THE METROPOLITAN WATER DISTRICT OF SOUTHERN CALIFORNIA

# Report

Office of the General Auditor

June 30, 2009

- Internal Audit Report for June 2009

## Summary

Four reports were issued during the month:

- **Employee and Director Expense Reports Audit Report**
- **Energy Management Audit Report**
- **Official Statement for the Water Revenue Refunding Bonds, 2009 Authorization, Series B and C**
- **Official Statement for the Water Revenue Refunding Bonds, 2009 Authorization Series C, and 2008 Authorization Series B & C**

## Discussion Section

This report highlights the significant activities of the Internal Audit Department during June 2009. In addition to presenting background information and the opinion expressed in the audit reports, a discussion of findings noted during the examination is also provided.

# Employee and Director Expense Reports 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 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 issue payments.

For the twelve months ending March 31, 2009, expenses totaling approximately $2.3 million (15 percent decrease from prior year) were approved and processed through TER for employees, as well as directors. This total was made up of 4,857 employee expense reports totaling approximately $2.1 million and 130 director expense reports totaling $166,000. Tuition reimbursement, per diem of employees, lodging, airfare, conference, and business mileage accounted for $1.6 million or 70 percent of total expenses incurred for the review period.

**Opinion**

In our opinion, the accounting and administrative procedures over the Employee and 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, 2008 through March 31, 2009.

**Comments and Recommendations**

LATE SUBMISSION OF TRAVEL EXPENSE CLAIMS; UNFILED TRAVEL EXPENSE REPORTS AND RECONCILIATION FOR PREPAID EXPENSES

Section 6331(b)(2)(3) of the Administrative Code requires that the directors' and employees' expense claims be submitted to the Office of the Executive Secretary and the Office of the Chief Financial Officer, no later than 60 days, and AFSCME no later than 90 days, following the day director or employee incurred the expenses or participated in an activity for which Metropolitan funds were utilized on the director's or employee's behalf.

We reviewed 27,283 expense line items claimed on 5,190 Employee and Director Travel Expense Reports (TERs) submitted between April 1, 2008 and March 31, 2009 for timely submission. Of this number, 4,987 TERs were submitted, approved, and processed (4,857 employees' TERs and 130 directors') and 203 were submitted but not processed.

1. **Employee Expense Reports**: 2,402 expense line items claimed on 392 TERs were submitted late (beyond the 60-day standard). This is an increase of 9 percent from prior year.

| No. of Days Expense was Incurred | No. of Expense Items | No. of Expense Reports (TERs) | Expenses Claimed |
|---|---|---|---|
| 61 to 90 days | 1,228 | 264 | $93,819 |
| 91 to 180 days | 1,002 | 136 | $107,932 |
| 181 to 365 days | 172 | 24 | $17,514 |
| Total | 2,402 | 392* | $219,265 |
| Total for Period | 27,283 | 5,059 | 2,231,592** |

2. **Director Expense Reports**: 736 expense line items claimed on 54 TERs were submitted late (beyond the 60 day standard). This is a decrease of 24 percent from prior year.

| No. of Days Expense was Incurred | No. of Expense items | No. of Expense Reports (TERs | Expenses Claimed |
|---|---|---|---|
| 61 to 90 days | 409 | 52 | $36,691 |
| 91 to 180 days | 271 | 23 | $21,567 |
| 181 to 365 days | 56 | 2 | $4,133 |
| Total | 736 | 54* | $62,390 |
| Total for Period | 2,461 | 131 | $166,589*** |

* This does not equate the total of TERs submitted beyond 60 days because one TER may include items which fall into 61- 90, 91-180, or 181-365 days delay category.
* * Represents submitted, approved and processed TERs ($2.1 million) as well as submitted but not approved/processed ($138,000).
*** Represents, submitted, approved and processed TERs ($166,000) as well as submitted but not approved/processed ($589).

We also reviewed 656 expense line items for expenses prepaid by Metropolitan and incurred by employees and directors between April 1, 2008 and March 31, 2009, but TERs had not been filed. These items were prepaid through check payments or agency issued credit cards. Our analysis revealed:

3. Outstanding Prepaid Expenses: 57 employees and 21 directors have yet to file expense reports for $146,893 ($111,504 for employees and $35,389 for directors) prepaid by Metropolitan (through check payment and agency issued credit cards) within the 60-day standard.

