



March 23, 2011

To: Finance and Administration Committee
From: Will Kempton, Chief Executive Officer
Subject: Investments: Compliance, Controls, and Accounting, January 1 through June 30, 2010

The Internal Audit Department has completed a review of investments for the period January 1 through June 30, 2010. Based on the review, it appears that the Orange County Transportation Authority is generally in compliance with its debt, investment, and accounting policies and procedures; however, Internal Audit identified opportunities to improve controls over the wire transfer process and to ensure wire transfers are executed in accordance with policies and procedures.

Recommendation

Direct staff to implement recommendation in the Investments: Compliance, Controls, and Accounting, January 1 through June 30, 2010, Internal Audit Report No. 11-506.

Background

The Treasury/Public Finance Department is responsible for management of the Orange County Transportation Authority's (OCTA) investment portfolio. On June 30, 2010, the investment portfolio's book value was approximately \$851.9 million. The portfolio consists of two managed portfolios: liquid assets for OCTA's daily operations and the short-term portfolio for future budgeted expenditures. External investment managers administer the short-term portfolio, and OCTA's treasurer manages the liquid assets portfolio. OCTA also has funds invested in debt service reserve funds for various outstanding debt obligations. OCTA's Accounting Department is responsible for recording all debt and investment transactions and reconciling all bank and custodial accounts monthly.

Discussion

OCTA's investment activities are reviewed on a periodic basis by Internal Audit. The objective of this review is to determine if OCTA is in compliance with OCTA's debt, investment, and accounting policies and procedures for the review period of January 1 through June 30, 2010.

During testing, Internal Audit identified a wire transfer that had been released from an approved template by a single person. Although Internal Audit confirmed that the payment was legitimate and the template had been secondarily approved, OCTA's Debt and Investment Management Manual requires all wire disbursements be executed by two OCTA personnel. Internal Audit recommended management work with Bank of the West to restrict template options so that all wire transfers require secondary approval. Management concurred and directed Bank of the West to modify template options as recommended.

As a result of this observation, Internal Audit reviewed all system access rights and templates within the wire transfer system. This additional review identified a discrepancy between the rights authorized for system administrators on the Designation of Authorized Administrator's and Approvals Form and actual rights assigned in the wire transfer system. This access includes the ability to assign or delete users in the system, reset passwords, assign authorities to users, and create, modify, or delete wire templates without secondary approval. Internal Audit recommended management work with Bank of the West to ensure dual authority is required for any system administrator changes. Management concurred and has directed Bank of the West to reinstate the dual authority requirement.

Finally, Internal Audit recommended management utilize available system limits on transaction amounts, periodically review active wire templates, and delete any that are no longer used. Management concurred, instituted a maximum transaction limit, and agreed to review templates on a semi-annual basis.

Summary

Based on the review, investments were generally in compliance with OCTA's debt, investment, and accounting policies and procedures; however, Internal Audit offered recommendations to improve controls over the wire transfer process which management indicated would be implemented.

Attachment

- A. Investments: Compliance, Controls, and Accounting, January 1 through
June 30, 2010

Approved by:

A handwritten signature in dark ink, appearing to read "Janet Sutter", with a long horizontal flourish extending to the right.

Janet Sutter
Acting Executive Director, Internal Audit
(714) 560-5591

ORANGE COUNTY TRANSPORTATION AUTHORITY INTERNAL AUDIT DEPARTMENT



Investments: Compliance, Controls, and Accounting January 1 through June 30, 2010

INTERNAL AUDIT REPORT NO. 11-506

March 14, 2011



Internal Audit Team:

Janet Sutter, CIA, Acting Executive Director
Ricco Bonelli, CIA, Senior Internal Auditor

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Conclusion

The Internal Audit Department has completed a review of investments for the period January 1, 2010 through June 30, 2010. Based on the review, it appears that the Orange County Transportation Authority is generally in compliance with its debt, investment, and accounting policies and procedures; however, Internal Audit identified opportunities to improve controls over the wire transfer process and to ensure wire transfers are executed in accordance with policies and procedures.

