

Sonoma County

Auditor-Controller-Treasurer-Tax Collector

Internal Audit Report

**Internal Audit:
Sonoma County Economic Development Board
and Sonoma County Economic Development Board
Foundation**

For the Period
July 1, 2017 through June 30, 2019

Engagement No: 3156
Report Date: June 28, 2021



Erick Roeser

Auditor-Controller-Treasurer-Tax Collector

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Executive Summary

As a part of the 2020/2021 Annual Audit Plan, the Internal Audit Division of the Sonoma County Auditor-Controller-Treasurer-Tax Collector's Office (ACTTC) conducted an audit of the Sonoma County Economic Development Board (EDB) and Sonoma County Economic Development Board Foundation (Foundation) for the period July 1, 2017 to June 30, 2019 and determined that:

- Financial information contained in the Foundation's annual reports for the fiscal years ended June 30, 2018 and 2019 submitted to the Sonoma County Board of Supervisors are adequately supported by the underlying accounting records and supporting documentation with some exceptions. Foundation management identified the following errors in the 2018 and 2019 financial reports submitted to the Board. These reports will be corrected and resubmitted to the Board in fiscal year 2021-22.
 - Cash and cash equivalents and short-term investments for the fiscal year 2017-18 were overstated by \$63,657. The change in net assets (net income) and net asset balances were unaffected by this error (see recommendation on page 7).
 - The Foundation did not reimburse EDB in a timely manner for certain staffing and consulting expenses which resulted in an understatement of expenses by \$35,000 and \$46,780 and an understatement of accounts payable by \$35,000 and \$81,780 in the fiscal years 2017-18 and 2018-19, respectively. These errors did affect the change in net assets (net income) and net asset balances (see pages 9 and 10). Subsequently, the Foundation reimbursed the EDB for the above discussed expenses and provided the Auditors corrected annual reports for the Foundation.
- Adequate internal controls were not in place to ensure that the Foundation timely reimbursed EDB for payroll and consulting related expenditures. The EDB's internal controls over other billings and expenditures of funds received from the Foundation operated effectively during the period covered by our audit.

Management made appropriate changes in its procedures to address the above risks as discussed on page 7.

Introduction and Background

Introduction

The ACTTC has completed an audit of the EDB and the Foundation for the period July 1, 2017 through June 30, 2019. The audit was conducted in accordance with the *International Standards for the Professional Practice of Internal Auditing (Standards)*. These Standards require that we identify, analyze, evaluate, and document sufficient information and evidence to achieve our audit objectives. We believe that the evidence obtained provides a reasonable basis for the results, observations, and recommendations contained in our report.

The purpose of this audit report is to furnish management with independent and objective analyses, recommendations, and other information concerning the activities reviewed. The audit report is a tool to help management identify and implement improvements.

Background

In 1957 the County of Sonoma, acting through its Board of Supervisors, created the EDB pursuant to the California Government Code Section 26104. The purpose of the EDB is to enhance the local business environment for the benefit of all residents of the County of Sonoma through the creation and development of economic research, analysis, and programs that promote local businesses. The EDB is governed by a ten member Board, made up of two members appointed by each member of the Sonoma County Board of Supervisors.

The EDB presents several seminars and events throughout the year that address key opportunities, initiatives, and challenges facing Sonoma County. In addition, the EDB develops factual data regarding significant economic activities, trends, and projections for Sonoma County. These events and online reports are financially supported by business and community sponsors through the Foundation.

On January 23, 2001, the Sonoma County Board of Supervisors approved the establishment of the Foundation. In March 2001, the Foundation was incorporated as a California nonprofit public benefit corporation. The primary purpose of the Foundation is to assist in finding funding sources for EDB projects in need of financial support, that are approved by the County Board of Supervisors. For the fiscal years 2017-18 and 2018-19, the Foundation raised \$845,553 and \$500,719 in funds, respectively, for the County Board of Supervisors approved EDB projects. The Foundation spent \$611,045 and \$563,644 in the fiscal years 2017-18 and 2018-19, respectively, on approved projects.

