



THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA

Board Report

Office of the General Auditor

• General Auditor's Report for February 2024

Summary

This report highlights significant activities of the Office of the General Auditor for the month ended February 29, 2024.

One report was issued during this period, including five recommendations (see Attachment 1).

Purpose

Informational

Attachments

1. Final Report on Contract & Project Cost Audit: Roesling Nakamura Terada Architects

Detailed Report

Audit & Advisory Services

Twenty-six projects are in progress:

- Twelve audit projects are in the report preparation phase, including three preliminary draft reports/memos that are pending management comment.
- Thirteen projects are in the execution phase, including eight audits and five advisories.
- One audit project is in the planning phase.

Work priority is being given to carry-forward audits.

Final Report Details

1. **Contract & Project Cost Audit: Roesling Nakamura Terada Architects** issued February 28, 2024 (project number 22-2710)
 - Our audit scope included evaluating the accounting and administrative controls over Metropolitan's internal costs and the professional agreement awarded to the consultant.
 - Five total recommendations with the following ratings: two **Priority 1**, two **Priority 2**, and one **Priority 3**.

Follow-Up Audits

We will follow up on 10 audits from prior years. Follow-up audit forms have been submitted to and received from management for seven of these.

Follow-up audit work is in progress for three of the seven audits.

Date of Report: March 12, 2024

Board Report (General Auditor's Report for February 2024)

Other General Auditor Activities

1. FY 2024/25 General Auditor Business Plan

We commenced planning for next fiscal year's audit plan, including project tasks, deliverables, and timeframes.

2. Training

Audit management attended the IIA's 2024 Fraud Conference, which covered artificial intelligence, fraud risk management, fraud trends, and the role of the auditor and fraud.

3. IIA Quality Services

We received a recognition plaque acknowledging our conformance with professional internal auditing standards.



Office of the General Auditor

Contract & Project Cost Audit: Roesling Nakamura Terada Architects

Project Number: 22-2710
February 28, 2024



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Executive Summary

BACKGROUND

Metropolitan provides housing to employees involved in the operation and maintenance of the Colorado River Aqueduct (CRA) to ensure that appropriate staff members are on-site and can respond quickly to emergencies. Towards this goal, Metropolitan refurbished multiple housing units to varying degrees over the years and built new houses under a pilot program.

From 2019 to 2022, the Metropolitan Board authorized the District Housing and Property Improvement Program (Program) across four Metropolitan CRA pumping plants and moved two projects (Eagle and Iron Mountain Villages' kitchens and guest lodges replacement) into the Program. The Board authorized an architect-engineering contract with consultant Roesling Nakamura Terada Architects (RNT) on July 1, 2019, for a contract total of \$1.5 million. The latest contract, including amendments, has increased to approximately \$13.5 million as of this report date. The consultant's scope of work is to conduct a condition assessment for each of the remaining houses, develop a master plan concept to replace the kitchens and guest lodges at Eagle and Iron Mountain Villages, design village enhancements at Hinds, Iron, and Gene Pumping Plants, and provide preliminary design and architectural services in support of the Program.

WHAT WE DID

Our audit scope included evaluating the accounting and administrative controls over Metropolitan's internal costs and the professional agreement awarded to RNT under the Program. Our audit included costs incurred between July 1, 2019 and December 31, 2021.

Our audit objectives were to:

- (1) Determine if the procurement of the consultant contract was properly authorized, processed, and managed.
- (2) Determine if the contract administration (including task orders and deliverables) and reporting processes adhered to Metropolitan's policy and procedures.
- (3) Determine if charges paid to the consultant were authorized, complete, and accurate.
- (4) Determine if project expenditures were correctly recorded, posted, and reported in Metropolitan's accounting system.
- (5) Determine if internal labor costs charged to projects were reasonable, accurate, and approved.

WHAT WE CONCLUDED

- (1) The procurement of the consultant contract was properly authorized, processed, and managed.
- (2) Contract administration and reporting processes adhered to Metropolitan policy and procedures; however, certain areas of task order administration should be improved.
- (3) Charges paid to the consultant were authorized, complete, and accurate; however, contractual compliance monitoring should be enhanced.
- (4) Project accounting improvements should be implemented to ensure certain project expenditures are correctly recorded, posted, and reported in Metropolitan's accounting system.
- (5) Internal labor costs charged to projects were reasonable, accurate, and approved.

