



Internal Audit Report for August 2019

Summary

Two reports were issued during the month:

- 1. Quarterly Consulting and Services Contracts Review Report for Period Ending March 31, 2019**
- 2. Management Response to Audit Quality Assurance – Self-Assessment Review**

Discussion Section

This report highlights the significant activities of the Internal Audit Department during August 2019. 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.

Quarterly Consulting and Services Contracts Review Report for Period Ending March 31, 2019

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 2018/19, 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

Scope

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.

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 2019, the Professional Services Report disclosed that \$48.6 million was paid for consulting and professional services. 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 2019, 53 of 407 agreements were sole-source agreements totaling \$4.2 million. This represents 9% of total fiscal year-to-date expenditures for fiscal year 2018/19. We also noted that 93 of 407 agreements were small purchases of less than \$24,999, totaling \$708,678. See tables below for detail:

Fiscal 2018/19 Year-to-Date Q3	General Manager	General Counsel	General Auditor	Ethics Officer
Contract Expenditures	\$48,203,038	\$466,206*	\$417,400	\$15,107
Active Agreements	369	114	1	2
Agreements Terminated	35	1	-	-

* For agreements with transactions during the current fiscal year.

Govt. Agencies	RFP	RFQ	Small Purchases	Sole Source	Total**
\$841,359	\$25,506,953	\$17,386,162	\$708,678	\$4,192,393	\$48,635,545
11	47	203	93	53	407
2%	52%	36%	1%	9%	100%

**Total does not include General Counsel's Expenditures

Opinion

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 11, 2019.

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

Scope

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.

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, 2019, the Contracts Report disclosed 17 contracts that fit these criteria. We noted the total maximum amount payable for these contracts was \$20.5 million. Twelve of these seventeen contracts were awarded as a result of competitive bidding, two were cooperative agreements, whereas the remaining three were sole sourced.

Opinion

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 and sole source agreements are in place. Finally, we noted for quarter ending March 31, 2019 Contracts Report was issued to the Board on June 11, 2019.

Management Response to Audit Quality Assurance – Self-Assessment Review

Below are our responses to the recommendations contained in the Audit Quality Assurance – Self Assessment Review.

1. Engagement Work Program

Consideration should be given to adding available tools to the audit teams' resources such as on-line audit libraries and data analytic software. Review of work programs should occur prior to the start of fieldwork. Changes to the work program mid-stream should be adequately documented and traceable within the project files.

Management Response

Audit management is in the process of revising audit workflow to ensure audit programs and adjustments are reviewed and approved prior to initiation of fieldwork. Additionally, management is piloting a program to utilize more advanced features in TeamMate, including on-line audit libraries. The addition of two new staff members, including the Deputy General Auditor, have accelerated this process. We anticipate full implementation of the revised procedures by December 31, 2019. In addition, IT audit staff will be involved in the planning phase for each new audit to ensure data acquisition and analytics are employed to maximum advantage. Finally, we are evaluating software packages for use in data analytics, including IDEA, Alteryx and Arbutus.

2. Documenting Information

Internal audit staff should comply with Department standards. Audit staff should ensure that work is adequately documented with sufficient, reliable information to support engagement results and conclusions.

Management Response

Between June 1, 2018 and August 31, 2019, the entire audit staff completed on-line training courses sponsored by the Institute of Internal Auditors (IIA) on auditing concepts, internal controls, audit evidence and workpaper documentation. Additional department wide training on these and other technical topics, such as fraud and data analytics, will be completed by June 30, 2020. Furthermore, the Department has developed and implemented standardized worksheets to allow for more consistent, efficient and effective documentation of samples collected and tested. Combined with the revised workflows and enhanced procedures, mentioned above, we anticipate general compliance with Department Standards by December 31, 2019.

3. Engagement Supervision

Engagement supervision should be augmented with formal, documented reviews on a timely basis. Specifically:

- Reviews should be documented in the project file when performed.
- Reviews should occur as soon as possible after each major section of a project.
- All workpapers should be reviewed before the final report is submitted to the General Auditor.

Staff members should ensure to communicate with audit management when workpapers are ready for review, including when updates are made after the initial review. Review notes should be addressed within the project file and include actions taken to address comments made.

Management Response

With the revised workflows and enhanced procedures, mentioned above, we anticipate general compliance with Department Standards by December 31, 2019. Additionally, we have revised the audit staff performance evaluation criteria to place more emphasis on compliance with policies and procedures.

4. Audit Time Management

Recommendation

Future Annual Audit Plans should consider establishing more accurate budgets for recurring audits based on past experiences and current risk assessments.

Management Response

The FY 2019/20 Audit plan replaced “placeholder budgets” with estimates tailored to each individual audit. Budgets will be monitored and revised as appropriate, with revisions incorporated into future audit planning.

5. Policies and Procedures

Update Department Policies and Procedures to reflect current IIA *Standards* and practices.

Management Response

Department Policies and Procedures, including the enhanced workflows described above, are being updated to reflect current IIA Standards and will be completed by December 31, 2019. Additionally, Department Policies and Procedures will be reviewed periodically to ensure they more timely reflect changes in IIA Standards.

6. Audit Department Charter (Department Charter)

The Department Charter should be revised to reflect the most recent IIA *Standards*. In making revisions, consideration should be given to the IIA's 2017 model Internal Audit Activity Charter. Revisions should be included in MWD's Administrative Code and formally approved by the Board.

The Department Charter and mandatory elements of the International Professional Practices Framework (IPPF) should be reviewed annually by the Audit and Ethics Committee. The organizational independence of the Internal Audit department should be formally communicated, annually, to the Board.

Management Response

The Department Charter (Charter) is being revised to reflect current IIA Standards. The revised Charter, mandatory elements of the IPPF, and proposals for required changes to MWD's Administrative Code will be presented to the Board by March 31, 2020. Additionally, the Charter and mandatory elements of the IPPF will be reviewed with the Audit and Ethics Committee on an annual basis.

Audit and Ethics Committee Charter

Consider revising the Audit and Ethics Committee Charter to more fully define the committee's role and responsibilities in promoting effective organizational governance. The IIA's Implementation Guide IG1000 provides context for such an action and the IIA's Model Audit Committee Charter provides content suggestions.

Management Response

A proposal to revise the Audit and Ethics Committee Charter is being developed and will be presented to the Board by March 31, 2020.

Code of Ethics

Formally document the review and understanding of the IIA Code of Ethics with department staff. Consider incorporating into the on-boarding process of new staff members.

Management Response

During August 2019, each staff member received a copy of the IIA's Code of Ethics and was asked to confirm in writing that they have read it and understand it. This procedure will be repeated annually and will be incorporated into the on-boarding process for new employees.

7. Continuing Professional Education

To help ensure audit staff members complete the amount and type of CPE they need, staff members should develop an annual training plan. Training plan progress and completion should be monitored and become a component of each staff member's performance evaluation. Audit staff members that do not currently hold a certification or license should be encouraged to obtain one.

Management Response

Non-compliance with CPE standards was noted and considered in conducting FY 2018/19 annual performance reviews. Furthermore, all staff members without certification have been encouraged to obtain one. Finally, beginning in FY 2019/20, each staff member is required to prepare a formal training plan for use in planning and measuring progress toward meeting CPE requirements.