



February 8, 2017

To: Finance and Administration Committee

From: Darrell Johnson, Chief Executive Officer

Janet Sutter, Executive Director
Internal Audit Department

Subject: Fiscal Year 2016-17 Internal Audit Plan, Second Quarter Update

Overview

The Orange County Transportation Authority Board of Directors adopted the Fiscal Year 2016-17 Internal Audit Plan on July 25, 2016. This update is for the second quarter of the fiscal year.

Recommendation

Receive and file the second quarter update to the Orange County Transportation Authority Fiscal Year 2016-17 Internal Audit Plan as an information item.

Background

The Internal Audit Department (Internal Audit) is an independent appraisal function, the purpose of which is to examine and evaluate the Orange County Transportation Authority's (OCTA) operations and activities to assist management in the discharge of its duties and responsibilities.

Internal Audit performs a wide range of auditing services that include overseeing the annual financial and compliance audits, conducting operational and contract compliance reviews, investigations, pre-award price reviews, and Buy America reviews. Audits initiated by entities outside of OCTA are coordinated through Internal Audit.

Discussion

The OCTA Fiscal Year (FY) 2016-17 Internal Audit Plan (Plan) (Attachment A) reflects the status of each audit project. At quarter end, several audit projects are in process.

During the second quarter of the FY, Internal Audit issued the Review of Investments: Compliance, Controls, and Reporting for the period January 1 through June 30, 2016, concluding that OCTA complied with its debt, investment, and reporting policies and procedures.

Financial and compliance audits of eight Measure M2 Comprehensive Transportation Funding Programs Projects were also issued by the external audit firm BCA Watson Rice, LLP. The auditors recommended OCTA recover \$4,500 from the City of Laguna Niguel (City) to reimburse an overpayment due to a calculation error in the City's final cost claim. Also, the auditors recommended the City enhance controls to ensure accuracy of final cost claims. OCTA staff has received the recommended reimbursement, and the City has asserted that enhanced controls have been implemented. In addition to the auditors' recommendations, Internal Audit issued a supplemental recommendation to OCTA management to include procedures for monitoring the progress of local agencies' match expenditures under the Environmental Cleanup Program, and report shortfalls to the Board of Directors (Board) through the semi-annual review reports. Management agreed and indicated that procedures will be incorporated into the semi-annual review manual.

The primary focus of Internal Audit during the quarter was to provide coordination of the annual financial and compliance audits by OCTA's independent financial statement auditor, Vavrinek, Trine, Day & Company, LLP (VTD). In connection with the audits, VTD made four recommendations to management related to enhanced information system security. Management agreed with the recommendations and outlined actions to address the issues. The Finance and Administration Committee requested additional detail relating to the management responses which was incorporated into the Board agenda presented on January 23, 2017.

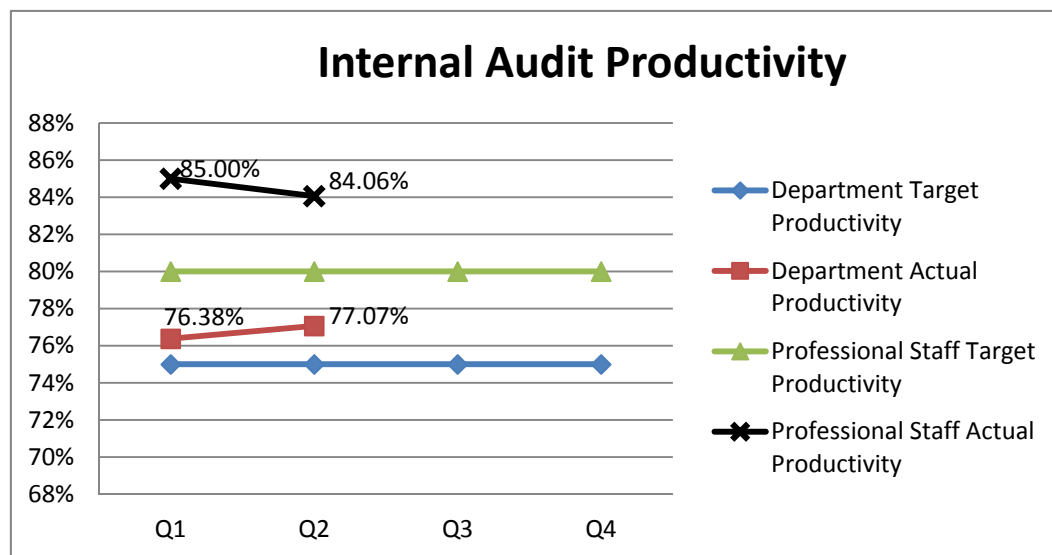
During the third quarter, Internal Audit will continue to provide coordination of Measure M2 agreed-upon procedures reviews of several cities and the County of Orange.