WHAT WE RECOMMEND

We recommended Metropolitan: (1) reclass approximately \$2 million from an asset account to the O&M expense account; (2) ensure future project costs are expensed during the preliminary stage and ensure project managers and approvers exclude design projects and studies that are considered preliminary; (3) ensure the consultant complies with the terms and conditions of the agreement; (4) request supporting calculations for proposed rates and document rate analysis and negotiation; and (5) update Operating Policy F-07 to include missing key criteria for evaluation of capitalization vs. expense.

NUMBER OF RECOMMENDATIONS



PRIORITY 1
Response time:
Immediate



PRIORITY 2
Response time:
Within 90 days



PRIORITY 3
Response time:
Within 180 days



THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA

Date: February 28, 2024
To: Executive Committee
From: Scott Suzuki, CPA, CIA, CISA, CFE, General Auditor
Subject: Contract & Project Cost Audit: Roesling Nakamura Terada Architects
(Project Number 22-2710)

This report presents the results of our audit of the Roesling Nakamura Terada Architects contract and certain District Housing & Property Improvement Program costs.

Results, including our observations and recommendations, follow this letter. Supplemental information, including our scope and objectives, are included in Appendix A. Appendix B includes a description of our new recommendation priority rating system. Finally, management's response to our audit is now included in Appendix C.

We appreciate the cooperation and courtesies provided by the Office of the General Manager, former Real Property Group (now under Water System Operations Group), Engineering Services Group, and Finance Group.

The results in this report will be summarized for inclusion in a status report to the Board. If you have any questions regarding our audit, please do not hesitate to contact me directly at 213.217.6528 or Deputy General Auditor Kathryn Andrus at 213.217.7213.

Attachment

cc: Board of Directors
General Manager
General Counsel
Ethics Officer
Office of the General Manager Distribution
Assistant General Managers
Finance & Administration Distribution
Operations Distribution
Water & Technical Resources Distribution
External Auditor

RESULTS

RECOGNITION

Positive aspects observed during our audit include:

- The procurement, which includes solicitation, selection, and awarding of the Roesling Nakamura Terada Architects (RNT) consultant contract (Agreement), was properly reviewed and approved.
- Metropolitan utilized PlanetBids for contract procurement and storage of comprehensive documents.
- Insurance certificates for the consultant were current and kept in the system.
- Monthly project reports were properly reviewed.
- Processes ensured the total project cost did not exceed the contract funding.

RESULTS OVERVIEW

	OBSERVATION	RISK	RECOMMENDATION	MANAGEMENT AGREEMENT
PRIORITY 1				
1	Certain fixed asset costs were capitalized and should have been expensed.	Overstated assets Understated expenses	Reclass capitalized costs to expenses. Ensure project costs in the preliminary stage are expensed.	Agree Agree
PRIORITY 2				
2	Certain invoicing requirements were not complied with.	Overpayments Unauthorized charges Interest charges from late payments	Ensure contract terms and conditions are complied with and conduct period reviews. Ensure task orders are timely authorized and amended.	Agree
3	Management of overhead and profit could be improved to reduce project costs.	Not obtaining the most advantageous best value pricing	Request support for proposed rates. Document rate analysis and negotiation.	Agree
PRIORITY 3				
4	Accounting policy and procedures for capitalization and expensing project costs were not current.	Inaccurate financial reporting	Update accounting policies and procedures.	Agree



OBSERVATIONS & RECOMMENDATIONS

1 Fixed Asset Cost Classification

Certain fixed asset costs were capitalized and should have been expensed.

We reviewed three task orders issued to RNT for Project No. 105076 included under the District Housing and Property Improvement Program (see Appendix A: Additional Information/Background for other projects under this Program). Under Project No. 105076, task orders were issued for:

- (1) The assessment of employee housing and preparation of conceptual design drawings and reports for improvements or replacement plans for up to 78 existing homes.
- (2) The study of community and site improvements and shared facilities, including shared kitchens and lodging facilities across the four pumping plant locations or "Villages."
- (3) Final design for four new prototype housing units to either replace existing housing or to be sited on existing vacant lots.