Introduction and Background

The Foundation began its first year of operations in the fiscal year 2002-03. In August 2002, it signed an Operational Memorandum of Understanding with the Sonoma County Board of Supervisors to formally define the relationship between the EDB, an agency of the County of Sonoma, and the Foundation. The Foundation produced its annual reports for the Board's review, for the fiscal years ending June 30, 2018 and June 30, 2019. These reports are required by Article 8.1(f) of the bylaws of the Foundation and the Memorandum of Understanding between the Foundation and the County of Sonoma (MOU). In accordance with the MOU, the ACTTC has performed financial audits every two years and reported the results to the County Board of Supervisors.

Objectives and Scope

Objectives

The objectives of this audit were to determine whether:

1. The financial information contained in the Foundation's annual report submitted to the Sonoma County Board of Supervisors, is adequately supported by the underlying accounting records and supporting documentation.
2. The EDB's internal controls over billing and expenditures of funds received from the Foundation, including payroll and contract payments operated effectively during the period covered by the audit.

Scope

The audit covered the period July 1, 2017 through June 30, 2019. The scope of our work included but was not limited to the following:

- A preliminary survey to update our knowledge of the operating environment; identify changes in laws and regulations, systems, personnel and organization structure.
- A risk analysis to identify significant risks of non-compliance with policies, procedures or laws, loss or misuse of assets and inefficiencies in processes.
- A review and evaluation of internal controls designed to ensure compliance with the above requirements and to adequately reduce the risk identified.

The audit included inquiry, observation, and tests to assess the adequacy of documentation supporting compliance with relevant sections of the Foundation's bylaws, and the MOU between the County and the Foundation.

Procedures

To achieve our audit objectives for the EDB and the Foundation, we performed the procedures outlined below:

1. Accounted for all depositories used by the Foundation during the audit period and reviewed bank reconciliations performed for those that had significant balances.
2. Agreed investment balances per Foundation's books as of June 30, 2018 and June 30, 2019 with those on the statements from banks and/or other investment custodians.
3. Determined if selected prepaid expenses were recorded in the proper period and correctly amortized.
4. Reviewed selected accounts receivable transactions and determined if they were recorded in the proper period.
5. Compared current year revenue and expenditures with that of the prior year and obtained explanations for any unusual or material variances.
6. Obtained a listing of revenue transactions from the Foundation's records, selected a sample and examined supporting documentation to substantiate that they were recorded in the correct period for the correct amount.
7. Reviewed selected revenue transactions, including grant revenue that may have been misclassified.
8. Obtained a listing of expenditure transactions from the Foundation's records, selected a sample and examined supporting documents to determine if they were recorded in the correct period for the correct amount.
9. Gained an understanding of the system of internal controls over EDB's contract monitoring, billing and expenditure of funds received from the Foundation. Performed tests of compliance over key control procedures.
10. Reviewed a sample of EDB's outstanding contracts and determined if they were properly authorized and payments were correctly coded.

Results and Recommendations

Objective #1: Financial information contained in the Foundation's annual report submitted to the Sonoma County Board of Supervisors, was adequately supported by the underlying accounting records and supporting documentation with some exceptions.

The errors in the financial reports submitted to the County Board of Supervisors (Board) discussed below were discovered as a result of reviews performed by Foundation management. The necessary corrections were made before providing these to the auditors. Management plans to provide the Board those corrected reports at a later date.

The following is a discussion of the errors that were noted and the Foundation management's planned corrective actions.

1. Overstatement of Cash and Short-Term Investments:

For the fiscal year ended June 30, 2018 the cash and cash equivalents and short-term investments on the Foundation's annual report were overstated by \$63,657 and not discovered prior to presentation to the Board. A secondary detailed review was not required, which we consider to be a significant control weakness. The related transactions in the Foundation's general ledger were however accurate.

