MWD
METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

Report
August 31, 2007
Office of the General Auditor

- **Internal Audit Report for August 2007**

Summary

Four reports were issued during the month:

- **Courion Identity Management System Audit Report – Generally Satisfactory**
- **Property and Plan Audit Report – Generally Satisfactory**
- **Employee and Director Expense Audit Report – Generally Satisfactory**
- **Brutoco Contract No. 1614 Audit Report – Generally Satisfactory**

Discussion Section

This report highlights the significant activities of the Internal Audit Department during August 2007. In addition to presenting background information and the opinions expressed in the audit reports, a discussion of findings noted during the examination are also provided.

Courion Identity Management System Audit Report

Background

The Courion system was deployed in late 2005 to provide for an automated password resetting routine that would alleviate the need for employees to call the Information Technology Section Help Desk for assistance in resetting passwords. Two modules were implemented: Password Courier and Profile Courier. The Password Courier module provides password-resetting features for five MWD applications: Peoplesoft, Oracle Financial, Travel Expense Reporting System, WorkTech, and Windows Network. Utilizing Password Courier, employees reset their password after authenticating their identity by answering three self-defined, pre-answered questions. Password Courier compares the employee’s answers to the authenticating responses saved in Profile Courier. Once the user’s identity is authenticated, the password is reset and Courion applies this new password to the appropriate applications (of the five listed above) to ensure that the user can gain access to these systems. During 2006, 4,460 password resets were successfully performed using Courion, which has aided in reducing the workload of the Help Desk related to manually resetting passwords.

Opinion

In our opinion, the operating and administrative procedures over Courion include those practices usually necessary to provide for a generally satisfactory internal control structure. The degree of compliance with such policies and procedures provided effective control for the period ended June 30, 2007.

Comments and Recommendations

ADMINISTRATOR ACCOUNT PASSWORD CHANGES

Compliance with the End-user Computing Standards (Standards) is necessary to ensure a uniform and consistent access control environment. These standards establish security practices that require that all passwords expire at least every sixty days.

During our review, we noted that the Courion system does not force periodic password changes for Administrator accounts. Further review revealed that the Administrator account passwords have not been changed since Courion was implemented in late 2005. It is important to note that the Courion Administrator accounts can be used to change security settings for users to include: failure logon attempts reset, password strength, password history, and logging configurations in the Courion software.

We recommend that the Information Security Team develop procedures to enforce the sixty-day password change policy for the administrator accounts.

WORKSTATION ENCRYPTION

Effective encryption over web-based applications is important to ensure data privacy and confidentiality. As stated in the Standards, critical user access control information including account passwords and user authentication data should be encrypted, when it is transmitted over the network. Courion, a web based application, utilizes Metropolitan's IntraMet to transmit access control information to users for password resetting functions.

During our review of the Password Courier and Profile Courier modules, we noted that critical user access control data is transmitted in a non-encrypted form. Furthermore, although Courion resides within the Metropolitan firewall, potential for internal security breaches is as important to control as external threats over the Internet.

We recommend that Information Security Team consider implementing encryption to the Courion user interface screens.

WINDOWS SERVERS SECURITY

We performed a vulnerability scan on the Windows server (usmwd147) that hosts both Password Courier and Profile Courier. The Microsoft Baseline Security Analyzer (MBSA) was used to evaluate security vulnerabilities on the server security.

We noted that the Server Administrator account has a non-expiring password and that the use of Internet Explorer is not restricted for non-administrator on this server. According to Microsoft, browsing Internet Web sites from a server should be restricted to reduce the possibility of an attack on the server by a malicious Web site.

We recommend that the Information Security Team remediate these vulnerabilities.

Property and Plant Audit Report

Background

Property and Plant is a major component of the Property, Plant, and Equipment account on Metropolitan's balance sheet. Property and Plant assets under review (land, completed features and construction-in-progress) represent 68% of Metropolitan's total assets. The land account includes acquisition of land, easements, and right-of-way. The completed features account includes storage facilities (i.e., dams and reservoirs), distribution facilities, pumping and treatment plants, and power plants and lines. Finally, the construction-in-progress account includes contract and non-contract costs incurred to bring the asset to its intended use. The contract costs include all payments to contractors and consultants whereas non-contract costs include Metropolitan labor hours, additives, interest incurred on bond instruments, and administrative overhead costs.

Metropolitan procedures specify that new facilities, betterment, replacement, or any item permanently affixed to one location that has total cost of at least $25,000, and a useful life of at least five years should be capitalized and depreciated over its' useful life. The useful life for these assets range from five years for nominal assets, fifty years for treatment plants and power facilities, and eighty years for storage and distribution facilities. Property and Plant net additions (assets placed into service less those sold, retired or disposed) were $831 million during the audit period of July 2005 to April 2007. As of April 30, 2007, Property and Plant assets totaled $7 billion, net of $1 billion accumulated depreciation.