Although the former Real Property Group (the team in Real Property Group that manages the Program has since moved under the Water System Operations Group as part of recent organizational changes) was in compliance with Metropolitan's Operating Policy F-07 (Capitalization & Retirement of Plant Assets) for accounting for project costs, two important criteria for fixed asset capitalization were not included in the policy. The inclusion of these two criteria would ensure compliance with authoritative literature on self-constructed assets. Specific accounting guidance applicable to this observation can be found in Appendix A: Additional Information for Observation No. 1. In Observation No. 4, we recommend an update to Operating Policy F-07 because the industry capitalization criteria referenced in Appendix A are not currently reflected in the policy.

Specifically, based on the task order descriptions, the project was in the preliminary stage (not to be confused with preliminary design, which can be capitalized depending on if two criteria are met) and could not be considered probable and directly identifiable with a specific asset. As a result, we determined that approximately \$2,075,209 charged to this project should be expensed rather than capitalized.

Subsequent to and as a result of our audit, the Finance Group has made the reclassification of the \$2,075,209 to reflect the expense.



Priority 1

Improper capitalization of costs can overstate assets and understate current-period expenses.

Recommendation 1

We recommend the Water System Operations Group work with the Finance Group to reclass Project No. 105076 costs of \$2,075,209 from Account 12155 to the Operations and Maintenance expense account.

Management Response

Agree. Costs were transferred to O&M and completed in June 2023.

Recommendation 2

We recommend the Engineering Service Group:

- (1) Ensure design/engineering costs and associated internal costs during the preliminary stage are expensed rather than capitalized.
- (2) Ensure project managers and approvers follow the revised capitalization policy in Recommendation No. 5 to capitalize costs only if the costs are directly identifiable with a specific asset and the costs are incurred after the asset is considered probable.

Management Response

Agree. (1) Engineering Services Group is already evaluating and assessing the design/engineering costs for projects during the initial stage regarding capitalization versus operations and maintenance funds. (2) All Project Managers and Approvers will follow the revised capitalization policy within 30 days after the policy is updated by Finance, as outlined in Recommendation No. 5.

The estimated implementation date is in November 2024.

2 Contractual Compliance

Certain invoicing requirements were not complied with.

Review and approval controls are designed to verify the accuracy of billings for services, provide assurance as to the propriety of transactions, confirm compliance with contractual terms and conditions, and ensure that follow-up procedures for exceptions exist. Furthermore, compliance with contractual requirements is necessary to ensure accurate accounting records, proper supporting details, and adequate control over the administration of the Agreement.

We statistically selected 41 invoices (or \$1,201,369.81) for detailed testing.

- For 21 of 41 (51%) invoices, no timesheets were submitted by the consultant as required by the Agreement. The consultant was not requested to submit any timesheets for review.



- For 16 of 41 (39%) invoices, RNT's labor charges did not have a description of work performed as required by the Agreement.
- For six of 41 (15%) invoices, no sub-consultant invoice was attached to the submitted invoice as required by the Agreement.
- For five of 41 (12%) invoices, no supporting documents for reimbursable expenses and travel were attached to the invoices as required by the Agreement.
- For four of 41 (10%) invoices, reimbursable expenses were not itemized as required by the Agreement.
- For three of 41 (7%) invoices, the sub-consultant's invoices did not follow the authorized task order type. Specifically, the sub-consultant billed as a percentage of completion, but the task order was for a not-to-exceed time and material type.

We also reviewed Task Order (TO) approvals and deliverables.

- Deliverables for TO #4 and #5 were issued on 10/13/2021, nearly three and a half months after the TO ending dates of 6/30/2021.
- Seven of the 41 invoices (17%) related to the TOs have service dates after the original TO end date. The Agreement Administrator executed and provided amendments extending the end dates for TO #4 and TO #5 during our audit.

Priority 2

Failure to comply with the terms and conditions of the agreements could result in overpayment, unauthorized charges, or interest charges from late payments.

