



Internal Audit Report for July 2022

Summary

Two reports were issued during the month:

- 1. Minor Capital Projects Program Audit Report**
- 2. Quarterly Consulting and Services Contracts Review Report for Period Ending March 31, 2022**

Discussion Section

This report highlights the significant activities of the Internal Audit Department during July 2022. 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.

Minor Capital Projects Program

The Audit Department has reviewed the accounting, and administrative controls over the Minor Capital Projects Program for FY 2016-17 through FY 2019-20.

Scope

Our review consisted of evaluating the internal controls over the project submittal, evaluation, administration, and close-out processes for the Minor Capital Projects Program. We also reviewed contractor selection and project accounting and reporting practices. Finally, we evaluated program performance against stated objectives and project schedules.

Background

Metropolitan's Capital Investment Plan (CIP) includes a mix of capital projects to support Metropolitan's strategic plan and financial targets. Capital investment plan projects include the construction of new facilities or infrastructure, additions, upgrades, or replacement and refurbishment of existing infrastructures such as pipes, structures, equipment, and systems. To develop the plan, Metropolitan uses an extensive evaluation process. Each capital improvement project requires the submittal of a formal proposal. The CIP is revised and updated every two years, providing the basis for the Board to approve the budget and appropriate funding.

To expedite smaller projects costing less than \$400,000, with implementation timeframes of no more than three years, Metropolitan implemented the Minor Capital Projects Program. Management can approve projects under this program without seeking additional Board approval. For Fiscal Years 2016-17 through 2019-20, projects authorized under this program are as follows:

Fiscal Years	Appropriation Number	Appropriation Amount	# of Approved Projects
2016/17 – 2017/18	15498	\$ 10,000,000	41
2018/19 – 2019/20	15504	15,500,000	48

Metropolitan management is responsible for establishing and maintaining 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; safeguarding assets; economic and efficient use of resources; and the accomplishment of established goals and objectives. In fulfilling this responsibility, management makes judgments to assess the expected benefits and related costs of control practices and procedures and whether those practices and policies can achieve Metropolitan's financial and operational objectives.

Opinion

In our opinion, the system of internal controls over the Minor Capital Projects Program is generally satisfactory; it was effective from July 1, 2016, through June 30, 2020.

Comments and Recommendations

OVERTIME APPROVAL AND MONITORING

Reviews and approvals help protect against unauthorized, inaccurate, or duplicate transactions. Written approvals should take place before incurring expenditures. Management should use due care in delegating authority and assigning responsibilities.

District policy requires non-emergency overtime (OT) to be pre-approved. Approvers must be authorized and should maintain evidence of such approval.

Our testing of time charged to Minor Capital Projects revealed the following:

- Management could not locate OT approval documentation for 10 of the 12 employees we selected (83%). The ten employees incurred overtime of 419 hours.
- Project Managers are not authorized to approve OT and therefore have no control over it. Additionally, they cannot access Oracle's Project Accounting and Grants Management Module (PAGM) to evaluate labor cost reports. Our analysis of labor cost reports between July 1, 2016, and February 23, 2021, revealed the following:
 - One hundred employees had OT totaling 2,502 hours charged against projects without any Straight Time (ST) against the same project.
 - One hundred eighty-three employees had OT hours exceeding ST, ranging from 25% to 5500%.
 - Twenty projects had OT hours that exceeded ST on a project by 25% to 840%.

Failure to obtain authorization and monitor OT could result in improper incurrence of overtime hours, resulting in unnecessary costs to the District.

We recommend management consider requiring Project Managers to pre-approve non-emergency overtime related to Minor Capital projects in writing. Project Managers should retain evidence of their approvals per the Record Retention Policy. The District should permit project Managers to access Oracle's PAGM to generate labor cost reports for their projects. Project Managers should review the data regularly, performing appropriate follow-ups as necessary.

PROJECT MANAGEMENT

Written procedures provide a framework for effectively and efficiently achieving department and District goals. They assist management in training new employees, offer guidelines in the performance of daily operations, and are a source of reference for experienced personnel.

The District assigns a Project Manager to each Minor Capital project, who is responsible for facilitating the execution of the project requirements with the construction team or contractor. Written procedures require a Project Authorization - New Project Request Form (EForm 540) for each approved Minor Cap project. EForm 540 documents the scope of work and funding levels, and authorizes the commencement of work.

Changes to the scope, approach, completion dates, funding, etc., require an approved Project Authorization – Charge Order Request (EForm 541), with notification to the Project Manager.

Upon project completion, receipt of technical documentation (e.g., warranty certifications, inspection reports, etc.), and signed Notification of Completion by construction management, the Project Manager signs the Request for Project Completion/Cancellation (EForm 543). This action triggers project closure in the Oracle PAGM, which prevents additional expenditures from being charged to the project. Project Management completes the Asset-in-Service Notification (EForm 2514) to place the asset in service and remove it from construction-in-process. Accounting moves the asset into service upon notification to do so.