Management will submit the corrected financial reports to the Board in fiscal year 2021-22.

Recommendation:

A secondary detailed review of the financial reports should be performed by Foundation management before submitting them to the Board. The reviewer should compare the numbers in the system reports to the Foundation's annual report. All reconciling items should be vouched and the mathematical accuracy of the financial reports should be tested.

Management Response:

Management concurs with the recommendation and will conduct a detailed secondary review process of the Foundation's annual report before it is submitted to the Foundation Economic Development Board and Sonoma County Board of Supervisors.

2. Understatement of Expenses and Accounts Payable

The processing of certain EDB staffing and consulting expenses required to be reimbursed by the Foundation per the terms of the agreement between the two entities was overlooked for fiscal years ending June 30, 2018 and 2019. As a result, the expenses and payables were understated in the Foundation's annual reports for both fiscal years as presented to the Board. Expenses were understated by \$35,000 and \$46,780 and payables were understated by \$35,000 and \$81,780, respectively.

The Foundation reimbursed EDB for staffing and consulting expenses in fiscal year 2020-21. Management will submit the Foundation's corrected annual report to the Board in fiscal year 2021-22.

Management implemented the following quality control procedures to ensure reimbursable expenses are identified and processed timely by the Foundation:

- Created transaction codes in the financial system to identify reimbursable transactions.
- Implemented procedures requiring running and reviewing monthly reports of reimbursable transactions to ensure all reimbursable transactions are processed.
- Implemented procedures requiring the accounting staff to review grant reports for the purpose of identifying the type and dollar value of costs that will be reimbursable.

Objective #2: The EDB's internal controls over the billing of payroll expenditures and consulting costs received from the Foundation did not operate effectively over the audit period. The EDB's internal controls over other billings and expenditures of funds received from the Foundation operated effectively during the period.

As discussed above, processing of certain reimbursements due from the Foundation to EDB were overlooked and not discovered in a timely manner. The Foundation has since reimbursed EDB for staffing and consulting expenses owed in fiscal 2020-21. Management enhanced internal control procedures to reduce the risk of such errors as discussed in Objective #1.

Staff Acknowledgement

Staff Acknowledgement:

We would like to thank Rebekah Heinze, of the EDB for her helpfulness and cooperation in conducting this audit. If you have any further questions regarding this report, please contact Olga Gray at (707) 565-8303.

Appendix A

**Sonoma County Economic Development Board Foundation
Comparative Statement of Financial Position
June 30, 2019 and 2018**

	<u>2019</u>	<u>2018</u>
Assets		
Current assets:		
Cash and equivalents	\$ 814,580	\$ 848,195
Short term investments	26,144	47,425
Accounts receivable	2,803	14,340
Prepaid expenses	<u>-</u>	<u>7,308</u>
Total assets	\$ <u>843,527</u>	\$ <u>917,268</u>
 Liabilities and Net Assets		
Current liabilities:		
Accounts payable	\$ 86,678	\$ 35,044
Deferred Grants Awarded	5,000	14,250
Deferred sponsorships	<u>7,500</u>	<u>60,700</u>
Total liabilities	<u>99,178</u>	<u>109,994</u>
 Net Assets:		
Unrestricted	9,725	9,725
Designated	438,097	436,102
Temporarily restricted	<u>296,527</u>	<u>361,447</u>
Total net assets	<u>744,349</u>	<u>807,274</u>
Total liabilities and net assets	\$ <u>843,527</u>	\$ <u>917,268</u>