Recommendation 3

We recommend the Water System Operations Group Agreement Administrator and Project Manager:

- (1) Ensure the consultant complies with the terms and conditions of the Agreement and conduct periodic reviews to ensure compliance.
- (2) Ensure task orders are timely authorized and amended as needed.
- (3) Periodically review timesheets and other supporting documents to ensure accurate billing on the not-to-exceed task orders.



Management Response

Agree. Agreement Administrators (AA) & Project Managers (PM) throughout the District, within all Groups, should enforce the terms and conditions of the agreement. AAs and PMs will periodically request timesheets and other supporting documents related to the agreement and individual task orders and include written documentation within the project files validating completion of the review. Implementation within 30 days from the issuance of this audit report.

3 Overhead & Profit Rates

Management of overhead and profit could be improved to reduce project costs.

Metropolitan paid the consultant in accordance with the agreed-upon burdened labor rates; however, the proposed overhead rate of one of the sub-consultants was 15% higher than the supported calculations provided by the sub-consultant.

Additionally, another sub-consultant proposed profit rates from 10% to 52% based on various labor categories.

In general, the profit rate should be a fixed fee applied to all direct labor. We were advised that the consultant and its sub-consultants submitted their proposed burdened rates as part of the Request for Qualifications (RFQ) process but the cost was not a scoring criterion when the proposals were evaluated. Furthermore, these rates were not negotiated when awarding the contract and issuing task orders.

A cost analysis looks at the individual elements of the price, such as labor rates, material, overhead, and profit, to determine reasonableness. While overhead or indirect rates can be verified and found reasonable by looking at industry standards, and labor hours can be assessed by technical or engineering staff, profit percentage can be negotiated in most cases. The winning bids should submit supporting calculations on the proposed overhead and profit rate. Furthermore, the burdened rate should be negotiated when awarding the Agreement and task orders.

Priority 2

Failing to review and negotiate contractor rates may lead to Metropolitan not obtaining the most advantageous best value pricing.

Recommendation 4

We recommend the Water System Operations Group:

- (1) Request supporting calculations for proposed overhead and profit rates for contract amendments and as part of contract awards.
- (2) Prepare documentation showing burdened rates were reviewed and negotiated for best value as part of the contract award process and cost analysis completed on a case-by-case basis.



These practices should be applied to contracts in other Metropolitan groups.

Management Response

Agree. All Groups within the District will request supporting calculations for the proposed overhead and profit rates. Cost analysis for the overhead and profit rates will only be performed on a case-by-case basis, when justified by scale, market analysis or other possible value. Documentation will be prepared and filed within the project files validating that the final burdened rates were negotiated in good faith effort that provide the best contract value and are competitive to the industry standards. Implementation within 30 days from the issuance of this audit report.

4 Accounting Policy & Procedures

Accounting policy and procedures for capitalization and expensing project costs were not current.

Metropolitan's Operating Policy F-07 (Capitalization & Retirement of Plant Assets) establishes a policy governing the capitalization and retirement of plant assets and was last revised in 2009. Operating Policy F-07 cites GASB (Government Accounting Standards Board) No. 34 and the GFOA's (Government Finance Officers Association) Accounting for Capital Assets (Guide). However, two critical criteria for capitalizing capital assets in the Guide were not included in Operating Policy F-07.

Priority 3

Outdated accounting policies and procedures can result in inaccurate financial reporting.

Recommendation 5

We recommend the Finance Group update Operating Policy F-07 to state a cost is capitalized only if (1) it is directly identifiable with a specific asset and (2) incurred after the acquisition of the related asset has come to be considered probable.

Management Response

Agree. Finance will work on incorporating language to clearly specify capitalization requirements by GASB, with an estimated implementation date of October 2024.

Updates to Operating Policies must first be coordinated through the technical writing team. Then the changes undergo multiple phases of review from stakeholders throughout the district, group managers and executive management, and often times the bargaining unit, thus the extended timeline.

EVALUATION OF MANAGEMENT'S RESPONSE

Internal Audit considers management's comments responsive to our recommendations, and their planned actions should resolve the conditions identified in the report.