Finally, an audit by the Department of Finance, on behalf of the California Department of Transportation, of Proposition 1B funds utilized on five grade separation projects and the Oso Parkway Widening Project will commence early in the third quarter. Internal Audit will provide coordination and oversight and will report final results once they are available.

Internal Audit Productivity

Internal Audit measures the productivity of the department by calculating a productivity ratio. The ratio, used broadly throughout the audit industry, measures the amount of time auditors spend on audit projects versus time spent on administrative duties. Productivity goals are established for both the professional staff and for the department as a whole. Because the Executive Director regularly participates in non-audit management activities such as planning and committee meetings, the department-wide target is set at 75 percent. The target for internal audit professional staff, not including the Executive Director, is 80 percent.

For the quarter ended December 31, 2016, Internal Audit achieved productivity of 77 percent, and the professional staff achieved productivity of 84 percent.



Price Reviews

At the request of the Contracts Administration and Materials Management Department (CAMP), and consistent with OCTA procurement policy, Internal Audit conducts reviews of single bid procurements to ensure that CAMP handled the procurement in a fair and competitive manner. Internal Audit also reviews prices proposed by architectural and engineering firms, and sole source contractors to ensure that the prices are fair and reasonable. Internal Audit makes recommendations to adjust proposed rates where they exceed the rates per review. When the value of recommended adjustments can be estimated, Internal Audit tracks and reports the potential savings, as noted below. During the quarter ended December 31, 2016, Internal Audit

conducted two pre-award agreed-upon procedures reviews and recommended price adjustments, as indicated below:

Quarter	Price Reviews Recommended Adjustments
1	\$ 662,136
2	197,557
3	
4	
Total	\$ 859,693

Fraud Hotline

During the quarter ended December 31, 2016, Internal Audit received and investigated two reports through OCTA's Fraud Hotline, www.ethicspoint.com. No findings or recommendations resulted from these investigations.

Internal Audit is committed to responding to all hotline complaints within eight business days. During the quarter ended December 31, 2016, Internal Audit made initial contact within two business days.

Monitoring Activities – Metrolink Audit Results

Independent accounting firm Moss Adams, LLP, issued an unmodified opinion on Metrolink's financial statements for the year ended June 30, 2016; however, the accompanying report included five deficiencies in internal control that were considered to be material weaknesses or significant deficiencies. The acting Internal Audit Manager, Ms. Lazuardi, has indicated that an update on the status of management actions to address these findings will be provided at the Executive Management and Audit Committee meeting scheduled for May 2017.

Findings and Recommendations Tracking

At the request of the Finance and Administration Committee, unresolved audit recommendations are included with the quarterly updates to the Plan as Attachment B. Internal Audit includes findings and recommendations generated internally, as well as those provided by regulatory auditors and OCTA's independent financial statement auditors.

During the quarter ended December 31, 2016, Internal Audit performed follow-up of fourteen unresolved audit recommendations. Nine

recommendations were addressed by management and were removed from the list. Two recommendations relating to the Investigation of the Deferred Compensation Plan Administration were partially addressed and remain open pending additional actions. Follow-up review of another recommendation relating to the Accounts Payable audit resulted in the identification of additional exceptions and recommendations. As such, the item will be reviewed again in six months. Lastly, two recommendations related to the audit of the Bristol Street Widening Project remain open pending implementation of management reviews of the City of Santa Ana's quarterly reconciliation documentation. Implementation of this oversight process was held up due to delays in executing an amendment to the cooperative agreement, which was completed in January 2017.

One supplemental recommendation made by Internal Audit resulting from the financial and compliance audits of eight Measure M2 Comprehensive Transportation Funding Programs Projects was added to the list. Also added to the list were the recommendations made by VTD in connection with their financial audit.

Summary

Internal Audit will continue to implement the Plan, report on performance metrics, follow-up on outstanding audit recommendations, and report progress on a quarterly basis.

Attachments

- A. Orange County Transportation Authority Internal Audit Department Fiscal Year 2016-17 Internal Audit Plan, Second Quarter Update
- B. Outstanding Audit Findings and Recommendations (Audit Reports Issued Through December 31, 2016)

Prepared by:



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