**Employee**:

| No. of Days Expense was Incurred | No. of Expense Items | Expenses Claimed for Employees |
|---|---:|---:|
| 61 to 90 days | 63 | $11,551 |
| 91 to 180 days | 168 | $46,794 |
| 181 to 365 days | 246 | $53,159 |
| Total | 477 | $111,504 |

**Director**:

| No. of Days Expense was Incurred | No. of Expense Items | Expenses Claimed for Directors |
|---|---:|---:|
| 61 to 90 days | 22 | $2,702 |
| 91 to 180 days | 77 | $14,976 |
| 181 to 365 days | 79 | $17,711 |
| Total | 178 | $35,389 |

4. Reconciliation of Prepaid Expenses: 150 expense items totaling $18,911, that were submitted on TERs and prepaid through company issued credit cards, have not been reconciled to the monthly credit card statements by the Payroll and Accounts Payable Team. These expenses were incurred between April 2008 and January 2009.

We recommend that Group Managers continue to emphasize the importance of submitting TERs within the 60-day guideline and conduct periodic tests to ensure compliance. We also recommend that the Payroll and Accounts Payable Team, through coordination with Group Managers, continue to follow-up outstanding prepaid expenses to employees and directors. Furthermore, we recommend that the Payroll and Accounts Payable Team complete review and verification of expenses paid through company issued credit cards in a timely manner.

MILEAGE REIMBURSEMENT

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.

We reviewed ten travel expense claims (of 208 total claims) with reported mileage over 200 miles one-way and noted that none had adequate information or explanation (i.e., cost consideration) for using personal car in lieu of air transportation. This is in contrast to Section 6326(d) of the Administrative Code that requires consideration for transportation's lowest overall cost to Metropolitan.

We recommend that the Group Managers emphasize the importance of providing adequate information or explanation for business mileage claimed on the expense reports. In addition, we recommend that the approving Manager and the Payroll and Accounts Payable Team ensure that the cost comparison information is provided in the TER by the claimants.

DUPLICATE PAYMENT OF CLAIMED EXPENSES

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.

We reviewed 350 potentially duplicated expense items totaling $17,814 and noted double payments for five expense items totaling $362. These expenses were claimed for reimbursement by four employees and one director. We understand that the Accounts Payable Team has contacted the four employees to seek reimbursement. We were informed that three of these employees had already paid $164 and that the other two employees have agreed to pay the remaining amount ($136) to Metropolitan. We were also informed that the duplicate payment of $60 to the director was deducted from his subsequent TER reimbursement.

We recommend that Group Managers conduct a thorough review of expense reports to ensure validity and accuracy of reported claims and completeness of supporting documentation. We also recommend that the Payroll and Accounts Payable Team review the TER system "Duplicate Transaction Report" on a monthly basis to verify for duplicate payments. In addition, we recommend that the Payroll and Accounts Payable Team make follow-ups to collect the remaining unreimbursed amount of $136.

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# Energy Management Program Audit Report

**Background**

Metropolitan initiated the Energy Management Program in the fall of 2006 partly in response to the California Global Warming Solutions Act of 2006 (Assembly Bill 32), which requires California to reduce Greenhouse Gas (GHG) emissions to 1990 levels by 2020. The Energy Management Program's four primary goals are to: 1) Identify Metropolitan's GHG inventory; 2) Implement additional renewable energy production; 3) Reduce energy consumption; and 4) Develop and implement comprehensive strategies to manage power resources in a cost-effective manner. By accomplishing these goals, Metropolitan hopes to reduce its carbon footprint and operate its facilities in a sustainable manner to help California comply with the requirements of Assembly Bill 32.

In February 2007, the Board authorized Metropolitan's membership to the California Climate Action Registry (CCAR). CCAR helps organizations like Metropolitan establish their GHG inventory baselines for comparison against GHG emission reduction accomplishments, and to evaluate these efforts against future requirements. The CCAR sponsored GHG inventory tracks the amount of GHG emitted to and removed from the atmosphere by human activities in California. In late 2007, Metropolitan completed its baseline GHG inventory for calendar years 2005 and 2006. Ongoing work under the Energy Management Program includes establishing design standards for energy-efficient facilities, taking advantage of available rebates for energy efficiency and energy-saving projects, and continuing to investigate renewable and sustainable energy sources.

