



• **Board of Directors**  
***Audit and Ethics Committee***

9/11/2018 Board Meeting

8-4

**Subject**

Adopt CEQA determination and adopt reporting structure for Metropolitan's Ethics Officer

**Executive Summary**

In July 2017, at the request of the Chairman of the Board, the General Manager entered into a contract for legal services with Wilmer Cutler Pickering Hale and Dorr LLP (Wilmer Hale) to review the policies and procedures of Metropolitan's Ethics Office and provide recommendations for consideration by Metropolitan's Board. In September 2017, the Metropolitan Board accepted the resignation of Metropolitan's Ethics Officer and appointed Metropolitan's Auditor to serve as the interim Ethics Officer. In February 2018, Wilmer Hale made a presentation to the Executive Committee regarding their review of the policies, procedures, and governance of the Ethics Office. After the presentation, the Board recommended that staff work with new counsel to propose appropriate actions to assist in the implementation of policies approved by the Board. The areas of discussion include the reporting structure for the Ethics Officer. The law firm Olson Hagel & Fishburn (Olson Hagel) was engaged to independently review the findings and recommendations of Wilmer Hale, make recommendations designed to clarify the role, enhance the operational effectiveness of the Ethics Office, and assist in the implementation of any changes authorized by the Board.

**Details**

**Background**

In 1999, SB 60 added Section 126.7 to the Metropolitan Water District Act. The new provision required Metropolitan to *"establish and operate an Office of Ethics and adopt rules relating to internal disclosure, lobbying, conflicts of interest, contracts, campaign contributions, and ethics for application to its board members, officers and employees . . ."* Section 126.7(c) (1) provides: *"The office shall operate as an independent entity that is not subject to political influence and shall be staffed with professional, qualified persons."*

In July 2017, in response to matters brought to the attention of the Chairman of the Board, at the Chairman's request, the General Manager entered into a contract for legal services with Wilmer Cutler Pickering Hale and Dorr LLP (Wilmer Hale) to review the policies and procedures of Metropolitan's Ethics Office and provide recommendations for consideration by Metropolitan's Board.

In September 2017, the Metropolitan Board accepted the resignation of Metropolitan's Ethics Officer and appointed Metropolitan's Auditor to serve as the interim Ethics Officer.

In February 2018, Wilmer Hale provided a written report and made a presentation to the Executive Committee. The scope of the review by Wilmer Hale included the role of the Ethics Office, policies and procedures relating to ethics investigations, the reporting structure and independence of the Ethics Officer, and compliance with SB 60.

Subsequent to receipt of the Wilmer Hale report, Olson Hagel was engaged to assist Metropolitan with the implementation of any changes in policy or procedures authorized by the Board, including preparation of appropriate amendments to Metropolitan's Administrative Code.

Olson Hagel made an initial presentation of their recommendations to the Audit and Ethics Committee in May 2018. At the July 2018 Audit and Ethics Committee meeting, Directors requested that Human Resources

initiate a review and, to the extent necessary, revision of the job description for the Ethics Officer and that the proposals for the reporting structure of the Ethics Officer be brought to the Board for consideration to facilitate initiation of the recruitment for a new Ethics Officer.

The Ethics Officer currently is one of four Officers of Metropolitan that report directly to the Board and serve at the pleasure of the Board (Administrative Code Section 6740). The Wilmer Hale report provided history of SB 60 and the initial decision regarding the reporting structure. It concluded:

*"SB 60's broad language, and the legislative history reflecting concerns about the political influence of both Directors and officers, suggest that SB 60 simply requires that the Ethics Officer has the freedom to reach her own conclusions—especially with respect to investigations—without interference by Directors or officers. This freedom can be maintained through procedures that insulate the Ethics Office's investigative function even if the Ethics Officer reports to Directors or officers."*

The report noted that in public agencies and corporations, there are a variety of reporting structures for ethics officers or chief compliance officers, including reporting to: (1) the Chief Executive Officer, (2) the General Counsel, (3) the Board of Directors or a Board Committee, or (4) the Chief Audit Executive or Risk Officer. Wilmer Hale recommended that the Ethics Officer report to the General Counsel, with dotted-line reporting to the Board's Audit and Ethics Committee.

## **Discussion**

In its May 2018 report to the Audit and Ethics Special Committee, Olson Hagel discussed at length the SB 60 requirements that the Board "shall establish and operate an Office of Ethics" and that the Office "shall operate as an independent entity that is not subject to political influence." In Olson Hagel's view, these requirements must be read together and that the requirement that the Ethics Office operate independently does not equate to a requirement that the Office be separate and apart from Metropolitan, or that it operate autonomously from any oversight by the Board of Directors. In Olson Hagel's view, the SB 60 requirements can be harmonized by the adoption of a reporting structure that ensures that the Ethics Office has the ability to fulfill its responsibilities in an unbiased manner that is free of conditions that would threaten its independence or objectivity while still remaining ultimately accountable to the Board of Directors.