APPENDIX A: SUPPLEMENTAL INFORMATION

ADDITIONAL INFORMATION

Background

Currently, the Program has three projects: (1) Project No. 105076 - District Housing Property Assessments, (2) Project No. 105077 - Employee Village Enhancements Master Planning, and (3) Project No. 105213 - CRA Kitchen and Lodging Facilities Improvements.

Observation No. 1

Generally Accepted Accounting Principles (GAAP), including Governmental Accounting Standards Board (GASB) No. 34 and Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 360, both require that property, plant, and equipment are reported at historical cost and are commonly adjusted subsequently for amortization, depreciation, and impairment. Construction-in-progress is generally capitalized as an asset but is not depreciable. While GASB No. 34 does not give detailed direction to capitalize construction-in-progress, other authoritative literature gives more in-depth guidance on this subject.

The Government Finance Officers Association's "Accounting for Capital Assets, A Guide for State and Local Governments," Chapter 4, Capitalizable Costs, states that a cost should be capitalized only (1) if it is directly identifiable with a specific asset, and (2) if incurred after the acquisition of the related asset has come to be considered probable (likely to occur).

Additionally, PricewaterhouseCoopers' "Accounting and Financial Reporting Guide for Property, Plant, Equipment and Other Assets" (published June 2020), based on FASB Accounting Standards Codification (ASC) on fixed assets, states that when determining which costs should be capitalized for self-constructed assets, it is important to distinguish between those costs that are "necessarily incurred" and those that the reporting entity could have avoided. To better distinguish what cost should be capitalized versus expensed, this guide identifies four stages during which costs may be incurred related to long-lived assets: the preliminary stage, the pre-acquisition stage, the construction stage, and the in-service stage.

In assessing probability, the reporting entity should consider whether (1) management, having the requisite authority, has implicitly or explicitly authorized, and committed to funding the acquisition or construction of a specific asset, (2) the financial resources available are consistent with such authorization, and (3) the ability exists to meet the necessary local and other governmental regulations.

During the preliminary stage (different from preliminary design), a project is not considered probable to be constructed. At this stage, activities are performed exploring the opportunities for the acquisition or construction of property, plant, and equipment, and a reporting entity may conduct feasibility studies and other activities related to asset selection. The guide states that costs, including surveying, zoning, consulting fees, feasibility studies, travel expenses, engineering studies, design layouts, procurement, and related salaries, are to be expensed (not capitalized) during the preliminary stage.



SCOPE & OBJECTIVES

Our audit scope included evaluating the accounting and administrative controls over Metropolitan's internal costs and the professional Agreement awarded to RNT under the Program. Our audit included costs incurred between July 1, 2019 and December 31, 2021.

Our audit objectives were to:

- (1) Determine if the procurement of the consultant contract was properly authorized, processed, and managed.
- (2) Determine if the contract administration (including task orders and deliverables) and reporting processes adhered to Metropolitan's policy and procedures.
- (3) Determine if the charges paid to the consultant were authorized, complete, and accurate.
- (4) Determine if project expenditures were correctly recorded, posted, and reported in Metropolitan's accounting system.
- (5) Determine if internal labor costs charged to projects were reasonable, accurate, and approved.

EXCLUSIONS

Our audit scope did not include (1) project costs incurred under the Desert Housing Program (predecessor housing program), (2) other internal costs, including meals, lodging, mileage, etc., nor (3) the efficiency or performance of the District Housing and Property Improvement Program.

PRIOR AUDIT COVERAGE

We have completed an audit report with a similar scope: Desert Housing Renovation Program, Report No. 18-2710 issued on September 18, 2018.

AUTHORITY

We performed this audit in accordance with the FY 2021/22 Audit Plan presented to the former Audit & Ethics Committee.

AUDIT TEAM

Kathryn Andrus, CPA, Deputy General Auditor
Chris Gutierrez, CPA, CIA, Program Manager - Audit
Andrew H. Lin, CPA, CIA, CIGA, Principal Auditor



PROFESSIONAL INTERNAL AUDIT STANDARDS

Our audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing issued by the International Internal Audit Standards Board.

