



Internal Audit Report for May 2015

Summary

Three reports were issued during the month:

- **Capital Investment Plan - Prestressed Concrete Cylinder Pipe Rehabilitation and Replacement Program Appropriation 15471 Audit Report**
- **Fraser Communications Agreement 143867 Audit Report**
- **Procurement Card Program Follow-up Review**

Discussion Section

This report highlights the significant activities of the Internal Audit Department during May 2015. In addition to presenting background information and the opinions expressed in the audit reports, a discussion of findings noted during the examination is also provided.

Capital Investment Plan - Prestressed Concrete Cylinder Pipe Rehabilitation and Replacement Program Appropriation 15471 Audit Report

Background

The Audit Department has completed a review of the accounting and administrative controls over the Capital Investment Plan (CIP) - Prestressed Concrete Cylinder Pipe (PCCP) Rehabilitation and Replacement Program Appropriation 15471, as of February 28, 2015.

Our review consisted of evaluating project administration and authorization, reporting practices, change authorizations, and project closeout processes. We also evaluated invoice payments for assurance that amounts billed were properly calculated, and adequately supported. Finally, we reviewed the Actual versus Budgeted Costs on a project-by-project basis and compared these totals to the appropriated amounts and management reports. Metropolitan's water delivery system includes approximately 830 miles of pipelines, of which 163 miles are PCCP lines. Metropolitan installed these lines between 1965 and 1985, in dense-urban areas and remote regions. These PCCP lines range between 54 and 201 inches in diameter.

However, during the 1990s, water systems throughout the country experienced an increasing number of PCCP line failures. These incidents compelled PCCP owners to develop inspection, monitoring, and repair programs to ensure the reliability of such pipelines. These efforts aided in the assessment and determination of the condition and stability of their PCCP lines, along with the potential for a reduced service life.

Metropolitan developed the PCCP Inspection Plan under its Infrastructure Reliability Protection (Infrastructure) Program to respond to these PCCP line reliability concerns. Accordingly, the Board authorized the PCCP Rehabilitation and Replacement Program in December 1996, to assess the condition of Metropolitan's PCCP lines. After assessing 163 miles of PCCP lines, the PCCP lines were prioritized based on a relative risk. The Engineering Services Group (ESG) initiated the PCCP Rehabilitation and Replacement Program in September 2011 to inspect, monitor, repair, and rehabilitate its PCCP lines.

The Second Lower Feeder was the first PCCP Rehabilitation and Replacement Project initiated under the Infrastructure Program. The Second Lower Feeder delivers treated water from the Robert B. Diemer Treatment Plant in Yorba Linda, to the Palos Verdes Reservoir in Rolling Hills Estates. Constructed in 1967, the Second Lower Feeder supplies water to the Central Pool portion of Metropolitan's distribution system. In addition, it has 11 service connections for deliveries to the cities of Long Beach, Los Angeles, and Torrance; the Central Basin Municipal Water District; and the Municipal Water District of Orange County. Approximately 30 miles of this 39-mile line are constructed of PCCP, with diameters ranging from 78 to 84 inches.

As of February 28, 2015, the PCCP Rehabilitation and Replacement Program consisted of four Second Lower Feeder projects and nine inspection/repair projects. Four projects have been completed and nine projects are in progress, with project costs totaling \$30.1 million out of \$38.1 million appropriated. To date, the PCCP Rehabilitation and Replacement Program is within budget and on schedule. It should be noted that ESG staff estimates the total PCCP Rehabilitation and Replacement Program costs at more than \$2 billion.

Opinion

In our opinion, the accounting and administrative procedures over the CIP - PCCP Rehabilitation and Replacement 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 controls for the period ending February 28, 2015.

Comments and Recommendations

PROJECT COMPLETION AND CLOSEOUT

The primary goal of project management is to achieve project objectives and manage resource constraints, including time and budget. This involves monitoring and controlling activities from project initiation to project completion. Projects should be promptly closed after all contractual requirements have been met, invoices paid, and Metropolitan has discharged its obligations. Our review of 13 projects revealed that Projects 104402 and 104398 were completed in December 2013, but closed 10 months after completion date.