See Notes 1 and 2 on page 12 of the Internal Audit Report

Appendix B

**Sonoma County Economic Development Board Foundation
Statement of Activities
For The Fiscal Year Ended June 30, 2019**

	Unrestricted	Temporarily Restricted	Total
Revenues, gains and other support			
Registration /participation fees	\$ 114,580	\$ -	\$ 114,580
Donations/sponsorships	106,529	18,646	125,175
Grants	1,000	256,625	257,625
Investment income	3,339	-	3,339
Net assets released from restrictions	2,728	(2,728)	-
	<u>228,176</u>	<u>272,543</u>	<u>500,719</u>
Total revenues			
	<u>228,176</u>	<u>272,543</u>	<u>500,719</u>
Expenses			
Program services			
Community outreach	93,954	337,464	431,418
Economic outlook	55,351	-	55,351
Research initiatives	59,526	-	59,526
Supporting services			
Administrative services	17,349	-	17,349
	<u>226,180</u>	<u>337,464</u>	<u>563,644</u>
Total expenses			
	<u>226,180</u>	<u>337,464</u>	<u>563,644</u>
Change in net assets	1,996	(64,921)	(62,925)
Net assets, beginning of year	445,827	361,447	807,274
Net assets, end of year	<u>\$ 447,823</u>	<u>\$ 296,526</u>	<u>\$ 744,349</u>

See Notes 1 and 2 on page 12 of the Internal Audit Report

Appendix C

**Sonoma County Economic Development Board Foundation
Statement of Activities
For The Fiscal Year Ended June 30, 2018**

	Unrestricted	Temporarily Restricted	Total
Revenues, gains and other support			
Registration /participation fees	\$ 121,352	\$ -	\$ 121,352
Donations/sponsorships	115,416	217,623	333,039
Grants	-	375,410	375,410
Miscellaneous Revenue	14,388	-	14,388
Investment income	1,364	-	1,364
Net Assets Released from Restrictions	20,170	(20,170)	-
	<u>272,690</u>	<u>572,863</u>	<u>845,553</u>
Expenses			
Program services:			
Community outreach	68,139	403,568	471,707
Economic outlook	59,057	-	59,057
Research initiatives	55,634	-	55,634
Supporting services:			
Administrative services	24,647	-	24,647
	<u>207,477</u>	<u>403,568</u>	<u>611,045</u>
Change in net assets	65,213	169,295	234,508
Net assets, beginning of year	380,614	192,152	572,766
Net assets, end of year	<u>\$ 445,827</u>	<u>\$ 361,447</u>	<u>\$ 807,274</u>

See Notes 1 and 2 on page 12 of the Internal Audit Report.

Notes

Note 1: Sonoma County Economic Development Board Foundation Comparative Statement of Financial Position and Statement of Activities presentation:

These Statement of Financial Position and Statement of Activities were prepared for the purpose of presenting revenues and expenditures of the Foundation pursuant to the Article 8.1(f) of the First Amended and Restated Bylaws of the Sonoma County Economic Development Board Foundation, MOU and Foundation Policies and Procedures Manual and is not intended to be a presentation in conformity with generally accepted accounting principles. The note disclosures required by Governmental Accounting Standards are not presented, since such disclosures are not required by the Article 8.1(f) of the First Amended and Restated Bylaws of the Sonoma County Economic Development Board Foundation and MOU.

Note 2: Cash Equivalents and Short-term Investments:

Investments with an original maturity of three months or less, as of the date of purchase, are considered cash equivalents, and consist of certificates of deposit and highly liquid money market instruments.

Investments with original maturities between three months and one year are considered short term investments, and consist of certificates of deposit.

Appendix D-Report Item Risk Classification

For purposes of reporting our audit findings and recommendations, we classify audit report items into three distinct categories to identify the perceived risk exposure:

- **Risk Classification A: Critical Control Weakness:**
Serious audit findings or a combination of Significant Control Weaknesses that represent critical exceptions to the audit objective(s), policies, and/or business goals of a department/agency or the County as a whole. Management is expected to address Critical Control Weaknesses brought to their attention immediately.
- **Risk Classification B: Significant Control Weakness:**
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.
- **Risk Classification C: Control Findings:**
Audit findings concerning internal controls, compliance issues, or efficiency/effectiveness issues 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.

The current status of implementation of recommendations will be followed up no later than the end of the second fiscal year after the report has been issued. Critical control weakness findings will be followed up between six months and one year of the date of the report.