

Internal Audit Department

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

EXHIBIT A

OCTOBER 2010 AUDITS BY IAD

MONTHLY AUDIT ACTIVITY REPORT

Presented on Board of Supervisors' Agenda
 November 23, 2010

- Audit Finds Auditor-Controller's and Treasurer-Tax Collector's Electronic Funds Transfer (EFT) Process Has Adequate Controls: The Auditor-Controller and Treasurer-Tax Collector process approximately \$22 billion in Electronic Fund Transfers (EFTs) annually.
- Oracle Database for CAPS+ Financial System was Generally Configured to Secure Data: The CAPS+ system records over \$3.4 billion collected and disbursed annually.
- No Countywide Policy/Oversight for Compliance with Payment Card Industry Data Security Standard (PCI DSS) Validation Requirements: County collects \$193 million annually in credit/debit card payments.
- Audit Reveals Revenue Generating Lease Records are Adequate: OCCR/OC Parks - Santiago Equestrian Center - \$16,000 rent paid annually.
- Audit Reveals Revenue Generating Lease Records are Adequate: OCCR/OC Parks - Irvine Park Railroad & Concessions - \$188,000 rent paid annually.
- DA Disability and Healthcare Insurance Fraud Program Passes Audit: We found the financial statement presents fairly, in all material respects, the approved budget, revenues and expenditures for the District Attorney's Office Audit of Disability and Healthcare Insurance Fraud Program.
- Monthly CAAT Reveals Vendors Payments Are Only Paid Once: We found only one (1) duplicate payment for \$300 out of 12,960 vendor invoices paid in September 2010.
- First Follow-Up Audit of Countywide Pension Practices – Our First Follow-Up Audit indicated that one (1) recommendation was closed and two (2) recommendations were partially implemented.

by **Dr. Peter Hughes, MBA, CPA**
 Director of Internal Audit

Assistance in assembling this report provided by:
Eli Littner, Deputy Director, CPA, CIA, CFE, CFS, CISA
Alan Marcum, Senior Audit Manager, MBA, CPA, CIA, CFE
Michael Goodwin, Senior Audit Manager, CPA, CIA
Autumn McKinney, Senior Audit Manager, CPA, CIA, CGFM, CISA

Project No. 1007-4

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



2009 Association of Certified Fraud Examiners' Hubbard Award to Dr. 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

Letter from Dr. Peter Hughes, CPA



Dr. Peter Hughes, CPA
DIRECTOR
PH.D., MBA,
CCEP, CITP, CIA, CFE, CFF

E-Mail:
peter.hughes@iad.ocgov.com

Eli Littner, CPA
DEPUTY DIRECTOR
CIA, CFE, CFS, CISA

Michael J. Goodwin, CPA
SENIOR AUDIT MANAGER
CIA

Alan Marcum, CPA
SENIOR AUDIT MANAGER
MBA, CIA, CFE

Autumn McKinney, CPA
SENIOR AUDIT MANAGER
CIA, CISA, CGFM

Hall of Finance & Records

12 CIVIC CENTER PLAZA,
ROOM 232
SANTA ANA, CA 92701

www.ocgov.com/audit

(714) 834-5475
(714) 834-2880 Fax

RISK BASED AUDITING



OC Fraud Hotline
(714) 834-3608

November 23, 2010

Honorable Board of Supervisors,

It is my pleasure to submit to you the Monthly Audit Activity Report for the month of October 2010. For each audit report we provide an overview and a detailed briefing for your review.

As always, I'm available at your convenience to discuss any aspect of these items.

Respectfully submitted,


Dr. Peter Hughes, CPA

The Internal Audit Department is an independent audit function reporting directly to the Orange County Board of Supervisors.