Background

The Treasury/Public Finance Department is responsible for management of OCTA's investment portfolio. On June 30, 2010, the investment portfolio's book value was approximately \$851.9 million. The portfolio consists of two managed portfolios: liquid assets for OCTA's daily operations, and the short term portfolio for future budgeted expenditures. External investment managers administer the short-term portfolio, and OCTA's Treasurer manages the liquid assets portfolio. OCTA also has funds invested in debt service reserve funds for various outstanding debt obligations. OCTA's Accounting Department is responsible for recording all debt and investment transactions and reconciling all bank and custodial accounts monthly.

Objectives, Scope and Methodology

The primary objective of the review was to determine if OCTA was in compliance with its debt, investment, and accounting policies and procedures.

Additional audit objectives included determining if:

- Internal controls over OCTA's investment activities were adequately designed;
- OCTA was in compliance with California Government Code;
- Investment transactions were adequately supported; and
- OCTA was in compliance with investment requirements of debt issuances.

OCTA's independent auditors, Mayer Hoffman McCann P.C. (MHM), performed agreed-upon procedures with respect to the Treasury Department for the year ended June 30, 2010, and issued their report dated December 28, 2010. Internal Audit limited the scope of this review to procedures not performed by MHM during the course of their agreed-upon procedures.

The methodology consisted of reviewing a judgmental sample of daily cash worksheets prepared by the Accounting Department and the Treasury/Public Finance Department, reviewing a judgmental sample of wire transfers, and reviewing two quarterly debt and

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investment reports provided to OCTA's Board of Directors. The review period was January 1, 2010 through June 30, 2010.

This review was conducted in accordance with Generally Accepted Government Auditing Standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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Audit Comments, Recommendations and Management Responses

Wire Transfer Controls Should Be Strengthened

OCTA's Debt and Investment Management Manual states that "all wire disbursements require two OCTA personnel to complete the process. One is responsible for initiating the transfer and the second person is responsible for releasing the transfer." During testing, Internal Audit identified a wire transfer that had been released from an approved template by a single person.

For all wire transfers, Treasury staff utilizes a wire template (template). Creating a template involves entering recipient bank and payee account information, as well as setting certain control options, such as the number of required approvals when using the template to execute a wire transfer. Once the template is created and approved by a second person it can be used repetitively and the only fields required to be completed are the date and amount. For the wire transfer identified, a template was created and approved; however, the number of required approvals for use of the template was set at zero. On the following day, a wire transfer was initiated from the template and was executed without the required secondary approval.

As a result of this observation, Internal Audit reviewed all system access rights and templates within the WebDirect system, the online cash management application provided by Bank of the West. This additional review identified a discrepancy between the rights authorized for system administrators on the Designation of Authorized Administrator's and Approvals Form (Form) and actual rights assigned in the WebDirect system. The Form on file indicates that OCTA requires approval by a different system administrator (e.g. dual authority) to create, modify, and assign security levels; however, the Bank of the West had assigned each of the two designated system administrators with sole authority to process these changes. This access provides system administrators with the ability to assign or delete users in the system, reset passwords, assign authorities to users, and create, modify, or delete wire templates without secondary approval. According to Bank of the West, the assignment of sole authority to each system administrator was processed based on a request from OCTA; however, a signed Form authorizing this change could not be found.

Finally, Internal Audit noted that, while the system allows for limits to be set on wire transfer amounts by user, this control is not utilized. Also, because wire templates are created for all wires, both one-time transfers and repetitive wires, there are over 50 active templates in the system, many of which are no longer needed.

Recommendation 1: Internal Audit recommends that management enhance controls over the wire transfer process as follows:

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- Work with Bank of the West to ensure dual authority is required for any system administrator changes,
- Work with Bank of the West to restrict system options so that the number of required approvals on a wire template cannot be set at zero,
- Utilize available system limits on maximum amounts for transactions,
- Periodically review and delete any templates that are no longer used.

Management Response (Finance and Administration Division):

Management agrees with the recommendation. Bank of the West has reinstated the dual authority requirement for all system administrator changes. The Bank has also modified their system to eliminate the option of zero approvals for establishing templates. The maximum transaction limit has been lowered to \$20,000,000. The Treasury Department will review templates on a semiannual basis, eliminating templates that are no longer needed.