In August 2008, the Board approved twelve energy principles that provide direction for Metropolitan's activities. These principles were grouped into four categories: reliability, economics, compliance/ regulatory, and stewardship. They complement and augment the existing energy policy principles adopted in 1996 and 2002, to reflect the changes to the energy industry and to address issues such as climate changes and GHG emission management.

Responsibilities for the Energy Management Program are split between the Water System Operations and the Corporate Resources Groups. The areas of demand management, energy efficiency, power resources, treatment process assessments, and impacts to operations are managed by representatives from the Water System Operations Group. Whereas, design, facilities, equipment, carbon footprint, and information technology are managed by the Corporate Resources Group. Together, they are tasked with implementing Energy Management Program principles and achieving the program's goals. The total amount spent on the Energy Management Program as of February 2009 was $418,000.

## Opinion

In our opinion, the accounting and administrative procedures over the Energy Management Program 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 January 2007 through March 2009.

## Comments and Recommendations

### POLICIES AND PROCEDURES

Operating policies and procedures should be established and documented to provide a framework for achieving Metropolitan's goals properly and adequately. Whereas policies guide actions toward a desired outcome, procedures provide Management with guidelines for consistent performance of daily operations. For the Energy Management Program, formal policies should establish standards for measuring the progress of the program and define responsibilities over energy use and conservation efforts. Formal procedures, then should establish processes for compiling and analyzing Greenhouse Gas (GHG) emission amounts. Procedures also should identify guidelines for using the GHG emissions spreadsheet, establish standards for security, and access restriction of the GHG emissions spreadsheet, as well as define the roles and responsibilities in the preparation and review of GHG inventory.

Although Management has established energy management principles that provide direction for Metropolitan's energy activities, detailed policies and procedures have not been established to ensure that long-term goals are achieved and to establish standards for daily operations. Specifically, while we note that Management has prepared an overview of Metropolitan's carbon footprint preparation process, detailed procedures for the preparation of GHG inventory have not been developed. These procedures should include those processes for securing access to the GHG emissions spreadsheet, provide for the training of personnel, ensuring the use of current protocols, and for the review and approval of Management reports.

We recommend that Management develop and implement comprehensive policies and procedures for the Energy Management Program.

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## Official Statement for the Water Revenue Refunding Bonds, 2009 Authorization, Series B and C

**Background**

The Audit Department has completed a review of the Official Statement for the Water Revenue Refunding Bonds, 2009 Authorization, Series B and C. This review was undertaken to provide the underwriters of the Water Revenue Refunding Bonds (Bonds) "comfort" that the Official Statement for the Bonds is complete, consistent with supporting financial records, and accurate in all material respects. The review was completed and no exceptions were noted. We issued letters describing the agreed upon procedures, and the results obtained to the underwriters of the Bonds.

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## Official Statement for the Water Revenue Refunding Bonds, 2009 Authorization Series C, and 2008 Authorization Series B & C

**Background**

The Audit Department has completed a review of the Official Statement for the Water Revenue Refunding Bonds, 2009 Authorization Series C, and 2008 Authorization Series B and C. This review was undertaken to provide the underwriters of the Water Revenue Refunding Bonds (Bonds) "comfort" that the Official Statement for the Bonds is complete, consistent with supporting financial records, and accurate in all material respects. The review was completed and no exceptions were noted. We issued letters describing the agreed upon procedures, and the results obtained to the underwriters of the Bonds.

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## Continuous Audit Activities (Monthly Reviews)

Inland Feeder Project

Our review included agreeing actual costs reported to the Board 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. These meetings included extensive discussions on the progress of obtaining pipe hauling permits from the city of San Bernardino and the impact that these efforts have on project costs. We also reviewed the procedures designed to dispose of salvaged equipment to ensure the safeguarding of assets and the propriety of the processes. 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 consulted with the Chief Financial Officer, IFP Management, or General Counsel's Office to evaluate the magnitude of potential loss to Metropolitan. It should be noted that the IFP Manager reports on contractors' claims currently in litigation and other potential claim issues to the Board monthly.