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Executive Summary

Exhibit

Reports:

- B. Auditor-Controller's and Treasurer-Tax Collector's \$22 Billion Electronic Funds Transfer We found controls are adequate and provide reasonable assurance in all material regards for: (1) establishing, authorizing and processing EFTs completely and accurately in the Auditor-Controller and Treasurer-Tax Collector; (2) segregation of duties in the Quantum and Commercial Electronic Office systems, including user access profiles, system enforced dual authorization, and password settings; (3) access and transmission of EFT payment files transmitted to Wells Fargo Bank; and (4) ensuring EFT processes are efficient and effective.
- C. IT Audit of CAPS+ Financial System Oracle Data Base Configuration We found that the Oracle database was generally configured to secure the CAPS+ financial system data, but there are enhancements that can and should be made to provide better security. The CAPS+ system records over **\$3.4 billion** collected and disbursed annually.
- D. IT Audit of Treasurer-Tax Collector Controls over Compliance with Payment Card Industry Data Security Standard (PCI DSS) We found that the T-TC did not have a Countywide governance policy/procedure and there was no centralized oversight to ensure departments are submitting PCI DSS compliance validation documents to the acquiring banks. This is a **Significant Issue**.
- E. Special Purpose Lease Review for OC Community Resources/OC Parks of Santiago Equestrian Center We found that Santiago Equestrian Center's records adequately supported gross receipts and rent owed was properly paid to OC Parks. Gross receipts reported during the 12-month audit period was about **\$199,000** and rent paid to the County was about **\$16,000**. Over its twenty (20) year term, this lease agreement is estimated to generate about **\$274,000** in rent to OC Parks. This was the first audit of this lease.
- F. Revenue Generating Lease Audit for OC Community Resources/OC Parks of Irvine Park Railroad & Concessions We found that Irvine Park Railroad & Concessions' records adequately supported gross receipts and rent owed was properly paid to OC Parks. Gross receipts reported during the 12-month audit period was about **\$1.25 million** and rent paid to the County was about **\$188,000**. Over its approximate twenty-one (21) year term, this lease agreement is estimated to generate about **\$3.8 million** in rent to OC Parks.
- G. District Attorney's Office Disability and Healthcare Insurance Fraud Program We found the financial statement presents fairly, in all material respects, the approved budget, revenues and expenditures for the District Attorney's Office Audit of Disability and Healthcare Insurance Fraud Program grant, for Fiscal Year Ending June 30, 2010.

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Executive Summary

Exhibit **MONTHLY RESULTS OF CONTINUOUS AUDITING USING CAATS (COMPUTER ASSISTED AUDIT TECHNIQUES):**

H. **Auditor-Controller, Human Resources, and County Procurement Office – Duplicate Vendor Payments and Other Periodic Routines – October 2010:**

We analyzed **12,960** vendor invoices paid in September 2010 amounting to about **\$150 million** and found **99.99%** of the invoices were only paid once.

Of the \$150 million vendor invoices, we identified **one (1)** duplicate payment for **\$300** made to a vendor. To date we have identified **\$951,058** in duplicate vendor payments, of which **\$904,864** has been recovered and is a noteworthy achievement by the County.

Exhibit **Follow-Up Reports:**

I. **First Follow-Up Audit of Countywide Pension Practices – Our First Follow-Up Audit indicated that **one (1) recommendation was closed and two (2) recommendations were partially implemented.****

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

New Audit Findings by Risk Category

	Description	Results
	<p>Material Control Weaknesses A serious audit finding or a combination of Significant Control Weaknesses that can result in financial liability and exposure to a department/agency and to the County as a whole. Management is expected to address "Material Control Weaknesses" brought to their attention immediately.</p>	<p>None issued during October 2010. None issued since July 2010.</p>
	<p>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 generally will require prompt corrective actions.</p>	<p>Two (2) issued during October 2010. Two (2) issued since July 2010.</p>
	<p>Control Findings Audit findings concerning <u>internal controls</u>, <u>compliance issues</u>, or <u>efficiency/effectiveness issues</u> 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.</p>	<p>Forty-one (41) issued during October 2010. Forty-five (45) issued since July 2010.</p>