Opinion

In our opinion, the accounting and administrative controls over Property and Plant assets include those practices usually necessary to provide for a generally satisfactory internal control structure. The degree of compliance with such procedures provided effective control for the period from July 2005 to April 2007.

Comments and Recommendations

LAND ACCOUNT RECONCILIATIONS

Our review of the January 2007 Land Account reconciliation revealed a discrepancy of $5 million between the Oracle Assets Tracking System (OATS) and the Oracle General Ledger. OATS is used by the Accounting Operations Unit to track, account for, and reconcile Metropolitan's assets, including land, easements, and right-of-way, to the general ledger. We acknowledge that Management is researching this item and we encourage them to resolve the noted discrepancy.

Employee and Director Expense Audit Report

Background

Metropolitan's Administrative Code and Travel Guide specify travel policies; expense reporting procedures; and guidelines for preparing and submitting expense reports. Expense reports are processed through the Travel Expense Reporter (TER) System for Board of Directors and employees who have incurred travel expenses and operating expenses on behalf of Metropolitan. The Payroll and Accounts Payable Team from the Controller Section in the Office of the Chief Financial Officer administers and records expense reports and issues payments.

For the twelve months ended March 31, 2007, expenses totaling approximately $2.8 million were processed through TER. This total was made up of 1,204 employees, who submitted 6,211 expense reports totaling approximately $2.6 million and 34 Board of Directors, who submitted 169 reports totaling $211,682. Airfare, lodging, Per Diem of employees, conference, and business mileage accounted for $1.7 million or 63% of total expenses incurred for the review period.

Opinion

In our opinion, the accounting and administrative procedures over employee and Board of Director expense reports include those practices usually necessary to provide for a generally satisfactory internal control structure. The degree of compliance with such procedures provided effective control for the period April 1, 2006 through March 31, 2007.

Comments and Recommendations

SUBMISSION OF TRAVEL EXPENSE REPORTS AND OUTSTANDING PREPAID EXPENSES

Section 6331 (b)(2) of the Administrative Code requires that the Board of Directors' expense claims shall be submitted to the Executive Secretary's office no later than the end of the month, following the month in which the Board of Director incurred the expenses or participated in an activity for which District funds were utilized on the director's behalf. In addition, Section 6331 (b)(3) also requires that the Employees' expense claims, approved in accordance with the provisions of this section, shall be submitted to the Office of the Chief Financial Officer no later than the end of the month following the month in which the employee incurred the expenses, or participated in an activity for which District funds were utilized on the employee's behalf.

Our review of employee and Board of Director expense reports submitted between April 1, 2006 and March 31, 2007, and analysis of the outstanding prepaid expenses revealed:

1. Employee Expense Reports: 523 expense reports were submitted beyond the 60-day guideline. It should be noted that the number of expense reports submitted beyond the 60-day guideline decreased by 1%, from 9% during the prior audit to 8% during the current review period.

Expense Reports Submitted	No. of Reports	Expenses Claimed
61 to 90 days	339 (5%)	$ 197,265
91 to 365 days	184 (3%)	140,511
Total	523 (8%)	337,776
Total for Period	6,211	$2,572,376

2. Director Expense Reports: 77 expense reports were submitted beyond the 60-day guideline. It should be noted that the number of expense reports submitted beyond the 60-day guideline decreased by 9%, from 54% during prior audit to 45% during review period.

Expense Reports Submitted	No. of Reports	Expenses Claimed
61 to 90 days	38 (22%)	$ 47,770
91 to 365 days	39 (23%)	87,631
Total	77 (45%)	135,401
Total for Period	169	$ 211,682

3. Outstanding Prepaid Expenses: 54 employees and Board of Directors, who incurred prepaid expenses totaling $26,310 between April 2006 and January 31, 2007, have yet to file the expense reports as of March 31, 2007. We understand that the Accounts Payable Team has sent letters to these employees and Board of Directors requesting them to submit travel expense reports to clear the outstanding prepaid expenses. The details of the outstanding prepaid expenses are:

Employee Outstanding Prepaid Expenses

No. of Days Outstanding	No. of Employees	Amount
61 to 90 days	8	$ 2,359
91 to 365 days	26	14,707
Total	34	$ 17,066

Board of Director Outstanding Prepaid Expenses

No. of Days Outstanding	No. of Directors	Amount
61 to 90 days	6	$ 1,931
91 to 365 days	14	7,313
Total	20	$ 9,244

We recommend that Group Managers continue to emphasize the importance of submitting travel expense reports within the 60-day guideline and conduct periodic tests to ensure compliance. We also recommend that the Accounts Payable Section, through coordination with Group Managers, continue to follow-up outstanding prepaid expenses of employees and Board of Directors.

TRAVEL IN EXCESS OF 200 MILES ONE-WAY GUIDELINE

Section 6326 (d) of the Administrative Code requires that the type of transportation employed shall be selected on the basis of the lowest overall cost to Metropolitan, after all costs are considered, including the travel time and the salary of the employee. This section also requires that trips, which require travel in excess of 200 miles one-way, shall be made by commercial airline. The reimbursements for any transportation costs for trips over 200 miles one-way by any form of transportation shall generally not exceed the standard round-trip airline coach airfare in effect at the time. These cost estimates are established by the Manager, Contracting Services, and include personal auto mileage and airport parking that would have been incurred and reimbursable, if airline transportation had been used.