Using systematic sampling, we selected and tested 30 projects across Appropriations 15498 and 15504. We selected and tested ten projects for close-out.

- The project schedule section was not completed for three project proposals (10%). Two of these projects exceeded the 3-year completion standard. The policy currently recommends but does not require completion of this section.
- The Project Management Plan (PMP) is not consistently approved, updated, or completed:
 - The Project Manager did not approve nineteen (63%)
 - Four (13%) were not updated to reflect the project completion date, project manager, or budget amount

- One project did not have a PMP
- Management could not provide the Project Change Form (Eform 541) for 18 projects (60%). Two of these projects incurred labor charges after the completion date per PAGM.
- Minor Capital Projects are not consistently closed timely, and project files are not always complete:
 - Three of 10 projects (39%) were closed in the PAGM system between 40 and 64 days after the approval date on the Form.
 - Two of the ten project close-out files (20%) did not contain the supporting Budget vs. Cost report.
 - Project 104948 (Appropriation 15498) was canceled in April 2021 but wasn't closed in PAGM until seven months later. Incurred cost at the time of closure was \$81,000.

Failure to control input and processing procedures can result in incomplete data in formulating project-specific and broader-based business decisions, undermining the cost-effectiveness and timely completion of Minor Capital projects.

We recommend management enhance existing procedures to clarify the necessary control procedures and explain the control purpose for each. Further, we recommend management conduct periodic reviews to identify areas requiring further clarification or enhancement.

PROJECT REPORTING

Management reports combine information into a meaningful form to allow management to assess operations and develop strategic plans. Management reports also allow for analysis and tracking without daily project involvement and provide line management with timely and relevant feedback.

We compared Minor Capital Projects Program data per PAGM to the CIP Quarterly Reports for the first and second quarters of 2020. We noted that projects exceeding three years in duration (7 projects) and projects canceled and transferred to a Major Capital Projects program due to scope expansion (4 projects) were not reported. Additionally, we noted that estimated costs for approved projects, actual costs for completed projects, and costs to date for projects exceeding three years are currently not included in the CIP Quarterly Reports.

Incomplete project reporting can result in delayed or erroneous management decisions.

We recommend management expand the CIP Quarterly Reporting to include projects that exceed the 3-year standard and those canceled due to work moving under a Major Capital Projects

program. Management should consider incorporating the cost data for completed projects, projects exceeding the 3-year standard, and closed projects.

Quarterly Consulting and Services Contracts Review Report for Period Ending March 31, 2022

We reviewed the reports for consulting and routine services contracts for the period ending March 31, 2022, issued by the Chief Administrative Officer. This review included the Third Quarter 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 Report) for the Third Quarter of the fiscal year 2021/22. Internal Audit reviews these reports to ensure they are accurate, complete, timely, and compliant 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 2022, the Professional Services Report disclosed that \$37.71 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 \$1.95 million.

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 2022, 37 of 403 agreements were sole-sourced, totaling \$2,959,780. This represents 8% of total fiscal year-to-date expenditures for the fiscal year

2021/22. We also noted that 116 of 403 agreements were small purchases of less than \$74,999, totaling \$1,211,539. See tables below for detail:

Fiscal 2020/21

Fiscal Year-to-Date	General Manager	General Counsel	General Auditor	Ethics Officer
Contract Expenditures	\$36,994,844	*\$538,466	\$460,423	\$254,020
Active Agreements	378	164	1	1
Agreements Terminated	23	5	-	-

*For agreements with transactions during the current fiscal year.

Govt. Agencies	RFP	RFQ	Small Purchases	Sole Source	Total**
\$331,071	\$18,629,971	\$14,576,925	\$1,211,539	\$2,959,780	\$37,709,286
10	46	194	116	37	403
1%	49%	39%	3%	8%	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 an 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 Report for the quarter ending March 2022 was issued to the Board on June 14, 2022.

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 quarterly 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. Section 8122(g) states: “The General Manager may execute contracts for the purchase of materials, supplies, other consumable items such as fuels, water treatment chemicals, materials for construction projects and other bulk items, and for routine services such as waste

disposal and maintenance services, which are generally identified in the budget, regardless of dollar value, provided that sufficient funds are available within the adopted budget for such materials, supplies, and routine services.”

During the quarter ending March 31, 2022, the Contracts Report disclosed seventeen contracts that fit these criteria. We noted the total maximum amount payable for these contracts was \$25.27 million. Eleven contracts were awarded due to competitive bidding under Administrative code section 8140 – Competitive Procurement; two were cooperative agreements, and 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. Further, we reviewed sole-source agreements for justification and approval. Finally, we assessed the timeliness of board reporting.

Testing results

Our review did not reveal discrepancies between contracts and amounts 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 the quarter ending March 31, 2022 Contracts Report was issued to the Board on June 14, 2022.