March 8, 2017

To: Finance and Administration Committee

From: Darrell Johnson, Chief Executive Officer

              Janet Sutter, Executive Director
              Internal Audit Department

Subject: Budget Development, Monitoring, and Reporting, Internal Audit
              Report No. 16-509

Overview

The Internal Audit Department has completed an audit of budget development, monitoring, and reporting. Based on the audit, controls are generally adequate; however, recommendations were made to enhance and expand written procedures, to improve controls over salary grade changes, to adhere to the Position Control Policy, and to improve estimates and explanations included with the Sole Source List.

Recommendation

Direct staff to implement four recommendations provided in Budget Development, Monitoring, and Reporting, Internal Audit Report No. 16-509.

Background

Every year, the Orange County Transportation Authority develops its staffing, operating, and capital plans for the upcoming fiscal year (FY). The product of this effort is an approved FY budget. The Financial Planning and Analysis staff, within the Finance and Administration Division (F&A) is responsible for inputting budget assumptions, providing training and support to the user departments, meeting with project management and executive management, and addressing concerns from committees prior to the public hearing.

Also, as part of the budget, the Human Resources and Organizational Development Division (HROD) submits an annual Personnel and Salary Resolution (P&SR) for Board of Directors (Board) approval. The P&SR outlines general policies regarding employment practices, employee benefits,

compensation, and salary structure for administrative employees. The FY 2016-17 P&SR included changes in salary grades for multiple classifications, along with a statement that the changes resulted from a compensation study conducted by a consultant.

Also, in conjunction with approving the budget, the Board approves an annual Sole Source List developed by the Information Systems Department within F&A. The Sole Source List contains details of software and hardware licensing and maintenance agreements that have been executed with developers on a sole source basis.

Quarterly, F&A staff prepare and submit quarterly budget status reports to the Finance and Administration Committee and the Board.

Discussion

Budget policies, calendars, and forms are maintained; however, there are no written procedures on the development of salary and benefit budget assumptions and the budget transfer process. In addition, the Internal Audit Department (Internal Audit) identified some salary and benefit budget assumptions that appear to overstate budget expenditures. Finally, written procedures for budget to actual reporting include requirements to investigate variances in individual projects exceeding a set threshold; however, several projects with variances exceeding the threshold were not investigated. Internal Audit recommended that F&A develop certain procedures, including re-evaluating and documenting budget assumptions and requiring specific approvals for special budget transfers. Also, F&A should ensure that project variances are investigated as required by procedures. F&A agreed to re-evaluate and document salary and benefit budget assumptions and to outline approvals for budget transfers requiring explanation for special circumstances. Finally, F&A advised that investigation requirements will be clarified and adhered to.

The Board-approved P&SR included upgrades to job classifications which were attributed to a consultant-prepared compensation study; however, Internal Audit found that the consultant's final report did not include a listing of grade change recommendations. Rather, HROD staff asserted that the recommendations were based on schedules provided by the consultant outside of the final report and considered input from management; however, these schedules did not reconcile to either the final report or the P&SR, nor did documentation of management discussions support all recommendations. Internal Audit recommended that procedures be implemented to ensure that changes to salary grade levels are based on reasonable and consistent methodologies and that documentation is

maintained. Changes should also be communicated to management prior to seeking Board approval. HROD responded that they are in the process of obtaining a compensation and market salary data system, which will be utilized to enhance data collection, consistency, and documentation. HROD agreed to communicate P&SR changes to management prior to seeking Board approval.

The Sole Source List identifies the proposed budget for each software and hardware maintenance agreement; however, these proposed budget amounts exceeded the actual amounts budgeted for most items. In addition, one group's maintenance budget was not based on the estimated value of the agreements but on the prior year budget which was overrun. Finally, emergency malware support, which can be provided by multiple vendors, was included on the Sole Source List. Internal Audit recommended that actual budgeted amounts be reflected on the Sole Source List. For services that can be performed by multiple vendors, Internal Audit recommended that the budget package provide an explanation and justification for using the selected vendors. F&A agreed and will show the actual budgeted amount for software and hardware maintenance when the Sole Source List is presented to the Board for approval. F&A will also develop a budget justification for emergency malware support and include it in the budget package.

The Position Control Policy (Policy) and the annual budget indicate that the Board approves positions at the job family level; however, the Policy also allows positions to be filled outside of the job family, which appears to conflict with the former statement. In addition, the Policy allows positions to be dual-filled by two employees with Chief Executive Officer (CEO) approval; however, Internal Audit found that both instances of dual-filling lacked CEO approval. Further, the requirement to borrow a budgeted vacant position when allowing a dual-fill was eliminated, thereby creating the possibility that the total number of employees could exceed the Board-approved number. Finally, an allowed practice is to over-fill a position by borrowing an under-fill or vacancy of another position, but this practice appears contrary to the policy which states that positions must be filled at or below the budgeted level. Internal Audit recommended that management clarify the Policy with regard to Board-approved positions and develop procedures and controls to ensure compliance with the Policy. HROD responded that the Policy will be revised to clarify the approval process and require Board approval for any additions to Director-level executive headcount. Procedures will be reviewed to ensure the total number of employees does not exceed the Board-approved number. In addition, CEO approval will be obtained for recruitments that will result in a dual-fill.

Summary

Based on the audit, controls over the budget development, monitoring, and reporting processes are generally adequate; however, four recommendations were made to enhance and expand written procedures, to adhere to the Policy, and to improve estimates and explanations included with the Sole Source List.

Attachment

A.   Budget Development, Monitoring, and Reporting, Internal Audit Report No. 16-509

Prepared by: **Approved by:**

Serena Ng   Janet Sutter
Senior Manager   Executive Director, Internal Audit
714-560-5938   714-560-5591