FOLLOW-UP AUDITS

The Office of the General Auditor has implemented a new follow-up process to ensure management has effectively implemented corrective action related to our recommendations. Management is required to report recommendation implementation status to our office within six months following the issuance of this report and a first follow-up audit will occur shortly thereafter. All audit recommendations are expected to be implemented within a year of this report and if necessary, a second follow-up audit will occur approximately six months after issuance of the first follow-up audit report. Any audit recommendations not implemented after the second follow-up audit will be shared with the Board/Audit Subcommittee of the Executive Committee at its next scheduled meeting.

INTERNAL CONTROL SYSTEM

An internal control system is a continuously operating and integrated component of Metropolitan's operations. Internal controls are implemented by Metropolitan management and seek to provide reasonable (not absolute) assurance that the district's business objectives will be achieved. However, limitations are inherent in any internal control system no matter how well designed, implemented, or operated. Because of these limitations, errors or irregularities may occur and may not be detected. Specific examples of limitations include but are not limited to, poor judgment, carelessness, management override, or collusion. Accordingly, our audit would not necessarily identify all internal control weaknesses or resultant conditions affecting operations, reporting, or compliance. Additionally, our audit covers a point in time and may not be representative of a future period due to changes within Metropolitan and/or external changes impacting the district.

METROPOLITAN'S RESPONSIBILITY FOR INTERNAL CONTROL

It is important to note that Metropolitan management is responsible for designing, implementing, and operating a system of internal control. The objectives of internal controls are to provide reasonable assurance as to the reliability and integrity of information; compliance with policies, plans, procedures, laws, and regulations; the safeguarding of assets; the economic and efficient use of resources; and the accomplishment of established goals and objectives. In fulfilling this responsibility, management judgment is required to assess the expected benefits and related costs of internal control policy and procedures and to assess whether those policies and procedures can be expected to achieve Metropolitan's operational, reporting, and compliance objectives.



APPENDIX B: PRIORITY RATING DEFINITIONS

The Office of the General Auditor utilizes a priority rating system to provide management a measure of urgency in addressing the identified conditions and associated risks. We assess the significance of each observation identified during the audit using professional judgment and assign priority ratings to each recommendation using the criteria listed below. Factors taken into consideration in assessing the priority include the likelihood of a negative impact if not addressed, the significance of the potential impact, and how quickly a negative impact could occur.

PRIORITY			
Definition	Observation is <i>serious</i> enough to warrant <i>immediate</i> corrective action. The condition may represent a serious financial, operational, or compliance risk. A priority 1 recommendation may result from a key control(s) being absent, not adequately designed, or not operating effectively.	Observation is of a <i>significant</i> nature and warrants <i>prompt</i> corrective action. It may represent a moderate financial, operational, or compliance risk. A priority 2 recommendation may result from a process or less critical control(s) not being adequate in design and/or not operating effectively on a consistent basis.	Observation involves an internal control issue or compliance lapse that can be corrected in the <i>timely</i> course of normal business. A priority 3 recommendation may result from a process or control that requires enhancement to better support Metropolitan’s objectives and manage risk.
Response Time	Immediate	Within 90 Days of report issuance	Within 180 Days of report issuance



APPENDIX C: MANAGEMENT'S RESPONSE



THE METROPOLITAN WATER DISTRICT
OF SOUTHERN CALIFORNIA

Date: February 21, 2024
To: Scott Suzuki, General Auditor
From: Adel Hagekhalil, General Manager
Subject: Management Response to Audit Number 22-2710

Please find below the management response to the Roesling Nakamura Terada Architects Contract & Project Cost Audit, revised with clarifications based on your meeting with staff leads from my team. I appreciate the opportunity you offered for these clarifications. Thank you for your partnership in strengthening Metropolitan's systems, controls and capacity. I look forward to working with you throughout the implementation of your recommendations. Please do not hesitate to contact me or my chief of staff Mohsen Mortada if you would like to discuss our response or any other matters.



