



Internal Audit Report for June 2016

Summary

Three reports were issued during the month:

1. **Internal Controls over Financial Reporting Review**
2. **Official Statement for the Water Revenue Refunding Bonds, 2016 Authorization, Series A**
3. **Colorado River Aqueduct Conveyance Reliability 15373 and Discharge Containment 15385 Programs Audit Report**

Discussion Section

This report highlights the significant activities of the Internal Audit Department during June 2016. In addition to presenting background information and the opinion expressed in the audit report, a discussion of findings noted during the examination is also provided.

Internal Controls over Financial Reporting Review

We have completed a limited review of the internal controls over financial reporting for fiscal year ended June 30, 2015. Specifically, we performed procedures to provide a level of assurance to the Board and management, that controls related to the reliability and integrity of financial reporting are effective. The review was required by Administrative Code Section 6451(d) (3) - Audit Department Charter Responsibilities, which directs the Audit Department to issue an opinion on internal controls over financial reporting on an annual basis.

The Institute of Internal Auditors International Standards for the Professional Practice of Internal Auditing requires that auditors evaluate the risk exposure, adequacy, and effectiveness of controls relating to the reliability of financial information. It should be noted that the review was for the limited purpose of assessing controls over financial reporting. In accordance with these requirements, our review procedures were based on the internal controls integrated framework set forth by the Committee of Sponsoring Organizations of the Treadway Commission. Utilizing this framework:

1. We analyzed the results of the fiscal year 2014/15 Audit Plan which included completion of 25 audits, 9 monitoring reports, 5 bond Comfort Letters, 2 special projects, and 2 follow-up reviews over areas rated with opinions of less than satisfactory. As part of the audit results review, we also evaluated management's responses to ensure they were timely and that management had effectively addressed our concerns. We also evaluated documentation pertaining to key business controls prepared by the Controller's Office, in accordance with their responsibilities specified in Administrative Code Section 2700 (c) (2), General Manager's Annual Report to the Executive Committee on the effectiveness of Metropolitan's internal control system, including information technology security and control.

Date of Report: June 30, 2016

The Controller's final assessment concluded that internal controls over financial reporting, and information technology security were effective for the 12 months ending June 30, 2015. We considered the results of this review a part of the assessment. Lastly, we evaluated the scope and results of the substantive testing performed for the external auditors during their fiscal year 2014/15 Financial Statements audit. This testing provided us with evidence used in the evaluation of financial reporting controls.

2. We analyzed selected financial statement accounts and transactions, based on risk and materiality. We also performed process walkthroughs and selected testing in key financial areas including revenue and receivables; cost of water and water inventory; property, plant, and equipment; purchasing and payables; debt management; employee compensation and benefits; and financial reporting. Finally, we evaluated selected application controls over major financial systems; reconciliation controls for major accounts including Accounts Payable, Accounts Receivable, and cash; access controls for financial information systems; and controls over documents supporting financial transactions.

Our evaluation was made for the limited purpose described in the first paragraph, and would not necessarily disclose all material weaknesses in the system. We did not express an opinion on the system of internal controls taken, as a whole. Based on the results of the review, there is reasonable assurance that internal controls on June 30, 2015 were adequate to achieve reliable financial reporting.

Official Statement for the Water Revenue Refunding Bonds, 2016 Authorization, Series A

The Audit Department has completed a review of the Official Statement for the Water Revenue Refunding Bonds, 2016 Authorization, Series A. 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 underwriters. We found such information to be correct in all material respects. We issued letters to the underwriters describing the agreed-upon review procedures performed, and results obtained.

Colorado River Aqueduct Conveyance Reliability 15373 and Discharge Containment 15385 Programs Audit Report

Background

The Audit Department has completed a review of the accounting and administrative controls over the Colorado River Aqueduct Conveyance Reliability (15373) and Discharge Containment (15385) Programs as of March 31, 2016.

Our review consisted of evaluating the internal control structure over contractor selection, reviewing agreement administration and reporting practices, and testing compliance with the significant terms and conditions of the contract. In addition, we reviewed project authorizations, actual versus budgeted costs and close-out processes of the Program. Lastly, we evaluated the reasonableness and validity of progress payments, and the accuracy and completeness of source documents and financial records.