We recommend project management modify procedures to ensure projects are closed out on a timely basis, and conduct reviews to ensure compliance.

Fraser Communications Agreement 143867 Audit Report

Background

The Audit Department has completed a review of the accounting and administrative controls over consulting Agreement 143867 with Fraser Communications (Fraser), as of February 2015. Our review consisted of evaluating internal controls over agreement administration, reporting practices, and testing compliance with the terms and conditions of the agreement. We also evaluated the validity and propriety of invoice payments for assurance that amounts billed were properly calculated, and adequately supported.

The Metropolitan Board declared a Water Supply Alert throughout its 5,200 square-mile service area on February 11, 2014 in response to statewide drought, formally endorsing Governor Edmund G. Brown Jr.'s statewide call for conservation. The Metropolitan Board called for water-use reductions, and doubled Metropolitan's annual conservation and public outreach budget from \$20 million to \$40 million. The increase provided additional rebate incentives for Southern Californians to purchase water-saving devices throughout Metropolitan's six-county service area. They also provided for funding to increase awareness about the ongoing unprecedented drought condition and to educate the public on critical water conservation measures.

Metropolitan entered into a three-year Sole Source Agreement 143867 with Fraser to deploy a Strategic Water Awareness campaign. Agreement 143867 was effective from March 11, 2014 through March 10, 2017 with a maximum amount payable of \$5.5 million the first year, and remaining two years subject to board approval. Payments to Fraser from March 11, 2014 through February 2015 totaled \$5.44 million consisting of: Airtime \$4.38 million; Media and Production \$482,000; and Agency Commission and Other Charges \$580,000.

In January 2015, Metropolitan issued Request For Proposals (RFP) 1089 to provide Water Awareness and Conservation Advertising Services and terminated Fraser Agreement 143867; 12 firms responded to RFP 1089. Quigley-Simpson and Heppelwhite Incorporated received the highest score and was awarded a one-year contract, not-to-exceed \$5.5 million.

Opinion

In our opinion, the accounting and administrative procedures with Fraser 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 controls from March 2014 through February 2015.

Comments and Recommendations

NONCOMPLIANCE TO TERMS AND CONDITIONS

Compliance with contractual requirements is necessary to ensure accurate accounting records, proper supporting detail, and adequate control over administration of the agreement. Further, compliance with agreement terms and conditions ensure that parties fully discharge their duties and obligations,

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exercise their rights associated with the agreement. During our review of nine Fraser invoices totaling \$2.3 million, we noted:

1. We could not locate evidence to support that External Affairs had performed random tests of source documentation, in support of consultant billings. These tests would provide greater assurance that the number of advertisement spots ordered was actually aired, as scheduled. It is important to note that further testing did not reveal any discrepancies or incorrect billings.
2. Section 9 of Agreement 143867 requires Fraser to submit monthly invoices to Metropolitan, with invoice billing periods. We noted one invoice totaling \$184,860 without the billing period.
3. Two invoices were paid two to 19 days, after the due date.

We recommend that management develop written procedures to ensure random checks of source documentation, in support of consultant billings. We also recommend that the agreement administrator remind the consultant to comply with agreement terms and conditions.

Procurement Card Program Follow-up Review

Background

We have completed a Follow-up Review of the Procurement Card (P-Card) Program Audit Report recommendations issued on February 27, 2014. This review is required by Audit Department Policies and Procedures, which prescribes a Follow-up Review on audits receiving a less than satisfactory opinion.

We reviewed management's Action-Plan Implementations to ascertain whether actions taken adequately mitigated issues identified, and lowered associated risks to a reasonable level. Our review revealed that Contracting Services Unit management has taken the necessary steps to address audit report issues; worked with staff to complete resolution of noted P-Card transaction discrepancies; developed and updated procedures to streamline transaction review and approval process; and improved overall supervision and reporting of the P-Card Program.

Testing further revealed that P-Card management has established specific responsibilities and administrative guidelines for P-Card renewals, replacements, and cancellations; performed detailed transaction analyses to monitor and report P-Card activities; developed and provided training to cardholders and their approving managers; and conducted random examinations to test P-Card Policies and Procedures compliance.