Our review of 48-employee expense reports with reported mileage over 200 miles one-way revealed that 11 were without explanation or provided inadequate information (i.e., cost consideration, destination, purpose, duration), for using personal car in lieu of air transportation. In addition, although the expense reports submitted by an employee and a Board of Director were provided with explanation for using personal car, we noted that the car mileage incurred (1,018 and 1,428 miles, respectively) was more than five times the 200 miles one-way guideline.

We recommend that Group Managers continue to emphasize the importance of providing adequate information or explanation for business mileage claimed on the expense reports.

DOUBLE PAYMENT OF PER DIEM AND INTERNET CHARGES

Review and approval controls serve to protect against unauthorized, inaccurate, or duplicate transactions or requests; identify items that require correction; and ensure that follow-up procedures exist for exceptions. For expense reports, authorized personnel must review detail for compliance to policies and procedures, check attached documentation for completeness, and examine the claimed expenses for propriety.

Our review of expense reports revealed double payments totaling $330 to two employees and three Board of Director members for Per Diem and/or Internet communication charges. We understand that the Accounts Payable team has contacted the employees to seek reimbursement for $200 double payment. Furthermore, we understand that the Executive Office is resolving the Board of Director member items.

Brutoco Contract No. 1614 Audit Report

Background

In October 2005, Metropolitan entered into an $8.2 million contract with Brutoco Engineering and Construction, Inc. (Brutoco) to construct the Plant Maintenance Facilities (Project) as a component of the Oxidation Retrofit Program (ORP) at the Robert B. Diemer Water Treatment Plant (Diemer Plant). The ORP is being undertaken by Metropolitan to comply with the Environmental Protection Agency's Disinfectants/Disinfection Byproducts Rule and remove federal restrictions on blending Metropolitan water. The Diemer Plant blends Colorado River and

State Project water and delivers the blended water to Orange County and parts of Metropolitan's Central Pool. The Project consists of constructing new maintenance facilities, installing a 10-inch diameter fire water line and electrical substation/transformer, and excavating, paving, and landscaping the sites. The new maintenance facilities will include mechanical and electrical workshops, offices, and storage to support the maintenance of operating equipment. As of April 2007, the Project was completed and $8.6 million was paid to Brutoco.

Opinion

In our opinion, the operating and administrative procedures over Major Construction Projects-Brutoco Contract No. 1614 include those practices usually necessary to provide for a generally satisfactory internal control structure. The degree of compliance with such policies and procedures provided effective control for the period from October 2005 (contract inception) through June 2007.

Comments and Recommendations

REVIEW OF RETENTION DEPOSITS

Operational policies and administrative procedures are established and documented to provide a framework for managing construction contracts; preparing, processing, and recording monthly progress payments; and computing, monitoring and releasing contract retentions. A standard 10% "holdback" is retained from monthly progress payments on all construction contracts until_the project is 50% complete and is progressing satisfactorily. Under contract terms, retention amounts are either (1) held by Metropolitan, (2) transmitted to a bank escrow account selected by the contractor, or (3) released to the contractor upon the deposit of sufficient securities into escrow. Upon satisfactory completion of the project, the retention is released to the contractor.

Our review revealed that the 10% retention amounts withheld on the first three monthly progress payments (November and December 2005 and January 2006) were not deposited to the escrow bank until March 9, 2006. It should be noted, however, that retention amounts for subsequent monthly progress payments were deposited to the escrow bank timely, within 30 days of the invoice date.

We recommend that the Controller Management remind the Accounts Receivable and Accounts Payable to coordinate efforts and follow existing procedures to ensure retentions are deposited promptly to the escrow bank.

Continuous Audit Activities (monthly reviews)

Inland Feeder Project

Our review included agreeing actual costs reported to the Board of Directors to source documentation, including the general ledger, the Inland Feeder Project (IFP) Monthly Report, and selected contract payments; reviewing estimated costs at completion; analyzing changes in various cost components; and attending on-site meetings held to review actual costs and discuss current problems. Our review did not reveal any material differences between reported amounts and supporting documentation.

In addition, our ongoing review procedures for potential claims, liability exposures, and other pending issues have been designed to track such items in accordance with applicable reporting requirements under Financial Accounting Standards #5 (Accounting for Contingencies). Accordingly, for all pending legal claims, we consult with the Chief Financial Officer, IFP Management, or General Counsel's office to evaluate the magnitude of potential losses to Metropolitan. It should be noted that the IFP Project Manager reports on contractors' claims currently in litigation and other potential claim issues to the Board monthly.

Center for Water Education

Assisted Management on the review and assessment of proposed payments of the Center for Water Education's construction debts.