**Contract & Project Cost Audit: Roesling Nakamura Terada Architects
Project Number 22-2710
Management Response**

OBSERVATION 1		Fixed Asset Cost Allocation
		Certain fixed asset costs were capitalized and should have been expensed.
RECOMMENDATION 1		We recommend the Water System Operations Group work with the Finance Group to reclass Project No. 105076 costs of \$2,075,209 from Account 12155 to the Operation and Maintenance expense account.
PRIORITY 1		
X	AGREE	MANAGEMENT ACTION PLAN
		ESTIMATED IMPLEMENTATION
	PARTIALLY AGREE	EXPLANATION
	DO NOT AGREE	
RECOMMENDATION 2		We recommend the Engineering Service Group:
PRIORITY 1		(1) Ensure design/engineering costs and associated internal costs during the preliminary stage are expensed rather than capitalized. (2) Ensure project managers and approvers follow the revised capitalization policy in Recommendation No. 5 to capitalize costs only if the costs are directly identifiable with a specific asset and the costs are incurred after the asset is considered probable.
X	AGREE	MANAGEMENT ACTION PLAN
		ESTIMATED IMPLEMENTATION
	PARTIALLY AGREE	EXPLANATION
	DO NOT AGREE	



OBSERVATION 2		Contractual Compliance
		Certain contractual terms were not complied with by the consultant.
RECOMMENDATION 3		We recommend the Water System Operations Group Agreement Administrator and Project Manager: (1) Ensure the consultant complies with the terms and conditions of the Agreement and conduct periodic reviews to ensure compliance. (2) Ensure task orders are timely authorized and amended as needed. (3) Periodically review timesheets and other supporting documents to ensure accurate billing on the not-to-exceed task orders.
PRIORITY 2		
X	AGREE	MANAGEMENT ACTION PLAN Agreement Administrators (AA) & Project Managers (PM) throughout the District, within all Groups, should enforce the terms and conditions of the agreement. AAs and PMs will periodically request timesheets and other supporting documents related to the agreement and individual task orders and include written documentation within the project files validating completion of the review. Implementation within 30 days from the issuance of this audit report.
		ESTIMATED IMPLEMENTATION March 2024
	PARTIALLY AGREE	EXPLANATION
	DO NOT AGREE	

OBSERVATION 3		Overhead & Profit Rates
		Management of overhead and profit could be improved to reduce project costs.
RECOMMENDATION 4		We recommend the Water System Operations Group: (1) Request supporting calculations for proposed overhead and profit rates for contract amendments and as part of contract awards. (2) Prepare documentation showing burdened rates were reviewed and negotiated for best value as part of the contract award process and cost analysis completed on a case-by-case basis. These practices should be applied to contracts in other Metropolitan groups.
PRIORITY 2		
X	AGREE	MANAGEMENT ACTION PLAN All Groups within the District will request supporting calculations for the proposed overhead and profit rates. Cost analysis for the overhead and profit rates will only be performed on a case-by-case basis, when justified by scale, market analysis or other possible value. Documentation will be prepared and kept



		within the project files validating that the final burdened rates were negotiated in good faith effort that provide the best contract value and are competitive to the industry standards. Implementation within 30 days from the issuance of this audit report.
	ESTIMATED IMPLEMENTATION	March 2024
<input type="checkbox"/>	PARTIALLY AGREE	EXPLANATION
<input type="checkbox"/>	DO NOT AGREE	

OBSERVATION 4		Accounting Policy & Procedures
		Accounting policy and procedures for capitalization and expensing project costs were not current.
RECOMMENDATION 5		We recommend the Finance Group update Operating Policy F-07 to state a cost is capitalized only if: (1) it is directly identifiable with a specific asset, and (2) incurred after the acquisition of the related asset has come to be considered probable.
PRIORITY 3		
	MANAGEMENT ACTION PLAN	Finance will work on incorporating language to clearly specify capitalization requirements by GASB, with an estimated implementation date of October 2024.
X	AGREE	Updates to Operating Policies must first be coordinated through the technical writing team. Then the changes undergo multiple phases of review from stakeholders throughout the district, group managers and executive management, and often times the bargaining unit, thus the extended timeline.
	ESTIMATED IMPLEMENTATION	October 2024
<input type="checkbox"/>	PARTIALLY AGREE	EXPLANATION
<input type="checkbox"/>	DO NOT AGREE	

