscal monitoring by performing a sample set of on-site reviews of contractor's expenditures during the contract period by February 12, 2012.

HCA appreciates the collaborative approach taken by Internal Audit in the finalizing of the report and in providing assistance in understanding the findings noted. Should you have any further questions, please contact Alice Moore, HCA Contract Development and Management, at (714) 834-2848.

  
David L. Riley, Director

DLR:amo 11-076

cc: Thomas G. Mauk, County Executive Officer  
Bob Wilson, Assistant Director, HCA  
Jeff Nagel, Ph.D., Deputy Agency Director & Chief Compliance Officer, HCA  
Alice Moore, Division Manager, Contract Development and Management, HCA