



## **Internal Audit Report for August 2018**

### **Summary**

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Two reports were issued during the month:

- 1. Quarterly Board Reports for period ending March 31, 2018**
- 2. Weymouth (Weymouth) Oxidation Retrofit Program**

### **Discussion Section**

This report highlights the significant activities of the Internal Audit Department during August 2018. 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.

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### **Quarterly Board Reports for period ending March 31, 2018**

We reviewed the Report of Professional Services Agreements (Professional Services Report) and the Report of Contracts for Equipment, Materials, Supplies, and Routine Services of \$250,000 or Above Contracts (Contracts Report) for the Third Quarter of fiscal year 2017/18, issued by the Chief Administrative Office. The purpose of this review is to gain reasonable assurance that information included in these reports is accurate, complete, timely, and in compliance with the Metropolitan Water District Administrative Code.

#### **PROFESSIONAL SERVICES AGREEMENTS REPORT**

##### **Background**

Administrative Code Section 2720(e)(2) requires that the General Manager report to the Organization, Personnel and Technology Committee on the employment of any professional and technical consultant, the extension of any professional and technical consulting agreement, and on the Exercise of Authority under Sections 8121(c) and 8122(h) during the preceding calendar quarter.

The Administrative Code also requires the Professional Services Report to indicate when a consultant is a former Metropolitan employee. Administrative Code Sections 2721-2723 require the General Counsel, General Auditor and Ethics Officer to report quarterly to their respective committee concerning any expert or professional service agreements executed pursuant to their authority under the Administrative Code.

The Professional Services Report is prepared on a quarterly and annual basis to comply with these Administrative Code requirements and identify those contracts administered by the General Manager, General Counsel, General Auditor, and Ethics Officer.

During the quarter ending March 2018, the Professional Services Report disclosed that \$38.8 million was paid for consulting and professional services. We compared the amounts expended on professional services during this quarter against the prior fiscal year's third quarter and noted a decrease of \$31.6 million. The Electric & Gas Industries Association (EGIA) Agreement 129415, under the Water Resource Management Group for Metropolitan's Regional Conservation Rebate Program, totaled \$45.3 million for the prior fiscal year's third quarter. This agreement was closed and replaced with EGIA agreement 168959, totaling \$14.7 million. Changes in the EGIA agreements accounted for \$30.6 million of the total decrease in expenditures.

It should be noted that totals reported under the General Counsel's authority exclude payments related to the San Diego County Water Authority litigation, which is accounted for under the Self-Insurance Retention Fund.

For the quarter ending March 2018, 40 of 354 agreements were sole-source agreements totaling \$3.5 million. This represents 9% of total fiscal year-to-date expenditures for fiscal year 2017/18. We also noted that 80 of 354 agreements were small purchases of less than \$24,999, totaling \$732,148. See tables below for details:

| Fiscal 2017/18<br>Year-to-Date Q3 | General Manager | General Counsel | General Auditor | Ethics<br>Officer |
|-----------------------------------|-----------------|-----------------|-----------------|-------------------|
| Contract Expenditures             | \$38,455,358    | \$916,189*      | \$324,715       | \$19,893          |
| Active Agreements                 | 328             | 105             | 0               | 3                 |
| Agreements Terminated             | 22              | 1               | 1               | 0                 |

\* For agreements with transactions during the current fiscal year.

| Govt. Agencies | RFP          | RFQ          | Small Purchases | Sole Source | Total**      |
|----------------|--------------|--------------|-----------------|-------------|--------------|
| \$235,562      | \$22,056,298 | \$12,232,979 | \$732,148       | \$3,542,979 | \$38,799,966 |
| 11             | 37           | 186          | 80              | 40          | 354          |
| 1%             | 56%          | 32%          | 2%              | 9%          | 100%         |

\*\*Total does not include General Counsel's Expenditures

### **Testing Procedures Performed**

Our procedures included a cursory review of the reasonableness of the professional service expenditures and analysis of consultants with multiple active agreements, to determine whether an agreement was split into smaller contract amounts to circumvent established approval limits. We also evaluated whether statistics in the Professional Services Report were adequately supported, and assessed the timeliness of board reporting.

### **Testing results**

Our review did not reveal any agreements that appeared to be unreasonable or split to override established approval limits. In addition, our review did not reveal any material differences between the reported amounts and supporting documentation. Finally, we noted the Professional Services Reports for the quarter ending was issued to the Board on June 12, 2018.

### **CONTRACTS FOR EQUIPMENT, MATERIALS, SUPPLIES, AND ROUTINE SERVICES OF \$250,000 OR ABOVE REPORT**

### **Background**

Administrative Code Section 2720(e)(2) requires that the General Manager report to the Organization, Personnel and Technology Committee on the execution of any contract authorized under Section 8122(g) – Contracts for Equipment, Materials, Supplies and Routine Services. This code section states that the General Manager may execute contracts for the purchase of materials, supplies, and other consumable items such as fuels and water treatment chemicals generally identified in the budget regardless of dollar value, provided that sufficient funds are available within the adopted budget for such purchases.

The Contracts Report is prepared on a quarterly basis to report on contracts that comply with these Administrative Code requirements. During the quarter ending March 31, 2018, the Contracts Report disclosed nineteen contracts that fit these criteria. We noted the total maximum amount payable for these contracts was \$17.9 million. Eleven of these nineteen contracts were awarded as a result of competitive bidding; four were through cooperative agreement competitively bid by another public agency; whereas the remaining four were sole sourced.

### **Testing Procedures Performed**

Our procedures included a cursory review of the reasonableness of expenditures. We also verified that all contracts of \$250,000 or more for specified items were included in the Contracts Report and adequately supported. Finally, we assessed the timeliness of board reporting.