Total Audit Findings for FY 2010-11: 47

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
B	<p>TITLE: \$22 Billion Electronic Funds Transfer (EFT) Processes</p> <p>DEPT: Auditor-Controller and Treasurer Tax Collector</p> <p>Audit No: 2821</p> <p>Issued: October 14, 2010</p>	<p>Scope: Internal Control Audit of the Auditor-Controller (A-C) and Treasurer-Tax Collector (T-TC) EFT processes, including an evaluation of controls for establishing, authorizing and processing EFTs; user access and application controls; access and transmission controls for EFT payment files, and for efficiency and effectiveness.</p> <p>Conclusion: Internal controls are adequate to provide reasonable assurance over: (1) establishing, authorizing and processing EFTs completely and accurately in the A-C and T-TC; (2) segregation of duties in the Quantum and Commercial Electronic Office (CEO) systems related to user access profiles, system enforced dual authorization, and password settings; and (3) access and transmission of payment files transmitted to Wells Fargo Bank, and (4) that EFT processes are efficient and effective. We identified fifteen (15) Control Findings to improve compliance and enhance existing controls.</p> <p>Background: A-C and T-TC processed \$22 billion in EFTs between March 2008 and March 2009, consisting of wire transfers and Automated Clearing House transactions.</p> <p>Recommendations: A-C Satellite Units verify payment approvals with authorized signature/access request forms; A-C Check Writing ensure <i>EFT/On Demand Wire Forms</i> contain authorized signatures; A-C Claims & Disbursing payment processors review data for accuracy/completeness; A-C evaluate if standardized policies/procedures for approving disbursements can be established; A-C evaluate if department <u>interfaces</u> should have review thresholds and require support documentation; Claims & Disbursing and Satellite Units ensure bank account codes/ABA numbers are correctly documented; T-TC remove “release” access in the CEO system for two manual approvers; T-TC improve Quantum account and password settings; A-C remove user accounts no longer needed to maintain CAPS+ hardware/software; CEO/IT remove administrative accounts for individuals no longer requiring access to the FTP server; CEO/IT limit FTP job accounts log-on capabilities; CEO/IT remove the global/generic FTP rule for network traffic through the external firewall; CEO/IT work with departments/agencies to consolidate external FTP activity; CEO/IT develop a Countywide policy for administration of FTP activity; and A-C Claims & Disbursing continue performing Quality Assurance Reviews and enhance the process to include low dollar payments and interface transactions.</p>

Board Date: November 23, 2010

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For a copy of the complete audit report that contains the audit objective, scope, findings, recommendations, and management’s response, contact the OC Internal Audit Department’s website at <http://www.ocgov.com/audit/>

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
C	<p>TITLE: Public Report - Information Technology Audit of CAPS+ Financial System Oracle Database Configuration</p> <p>DEPT: CAPS Steering Committee</p> <p>AUDIT NO: 2948</p> <p>Issued: October 27, 2010</p>	<p>Scope: We audited the CAPS+ Financial System Oracle Database Configuration as of January 31, 2010 to determine whether the database was adequately configured to secure the CAPS+ financial system data. Because of the sensitivity of the issues and risks of disclosing specific details, we have issued this public report (2948-A) containing general information and a confidential report (2948-B) containing the specific details. The confidential report distribution was limited to the CAPS Steering Committee and selected personnel within CEO/Information Technology and Auditor-Controller.</p> <p>Conclusion: We found that the Oracle database configuration was generally configured to secure the CAPS+ financial system data, but there are enhancements that can and should be made to provide better security. We identified one (1) Significant Issue and nine (9) Control Findings to improve configurations, controls, and processes for the Oracle database.</p> <p>Background: The County of Orange implemented CAPS+ on July 1, 2009, as its enterprise financial system to record general ledger, fixed asset, cost accounting, purchasing, cash receipting, and accounts payable transactions. The CAPS+ financial system uses Oracle 10g as its database management software. Although the CAPS+ financial system contains mainly non-confidential information, it does contain some sensitive or protected information. CAPS+ records over \$3.4 billion collected and disbursed annually.</p> <p>Recommendations: CAPS Steering Committee ensure an auditing/logging strategy is developed and implemented for the CAPS+ Oracle database; establish personal accounts for the database administrators; modify account profile password setting to best practice, utilize an Oracle password security function; modify account resource profile settings to best practice, modify two Listener configuration settings to best practice; remove unnecessary "Read" access to the Oracle database; improve procedure for changing user account passwords; and ensure additional Oracle security features are researched and those features that do not conflict with the CAPS+ financial system and are cost effective to adequately address risks are implemented.</p>