Olson Hagel further expressed the view that enhancing the oversight role of the Audit and Ethics Committee with respect to the Ethics Office, with a direct line of communication from the Office to the Committee and its Chair, is supportive of the independence of the Office in the fulfillment of its mission, in that it is consistent with the Committee's oversight role with respect to the Office of the Auditor. While direct oversight of the Ethics Office is to rest with the Audit and Ethics Committee and its Chair, Olson Hagel recommends that the Board of Directors retain ultimate responsibility for the hiring, evaluation, compensation, and termination of the Ethics Officer. Such hiring, evaluation, compensation, and any termination shall be done after review and recommendation of the Audit and Ethics Committee. In addition, the full Board of Directors will be responsible for approval of any amendments to the Administrative Code.

The Ethics Office would report monthly to the Audit and Ethics Committee relative to investigations, quarterly relative to contracts with outside consultants, annually with respect to the Ethics Office business plan, and biennially relative to the Ethics Office budget. In addition, the Audit and Ethics Committee and its Chair would resolve any issues relative to the independence of the Ethics Office or issues relative to the Ethics Office working collaboratively with the General Manager, General Counsel, and General Auditor.

Olson Hagel also recommends that the Audit and Ethics Committee be made a standing committee of the Board of Directors. In addition, appropriate changes to the Administrative Code should reflect the reporting structure and responsibilities of the Audit and Ethics Committee consistent with this recommendation.

In their May 2018 presentation, Olson Hagel additionally elaborated upon the need for a collaborative relationship between the Ethics Office and the Board, General Manager, and General Counsel in order for the Ethics Office to effectively fulfill its mission. To provide assurance to the Board that this requisite combination of a collaborative relationship and independence has been developed and is being maintained (or to provide visibility to the Board if it is not), Olson Hagel has recommended that the reporting relationship include a requirement that the Ethics

Officer must confirm to the Board of Directors annually, the organizational independence of the Ethics Office and the existence of the requisite collaborative relationship.

Olson Hagel's recommendation in this area differs from Wilmer Hale's initial recommendation regarding the organizational placement of the Ethics Office, which was to have the Office report to the General Counsel. Olson Hagel believes that this alternative organizational placement could compromise the ability of the Office to fulfill its role and mission by creating the potential for the appearance of executive control over the exercise of the Office's role and responsibilities.

The attached Reporting Structure provides a succinct summary of the above Discussion (**Attachment 1**).

#### **Recommendation:**

Olson Hagel's recommendation is that the Ethics Office should report to the Audit and Ethics Committee with the understanding that the ultimate decision to hire, evaluate, and terminate the Ethics Officer shall rest with the Board of Directors after recommendation by the Audit and Ethics Committee. In addition, the Ethics Officer shall certify annually directly to the Board of Directors whether the Ethics Office is able to operate independently without political influence and whether it has operated in a collaborative way with the General Manager, General Counsel, and General Auditor. Finally, the Board would approve any changes to the Administrative Code recommended by the Ethics Office and Audit and Ethics Committee.

Olson Hagel further recommends that to enhance the effectiveness of the Committee's oversight role with respect to the Ethics Office, the Committee should be made a standing Committee of the Board.

#### **Policy**

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Section 126.7 Metropolitan Act Establishment of Office of Ethics

#### **California Environmental Quality Act (CEQA)**

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##### **CEQA determination for Option #1:**

The proposed action is not defined as a project under CEQA (Public Resources Code Section 21065, State CEQA Guidelines Section 15378) because the proposed action will not cause either a direct physical change in the environment or a reasonably foreseeable indirect physical change in the environment and involves continuing administrative activities (Section 15378(b)(2) of the State CEQA Guidelines). In addition, the proposed action is not defined as a project under CEQA because it involves other government activities, which do not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment (Section 15378(b)(4) of the State CEQA Guidelines).

The CEQA determination is: Determine that the proposed action is not defined as a project under Public Resources Code Section 21065 and Sections 15378(b)(2) and 15378(b)(4) of the State CEQA Guidelines.

##### **CEQA determination for Option #2:**

None

#### **Board Options**

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##### **Option #1**

Adopt the CEQA determination that the proposed action is not defined as a project, and

Direct that the reporting relationship of the Ethics Office to the Board prospectively shall be done through the Audit and Ethics Committee.

**Fiscal Impact:** None

##### **Option #2**

No CEQA required

Do not change the current reporting structure for the Ethics Officer.

**Fiscal Impact:** None

**Staff Recommendation**

Adopt Option #1, with appropriate implementing revisions to the Administrative Code and policy to be developed by Olson Hagel and considered for adoption by the Audit and Ethics Committee and the Board at a later date.

A handwritten signature in black ink, appearing to read "Jeffrey Kightlinger".

Jeffrey Kightlinger  
General Manager

9/5/2018  
Date

**Attachment 1 – Reporting Structure**

Ref# e12657786

## ETHICS OFFICE REPORTING STRUCTURE