### **Testing results**

Our review did not reveal any discrepancies between contracts and amounts shown in the Contracts Report, and supporting documentation. We also noted that the policies and procedures for competitive bidding, cooperative agreements, and sole source agreements are in place. Finally, we noted for quarter ending March 31, 2018 Contracts Reports was issued to the Board on June 12, 2018.

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## **Weymouth (Weymouth) Oxidation Retrofit Program**

### **Background**

The Audit Department has completed a review of the accounting and administrative controls over the Weymouth (Weymouth) Oxidation Retrofit Program (ORP) as of January 31, 2018.

Our review consisted of evaluating administration and reporting practices, extra work orders, contract retention, and project closeout. In addition, we evaluated the validity and accuracy of contractor estimates and invoices for assurance that the amounts billed were properly calculated and adequately supported.

The addition of ozone as the primary disinfectant at each of Metropolitan's five treatment plants substantially reduces the formation of disinfection by-products (DBP) to comply with the U.S. Environmental Protection Agency's Disinfectant/Disinfection By-Products (D/DBP) Rule. The use of ozone also provides overall water quality benefits, enhances Metropolitan's ability to treat water with varying source-water quality, and provides critical operational flexibility to meet treatment challenges resulting from periodic water supply events, such as drought. Finally, the use of ozone allows Metropolitan to eliminate blend restrictions of State Water Project (SWP) and Colorado River Aqueduct (CRA) supplies. Weymouth is the last of Metropolitan's treatment plants to incorporate ozone as the primary disinfectant.

Weymouth was placed into service in 1941 and treats water from the CRA and SWP. Located in the City of La Verne, it was originally sized at a capacity of 100 million gallons per day (mgd) and was expanded twice to its current capacity of 520 mgd. Due to its size and complexity, the Weymouth ORP was completed in phases, using multiple construction and procurement contracts.

From March 1, 2016 through January 31, 2018, Weymouth ORP expenditures were \$29.6 million and consisted mainly of construction contract payments totaling \$12.8 million, professional consulting services totaling \$1.7 million, and Metropolitan labor and administrative overhead of \$13.4 million. The appropriated amount for the entire Weymouth ORP was \$251.5 million. As of January 31, 2018, the total projected cost was \$226.7 million.

## **Opinion**

In our opinion, the accounting and administrative procedures over the Weymouth ORP 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 March 1, 2016 through January 31, 2018.

## **Comments and Recommendations**

### **POLICIES AND PROCEDURES**

Policies and procedures should be established and documented to provide a framework for achieving Metropolitan's goals and objectives. Procedures provide management with guidelines for consistent performance of daily operations, assist management in the training of new employees, and provide a source of reference for experienced personnel.

Our review revealed that the ORP Project Management Plan was not updated to address the addition of Stage 2 to the Ozonation Facilities Project 104459. Stage 2 consists of outfitting two bypass contactors with piping, equipment, instrumentation, and electrical systems to make them fully functional.

Failure to update the Project Management Plan could result in ineffective project execution.

We recommend that management update the Project Management Plan on a timely basis.

### **COMPLIANCE WITH TERMS AND CONDITIONS OF AGREEMENT**

Compliance with contractual requirements is necessary to ensure accurate accounting records, proper supporting detail, and adequate control over the administration of the agreements. Furthermore, compliance with the contracts' terms and conditions also ensures that parties fully discharge their duties and obligations and exercise their legal rights associated with the agreements.

We analyzed a sample of 13 invoices from five consultants who provided professional services to the Weymouth ORP and found the following discrepancies:

#### **Untimely Invoice Submission**

Carollo Engineers, P.C. (Carollo) was engaged to provide engineering services for the Weymouth ORP. The agreement requires Carollo to submit monthly invoices showing both monthly and cumulative costs. On June 21, 2017, Carollo invoiced Metropolitan \$30,766 for charges from Lee & Ro, a sub-consultant, more than two years after the work was performed (invoice #0158718). Metropolitan approved the invoice for payment.

Failure to comply with the terms and conditions of the agreements could result in financial loss to Metropolitan due to erroneous or unauthorized transactions.

We recommend that management take steps to ensure compliance with agreement terms and conditions.

#### Improper Coding of Invoiced Charges

We found discrepancies between amounts billed and amounts charged to Project 104388 (Weymouth Hypochlorite and Sulfuric Acid Feed Facilities) on three invoices from AECOM Technical Services, Inc. (AECOM). The discrepancies may have resulted in project costs being overstated by \$56,328 and, consequently, costs for other capital projects may also have been misstated. The discrepancies are summarized in the table, below.

| Invoice No. | Invoice Date | Invoice Amount | Billed Amount to Projects other than Project 104388 | Billed Amount to Project 104388 | Amount Charged to Project 104388 | Discrepancy between Billed Amount and the Amount Charged to Project 104388 |
|-------------|--------------|----------------|---|---------------------------------|----------------------------------|--|
| 37827631Rev | 11/17/2016   | \$ 42,954      | \$ 42,954   | -                               | \$ 28,929                        | \$ 28,929  |
| 37843314    | 12/1/2016    | 28,766         | 28,766  | -                               | 13,783                           | 13,783   |
| 37866233    | 1/16/2017    | 37,506         | 37,506  | -                               | 13,616                           | 13,616   |
|             | Total        | \$ 109,226     | \$ 109,226  | \$ -                            | \$ 56,328                        | \$ 56,328  |

Failure to record consultant charges accurately could result in misstatement of project costs and inaccurate reporting.

We recommend that management take steps to ensure vendor invoices accurately reflect the work performed prior to approval and payment. We also recommend that management examine all AECOM invoices charged to Project 104388, document any discrepancies noted, and make corrections if necessary.