Board Date: November 23, 2010

Exhibit A, Page 7 of 14

For a copy of the complete audit report that contains the audit objective, scope, findings, recommendations, and management's response, contact the OC Internal Audit Department's website at <http://www.ocgov.com/audit/>

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
D	<p>TITLE: Information Technology Audit of Controls over Compliance with Payment Card Industry Data Security Standard</p> <p>DEPT: Treasurer Tax Collector</p> <p>AUDIT NO: 2946</p> <p>Issued: October 21, 2010</p>	<p>Scope: We audited the T-TC's governance policies/procedures (controls) to ensure Countywide compliance with Payment Card Industry Data Security Standard (PCI DSS) validation requirements. We also selected a sample of five (5) departments to determine whether: PCI DSS validation documentation was submitted to the acquiring banks; third party payment card processors and equipment complied with PCI DSS; and third party agreements addressed PCI DSS compliance. The County collects about \$193 million annually in credit/debit cards.</p> <p>Conclusion: We found T-TC did not have a Countywide governance policy/procedure and there was no centralized oversight to ensure departments are submitting PCI DSS validation documentation to the acquiring banks. We identified one (1) Significant Issue that has been subsequently corrected and eleven (11) Control Findings to enhance existing controls, processes, and systems for payment card processing.</p> <p>Background: PCI DSS is a collaborative effort among several payment card brands (American Express, Discover, JCB, MasterCard, and Visa) to achieve a common set of security standards for use by entities that process, store, or transport payment card data. Compliance is mandated by the individual payment card brands and is enforced by the merchant card processors (acquiring banks). For the 12-month period ended December 31, 2009, County department's processed over 840,000 payment card transactions totaling about \$193 million (excluding the Clerk-Recorder).</p> <p>Type of Recommendations: T-TC develop Countywide policies for oversight and compliance with PCI DSS validation requirements, establishment of bank accounts, and establishment of merchant accounts; A-C update Accounting Manual for payment cards; T-TC update checklist for Setting up New Merchant Accounts to address PCI DSS; T-TC annually monitor/verify that each County department submits PCI DSS Self Assessment Questionnaire to the acquiring banks; T-TC determine whether quarterly network security scans are required; T-TC update its payment card terminals to comply with PCI DSS; County Procurement Office develop standard terms/conditions for PCI DSS/PA DSS in contracts for third party payment processors or purchase of payment card equipment/systems; OCPW/Corporate Real Estate develop standard terms/conditions to address PCI DSS in operating agreements; and T-TC, OCPW, and OCCR modify their web sites to state customers are being directed to a third party for payment processing.</p>

Board Date: November 23, 2010

Exhibit A, Page 8 of 14

For a copy of the complete audit report that contains the audit objective, scope, findings, recommendations, and management's response, contact the OC Internal Audit Department's website at <http://www.ocgov.com/audit/>

