

**Date:** April 17, 2012

File No. 1166

**To:** Miles Burnett, Chief  
Office of Fiscal Services  
707 3<sup>rd</sup> Street, 9<sup>th</sup> Floor  
West Sacramento, CA 95605**From:** Department of General Services  
Office of Audit Services**Subject: REVIEW OF THE SYSTEMS OF INTERNAL CONTROL FOR  
FINANCIAL REPORTING**

This report presents the results of our review of the systems of internal control of the Department of General Services (DGS) for financial reporting. These systems are primarily administered by the Office of Fiscal Services (OFS). This review was conducted as part of the Office of Audit Services' biennial review of the DGS' systems of internal control. Our review was conducted in accordance with the International Standards for the Professional Practice of Internal Auditing.

The objective of our review was to determine the adequacy and effectiveness of the systems of internal control for the financial reporting transaction cycle. A transaction cycle is defined as the route by which a type of transaction flows from inception to final reporting.

The scope of our review involved a study and evaluation of the systems of internal control used in preparing the department's financial reports for the fiscal year ending June 30, 2010. Upon the completion of a preliminary survey of reporting operations, we selected 7 of the 28 funds administered by the OFS as the primary focus of our review of the financial reporting cycle. The following seven funds were selected for in-depth review: (1) Disability Access Account (0006); (2) State Emergency Telephone Number Account (0022); (3) State Motor Vehicle Insurance Account (0026); (4) Public School Planning, Design, and Construction Review Revolving Fund (0328); (5) Service Revolving Fund (0666); (6) Architecture Revolving Fund (0602); and, (7) Earthquake Safety & Public Buildings Bond (0768). The Service Revolving Fund was selected because it is the primary source of funding for the department's operations, while the other funds were selected due to the significance of their accounts payable activities reported at year-end.

Our review of financial reporting primarily involved determining whether sufficient policies and procedures have been implemented to provide reasonable assurance that: (1) assets are safeguarded against loss from unauthorized use or disposition; (2) transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of reliable financial statements; and, (3) financial operations are conducted in accordance with policies and procedures established in the State Administrative Manual (SAM). Reasonable assurance is provided when cost-effective actions are taken to restrict deviations to a tolerable level. These actions should result in material errors and improper or illegal acts being prevented or detected and corrected within a timely period by employees in the normal course of performing assigned duties.

Based on the results of our fieldwork conducted over the period September 29, 2010 through May 26, 2011, we concluded that the OFS has established adequate and effective systems of internal control over financial reporting. The OFS' systems of internal control provide reasonable assurance that assets are safeguarded, transactions are properly executed and recorded, and financial operations are conducted in compliance with SAM requirements.

To determine the adequacy and effectiveness of the systems of internal control for financial reporting, we reviewed policies and procedures, interviewed parties involved, observed operations, tested reporting procedures, records and transactions for the fiscal year ending June 30, 2010 and performed other tests as deemed necessary. An audit guide issued by the Department of Finance was used to assist us in our evaluation of the systems of internal control. The audit guide identified the following three control objectives that were evaluated during our review: (1) the compilation of financial statements and reports is adequately supervised; (2) financial statements are promptly and accurately prepared; and, (3) year-end accounts payable represent authorized current obligations, and encumbrance balances are valid and adequately disclosed.

Management should be aware that controls cannot prevent all problems because they would not be cost-effective. Moreover, the effectiveness of controls change over time. Limitations which may hinder the effectiveness of an otherwise adequate system of controls include resource constraints, faulty judgments, unintentional errors, circumvention by collusion, and management overrides. The presence of these limitations may not always be detected by an audit.

We greatly appreciated the cooperation and assistance provided by the OFS' personnel.

If you need further information or assistance on this report, please contact me at (916) 376-5058, or Andy Won, Audit Supervisor, at (916) 376-5052.



RICK GILLAM, CPA, CIA  
Chief, Office of Audit Services

Staff: Andy Won, Audit Supervisor  
Victoria LaTour  
Tam Nuynh

cc: Blanche Harbridge-Wright, Deputy Director, Administration Division  
Fee Chang, Accounting Officer, OFS