



THE METROPOLITAN WATER DISTRICT  
OF SOUTHERN CALIFORNIA

## **Internal Audit Report for September 2011**

### **Summary**

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Two reports were issued during the month:

- **Innovative Conservation Program Audit Report**
- **Official Statement for the Water Revenue Refunding Bonds, 2011 Authorization, Series C**

### **Discussion Section**

This report highlights the significant activities of the Internal Audit Department during September 2011. 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.

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## **Innovative Conservation Program Audit Report**

### **Background**

Our review consisted of tests of grants awarded under the Innovative Conservation Program (ICP) to innovators or sponsors (member agencies) of new water conserving technologies. In addition, we reviewed the United States Bureau of Reclamation (USBR) grant-matching agreements that supplement ICP. We examined the agreement administration, recording and reporting practices, and tested compliance with the terms and conditions of the contracts. We also tested the grant recipient invoice and payment processes, and examined Metropolitan's requests for reimbursement from USBR for propriety and timeliness.

Metropolitan's Integrated Water Resources Plan establishes a strategy for regional water supply reliability for the next 25 years. As a part of these plans, ICP was designed to award grants to developers for new water saving strategies and methods. In December 2005, the Board authorized grant funding totaling \$250,000 for ICP.

Concurrent with these efforts, Metropolitan obtained matching funding from USBR under two assistance agreements. The first agreement was executed in September 2006, effective through July 2009. This agreement provided matching funds of up to \$300,000 for new ICP projects. The second agreement was executed in 2008, effective through December 2010 and provided up to \$228,000 of additional funding. Both agreements were modified to extend the termination date for two years. As of July 31, 2011, ICP has awarded \$457,825 of the \$604,701 total available grant funding. ICP payments made by Metropolitan and USBR were \$231,746 and \$226,078, respectively.

A five-member panel consisting of a representative from Metropolitan, USBR, Southern California Gas Company, Huntington Botanical Gardens, and a member agency evaluated and selected participants for ICP. Under the September 2006 agreement, ICP received 29 proposals and awarded 11 grants.

Under the September 2008 agreement, ICP received 11 proposals and awarded four grants. Funded projects took about two years to complete. The following table summarizes ICP details:

USBR Agreement Year	USBR Funding Period	Number of Proposals Accepted under ICP	Total Grant Contract Amounts	Total Payments to Grant Recipients as of 7/31/2011			Total Matching Funds Received from USBR to date
				Total Paid to Grant Recipients	MWD's portion of Grant Payments	USBR's portion of Grant Payments	
2006	Sept 2006 - June 2011	11	\$428,985	\$336,725	\$168,362	\$168,363	\$168,363
2008	Sept 2008 - Dec 2012	4	\$175,716	\$121,100	\$63,384	\$57,716	\$37,620
Total			\$604,701	\$457,825	\$231,746	\$226,078	\$205,982

### **Opinion**

In our opinion, the accounting and administrative controls over the Water Resource Management (WRM) Group - Innovative Conservation 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 July 2007 through July 2011.

### **Comments and Recommendations**

#### COMPLIANCE WITH TERMS AND CONDITIONS OF THE AGREEMENTS AND DETERMINATION OF STANDARD TERMS AND CONDITIONS

Compliance with contractual requirements is necessary to ensure accurate accounting records, proper supporting detail, and adequate control over the administration of the agreements. Compliance with the contractual terms and conditions also ensures that parties fully discharge their duties and obligations, and exercise their legal rights associated with the agreements. We reviewed seven grant agreements and 12 grantee invoices totaling \$239,300 and noted:

1. Evidence for one invoice (\$8,500) to verify that it had been certified for complete installation could not be located. This is in contrast to the grant agreement.
2. Six of 12 grantee invoices (totaled \$137,000) were submitted directly to the agreement administrator rather than to the Accounts Payable Team. This is in contrast to the current procedures of submitting vendor invoices directly to the Accounts Payable Team.

3. Grant agreements do not contain language to reduce grant amount to actual project cost. For instance, Agreement 91615 states that Metropolitan's financial contribution is \$43,800, and that the grant recipient will be responsible for all costs in excess of that amount. However, Agreement 91615 was completed for \$39,100; \$4,700 less than the grant amount. It is important to note that Metropolitan only paid out \$39,100, and that it already sent an agreement termination letter to the grantee to affirm that all invoices were paid and obligations were met.

We also reviewed Metropolitan's billings to USBR to seek reimbursement for its share of ICP costs and noted:

4. Substantial delays in billing to USBR for reimbursement, after making payments to grantees. We noted that three invoices totaling \$110,590 were billed to USBR up to 515 days, after grantee payments.
5. Reimbursable amount totaling \$20,096 had not been invoiced to USBR, as of July 31, 2011 for payment to grantees under two projects (91695 and 91696) from March 2010 through December 2010.

Failure to comply with the established procedures and the terms and conditions of the grant agreements could result in financial losses to Metropolitan due to fraudulent, erroneous, duplicate, or unauthorized transactions. Noncompliance has resulted in late billings for reimbursable costs.

We recommend that WRM Group management remind ICP management and grant recipients to comply with Metropolitan's established procedures for the submission of grantee invoices, and adhere to the terms and conditions of the grant agreements. We also recommend that WRM Group management conduct periodic reviews to ensure compliance. Lastly, we recommend that ICP management invoice USBR for its share of ICP costs on a timely basis.

## CONTRACT CLOSEOUT PROCEDURES

Contract administration entails planning, organizing, and managing resources to bring about the successful completion of a contract. It involves monitoring and controlling activities from contract initiation to contract closeout. Moreover, contracts should be closed after all contractual requirements have been met, all invoices have been accrued or paid, and Metropolitan has discharged all obligations. We reviewed the contract closeout procedures and noted:

1. Closeout procedures for grant agreements are not documented in writing.
2. Four grant agreements were closed from 162 to 256 days, after agreement expiration date.
3. Grant Agreement 91618 remained open for 410 days passed its expiration date.

Failure to close out expired or terminated grant agreements could result in unrelated costs being charged to the agreement and financial losses to Metropolitan due to fraudulent, erroneous, or unauthorized transactions.

We recommend that ICP management develop closeout procedures for grant agreements to ensure consistency and prompt closure of expired or terminated agreements, and conduct periodic tests to ensure compliance.

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## **Official Statement for the Water Revenue Refunding Bonds, 2011 Authorization, Series C**

The Audit Department has completed a review of the Official Statement for the Water Revenue Refunding Bonds, 2011 Authorization, Series C. We performed this review to provide the issuer of the Bonds “comfort” that the Official Statement for the Bonds is complete, consistent with supporting financial records, and accurate in all material respects. We completed our review in accordance with agreed upon procedures specified by the underwriter. We issued letters to the underwriter describing the agreed upon review procedures performed, and the results obtained.

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