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
E	<p>TITLE: Special Purpose Lease Review of Santiago Equestrian Center</p> <p>DEPT: OC Community Resources/ OC Parks</p> <p>AUDIT NO: 2934</p> <p>Issued: October 5, 2010</p>	<p>Scope: Special Purpose Lease Review to determine whether Santiago Equestrian Center's records adequately supported monthly rent paid to the County. During the 12-month audit period, Santiago Equestrian Center reported approximately \$199,000 in total gross receipts and paid the County approximately \$16,000 in rent. This was the first audit of the lease. While this lease generates a relatively small amount of gross receipts, the goal of our review was to help ensure the lessee's records are on the "right track" and to make any necessary corrections timely in the lease term.</p> <p>Conclusion: We found that Santiago Equestrian Center's records adequately supported monthly rent paid to the County and rent owed was properly paid. We identified three (3) Control Findings related to improving recordkeeping and the accounting methodology used to report gross receipts.</p> <p>Background: The County of Orange entered into a lease agreement with Southern Sierra Land & Cattle Company dba Santiago Equestrian Center, dated December 8, 2009, for the operation of an equestrian center located within Limestone Canyon & Whiting Ranch Wilderness Park. Over the twenty (20) year term, this lease agreement is estimated to generate about \$274,000 in rent to the County.</p> <p>Recommendations: Improving records or accounting methodology including: pre-numbered horse boarding and trailer storage agreements, updating accounts receivable records for changes that impact billing amounts, and reporting gross receipts on the accrual basis.</p>

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
F	<p>TITLE: Revenue Generating Lease Audit of Irvine Park Railroad & Concessions</p> <p>DEPT: OC Community Resources/ OC Parks</p> <p>AUDIT NO: 2935</p> <p>Issued: October 5, 2010</p>	<p>Scope: Revenue Generating Lease Audit to determine whether Irvine Park Railroad & Concessions' records adequately supported monthly rent paid to the County. During the 12-month audit period, Irvine Park Railroad & Concessions reported approximately \$1.25 million in total gross receipts and paid the County approximately \$188,000 in rent.</p> <p>Conclusion: We found that Irvine Park Railroad & Concessions' records adequately supported monthly rent paid to the County and rent owed was properly paid. We identified three (3) Control Findings related to improving recordkeeping and changing the methodology for reporting gross receipts.</p> <p>Background: The County of Orange entered into a lease agreement with Irvine Park Railroad and Concessions, dated October 28, 2008, for the operation of a train ride concession and other park concessions (bike and boat rentals, food and merchandise sales) at Irvine Regional Park. Over its approximate twenty-one (21) year term, this lease agreement is estimated to generate about \$3.8 million rent to the County.</p> <p>Recommendations: Improving records or accounting methodology including: maintaining monthly schedule of rentals and payments for party pavilion and moonbounce rentals, retaining supporting documentation for void transactions, and reporting gross receipts on cash recorded rather than cash collected.</p>

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
G	<p>TITLE: Financial Statement Audit of Disability and Healthcare Insurance Fraud Program</p> <p>DEPT: OC District Attorney's Office</p> <p>AUDIT NO: 1010</p> <p>Issued: October 26, 2010</p>	<p>Scope: We audited the District Attorney (DA) Office's financial statement for the Disability and Health Care Insurance Fraud Program grant to determine that budgeted amounts, revenues and expenditures were fairly stated, i.e., the amounts are recorded accurately, completely, and timely. Also, in planning and performing our audit we reviewed internal controls over financial reporting and performed tests of the DA Office's compliance with certain laws, regulations and grant requirements.</p> <p>Conclusion: In our opinion, the financial statement presents fairly, in all material respects, the approved budget, revenues and expenditures. In addition, we did not identify any significant deficiencies or material weaknesses in the District Attorney's internal control over financial reporting.</p> <p>Background: The grant is funded by the California Department of Insurance, and the 2009/2010 fiscal year grant award totaled \$586,500. Current year's expenditures exceeded total Grant revenue by \$26,547. The excess of expenditures over revenues as of June 30, 2009 cannot be applied toward future years' grant revenue. Therefore, the excess expenditures will be absorbed by the District Attorney. The grant agreement requires that the DA obtain an annual audit of the financial statement. The DA has the option of outsourcing the audit to an outside CPA firm or requesting that the County Internal Audit Department conduct the audit.</p> <p>Type of Recommendations: None</p>