The Colorado River Aqueduct (CRA) is a 242-mile-long conveyance system which transports water from the Colorado River to Lake Mathews. It consists of five pumping plants; 124 miles of tunnels, siphons, and reservoirs; 63 miles of canals; and 55 miles of conduits. The five pumping plants along the CRA are located in remote areas of Riverside and San Bernardino Counties. Major portions of the system were initially constructed in the late 1930s and have been in continuous service ever since. However, in recent times portions of the system have exhibited signs of wear and tear. Accordingly, Metropolitan established the CRA capital investment program to repair, refurbish or replace worn system components. Included in these efforts are the Conveyance Reliability (15373) and the Discharge Containment (15385) Programs

The Conveyance Reliability program is designed to help ensure CRA reliability and operational efficiency. The program consists of 19 projects (7 completed and 12 ongoing), with an appropriation of \$99.6 million and costs incurred of \$87.5 million as of March 2016. The program is within budget and is estimated to be completed in 2025.

Conveyance Reliability Program (15373) Completed Projects

Item	Project #	Description	Amount
1	103201	CRA Conveyance Reliability, Phase II Repairs and Instrumentation	\$38,329,973
2	103253	CRA Pump Wells Conversion and Blow-Off Repair	1,697,861
3	103337	CRA Emergency Repair, Aqueduct Rupture in Desert Hot Springs, near Big Morongo Siphon	369,336
4	103426	CRA, Blow-Off Valve Flange Outlet Replacement	2,612,657
5	103609	CRA - DWCV-4 Valve Replacement	1,328
6	103749	CRA Transition Structure and Manhole Covers Replacement	5,038,154
7	103754	Cast-Iron Blow Off Replacement - Phase 4	843,953
		Total	\$48,893,262

Conveyance Reliability Program (15373) Ongoing Projects

Item	Project #	Description	Amount
1	103237	CRA - Siphons and Reservoir Outlets Refurbishment	\$1,237,621
2	103427	CRA - Head Gates Rehabilitation	292,282
3	103438	CRA - Iron Mountain, Tunnel Rehabilitation	821,470
4	103439	CRA - Eagle Mountain Sand Traps Inflow Study	33,820

5	103738	CRA Copper Basin Outlet Gates Reliability Study	12,058
6	103739	Copper Basin Outlet Rehabilitation	8,490,853
7	103750	CRA - Discharge Line Isolation Gates	1,038,929
8	103751	CRA Reliability Program Phase 6 (San Jacinto Diversion Structure & Service Connection DW-CV-4)	5,668,209
9	103770	CRA Siphons, Transitions, Canals, and Tunnels Rehabilitation and Improvements	13,816,331
10	104093	CRA Sand Trap Equipment Upgrades	3,160,527
11	104324	San Jacinto Tunnel East Adit Rehabilitation	3,225,430
12	104525	Copper Basin & Gene Wash Dam Sluiceways Rehabilitation	764,747
		Total	\$38,562,277

The Discharge Containment program is designed to ensure compliance with regulations for the safe disposal and discharge of chemicals used by the water treatment plants. The program consisted of 8 projects (2 completed and 6 ongoing), with an appropriation of \$7.9 million and costs incurred of \$6 million as of March 2016. The program is within budget and is estimated to be completed in 2021.

Discharge Containment Program (15385) Completed Projects

Item	Project #	Description	Amount
1	103272	CRA Discharge Containment Program, Gene Camp and Iron Mountain Equipment Wash Drains	\$209,000
2	104241	Hinds Pumping Plant Equipment Wash Area Upgrades	180,191
		Total	\$389,191

Discharge Containment Program (15385) Ongoing Projects

1	103151	CRA - Desert Sewer System Rehabilitation Project	\$1,065,502
2	103247	CRA Discharge Containment	246,285
3	103318	CRA Transformer Oil and Sodium Hypochlorite Containment	908,610
4	103621	CRA Desert Pump Plant Oil Containment Project	251,689
5	104526	CRA Pumping Plant Wastewater System - Gene & Iron Mountain	497,957
6	104542	CRA Pumping Plant Wastewater System - Hinds & Eagle Mountain	2,663,205
		Total	\$5,633,248

Opinion

Date of Report: June 30, 2016

In our opinion, the accounting and administrative procedures over the 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 2013 through March 2016.

Comments and Recommendations

PROJECT COMPLETION AND CLOSEOUT

Project Management involves planning, organizing, and managing resources to bring about the successful completion of project goals and objectives. It involves monitoring and controlling activities from project initiation to project closeout. Projects should be closed after all contractual requirements have been met, all invoices have been accrued, and/or paid, and Metropolitan has discharged all obligations.

Our review of ten selected projects (6 ongoing and 4 closed projects) revealed three closed projects were closed from 399 to 1,450 days after project completion date.

Failure to close projects upon completion could result in unrelated costs being charged to the projects, a potential understatement of depreciation expense, or projects being incomplete for an unacceptable length of time.

We recommend Program Management remind staff the importance to close completed projects in a timely manner and conduct periodic reviews to ensure completed projects are closed.