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
H	<p>DEPT: Auditor-Controller Human Resources County Procurement Office</p> <p>TITLE: Monthly Results of Continuous Auditing Using CAATS (Computer Assisted Audit Techniques) – October 2010</p> <p>AUDIT NO: 1041-D</p> <p>ISSUED: October 29, 2010</p>	<p>Scope: The monthly CAAT routines are automated queries applied to large amounts of electronic data searching for specified characteristics. We currently perform four (4) on-going CAAT routines utilizing selected payroll and vendor data. Depending on the nature of the CAAT, we perform them monthly, annually, or as necessary</p> <p>Conclusion:</p> <ul style="list-style-type: none"> • <u>Duplicate Payments to Vendors</u>: We analyzed 12,960 vendor invoices paid in September 2010 amounting to about \$150 million and found 99.99% of the invoices were only paid once. Of the \$150 million vendor invoices, we identified one (1) duplicate payment for \$300 made to a vendor. The County currently has a recovery rate from vendors of about 95% on these duplicate payments. Our prior research has indicated that duplicate payments are typically caused by a human clerical error. Based on the to-date recoveries of \$904,864, this CAAT routine has paid for itself and is returning monies to the County that may otherwise be lost. • <u>Employee Vendor Match</u>: We performed an analysis of 49,935 employee and 12,809 vendor addresses and phone numbers at 9/30/10. We identified (one) 1 potential employee/vendor match that was determined not to be a conflict. • <u>Retiree/Extra Help Hours</u>: As of September 20, 2010, no individuals have exceeded the annual limits for FY 10-11. • <u>Multiple Payroll Direct Deposits</u>: No findings noted.

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
	<p>CONTINUED,</p> <p>DEPT: Auditor-Controller Human Resources County Procurement Office</p> <p>TITLE: Monthly Results of Continuous Auditing Using CAATS (Computer Assisted Audit Techniques) – October 2010</p>	<p>Background: The CAATs differ from our traditional audits in that the CAATs can query 100% of a data universe whereas the traditional audits typically test but a sample of transactions from the population. The resulting matches identified by the CAATs are subjected to further review and analysis by the Internal Audit Department. We then forward any resulting findings to the Auditor-Controller, Human Resources, or County Procurement Office for their review and concurrence, and subsequent correction/recovery. We also work with these departments to identify internal control enhancements with the purpose of preventing future occurrences of the type of findings identified by the CAATs.</p>

MONTHLY INTERNAL AUDIT ACTIVITY STATUS REPORT

Detailed Report

Exhibit	Description	Comments
I	<p>TITLE: First Follow-Up Audit of Countywide Pension Practices</p> <p>DEPT: Human Resources Department</p> <p>AUDIT NO: 1016-D</p> <p>Issued: October 18, 2010</p>	<p>Scope: We have completed a First Follow-Up Audit of Countywide Pension Practices. Our audit was limited to reviewing, as of September 27, 2010, actions taken to implement the three (3) recommendations from our original audit report.</p> <p>Conclusion: Our First Follow-Up Audit indicated that one (1) recommendation was closed and two (2) recommendations were partially implemented.</p> <p>Background: We performed an audit of certain Human Resources records and related documents for the period from July 1, 2006 through June 30, 2009 in response to the recommendation made to the Internal Audit Department in the Orange County Grand Jury report entitled "The Guardian of Last Resort" on the Public Administrator/Public Guardian, dated May 9, 2009. We determined if additional instances of questionable pension practices exist in agencies other than the Public Administrator/Public Guardian's Office. In addition, we identified internal control weaknesses for which we provided recommendations for improvement.</p> <p>Type of Recommendations: We recommended that the Human Resources Department require pre-authorization of permanent and temporary promotions from the County Executive Officer for proposed and/or cumulative salary increases exceeding 15% prior to submission to the Board of Supervisors for their review and approval. We found that certain salary increases did not receive prior approval in accordance with policies and procedures. We also recommended that the Human Resources Department take appropriate actions to ensure monitoring of management salary increases are documented, reviewed and maintained on file for third party confirmation. We found that documentation for certain salary actions by the granting department and monitoring actions by HRD was not complete.</p>