



**AGENDA
AUDIT COMMITTEE MEETING
OF THE BOARD OF DIRECTORS
INLAND EMPIRE UTILITIES AGENCY*
AGENCY HEADQUARTERS, CHINO, CA 91708**

**MONDAY, MARCH 11, 2019
9:00 A.M.**

CALL TO ORDER

PUBLIC COMMENT

Members of the public may address the Board on any item that is within the jurisdiction of the Board; however, no action may be taken on any item not appearing on the agenda unless the action is otherwise authorized by Subdivision (b) of Section 54954.2 of the Government Code. Those persons wishing to address the Board on any matter, whether or not it appears on the agenda, are requested to complete and submit to the Board Secretary a "Request to Speak" form, which is available on the table in the Board Room. Comments will be limited to five minutes per speaker. Thank you.

ADDITIONS TO THE AGENDA

In accordance with Section 54954.2 of the Government Code (Brown Act), additions to the agenda require two-thirds vote of the legislative body, or, if less than two-thirds of the members are present, a unanimous vote of those members present, that there is a need to take immediate action and that the need for action came to the attention of the local agency subsequent to the agenda being posted.

1. ACTION ITEM

A. MINUTES

The Committee will be asked to approve the Audit Committee meeting minutes of December 11, 2018.

2. INFORMATION ITEMS

A. WATER CONNECTION FEES AUDIT (WRITTEN)

B. ACCOUNT RECEIVABLE FOLLOW-UP AUDIT – WATERMASTER AGREEMENT (WRITTEN)

C. SOUTHERN CALIFORNIA EDISON UTILITY PAYMENTS FOLLOW-UP AUDIT (WRITTEN)

D. THE AUDIT FUNCTION (WRITTEN/POWERPOINT)

- E. INTERNAL AUDIT DEPARTMENT QUARTERLY STATUS REPORT (WRITTEN)

- 3. GENERAL MANAGER'S COMMENTS

- 4. AUDIT COMMITTEE ADVISOR COMMENTS

- 5. COMMITTEE MEMBER COMMENTS

- 6. COMMITTEE MEMBER REQUESTED FUTURE AGENDA ITEMS

- 7. ADJOURN

*A Municipal Water District

In compliance with the Americans with Disabilities Act, if you need special assistance to participate in this meeting, please contact the Board Secretary (909-993-1736), 48 hours prior to the scheduled meeting so that the Agency can make reasonable arrangements.

Proofed by: 

DECLARATION OF POSTING

I, Laura Mantilla, Executive Assistant of the Inland Empire Utilities Agency, A Municipal Water District, hereby certify that a copy of this agenda has been posted by 5:30 p.m. in the foyer at the Agency's main office, 6075 Kimball Avenue, Building A, Chino, CA on Thursday, March 7, 2019.


Laura Mantilla

**ACTION
ITEM**

1A



**MINUTES
SPECIAL AUDIT COMMITTEE MEETING
INLAND EMPIRE UTILITIES AGENCY*
AGENCY HEADQUARTERS, CHINO, CA
TUESDAY, DECEMBER 11, 2018
3:00 P.M.**

COMMITTEE MEMBERS PRESENT

Kati Parker, Chair
Steven J. Elie

COMMITTEE MEMBERS ABSENT

None

STAFF PRESENT

Halla Razak, General Manager
Christina Valencia, Executive Manager of Finance & Administration/AGM
Randy Lee, Executive Manager of Operations/AGM
Lucia Diaz, Facilities Program Supervisor
Javier Chagoyen-Lazaro, Manager of Finance & Accounting
Jason Gu, Manager of Grants
Chander Letulle, Manager of Operations & Maintenance
Kenneth Monfore, Deputy Manager of Maintenance
Peter Soelter, Senior Internal Auditor
Teresa Velarde, Manager of Internal Audit
Laura Mantilla, Executive Assistant

OTHERS PRESENT

Travis Hickey, Audit Committee Advisor
Debbie Harper, Auditor

The meeting was called to order at 3:00 p.m. There were no public comments received or additions to the agenda.

Manager of Internal Audit Teresa Velarde reported that LSL audited IEUA's financial statements and as a result will be issuing an unmodified opinion. Debbie Harper/LSL distributed the following draft documents: Opinion Letter, Report on Internal Control and Audit Communication Letter.

ACTION ITEMS

The Committee:

- ◆ Approved the Audit Committee meeting minutes of September 11, 2018.

◆ Recommended that the Board:

1. Approve the Inland Empire Utilities Agency Comprehensive Annual Financial Report for Fiscal year ended June 30, 2018; and
2. Direct staff to distribute the report as appropriate to the various federal, state, and local agencies, financial institutions, bond rating agencies, and other interested parties;

as a Consent Calendar Item on the December 19, 2018 Board meeting agenda.

◆ Recommended that the Board:

1. Approve the Single Audit Report for FY 2017/18; and
2. Direct Staff to distribute the report, as appropriate to the State Controller's Office, the Federal Audit Clearing House, and other interested parties;

as a Consent Calendar Item on December 19, 2018 Board meeting agenda.

◆ Recommended that the Board:

1. Reconfirm the Audit Committee Charter and the Internal Audit Department Charter; and
2. Direct staff to implement the charters;

as a Consent Calendar Item on December 19, 2018 Board meeting agenda.

◆ Recommended that the Board:

1. Approve the Fiscal Year 2018/19 Annual Audit Plan Amendment to be consistent with the requirements of the IA Charter;

as a Consent Calendar Item on December 19, 2018 Board meeting agenda.

INFORMATION ITEMS

The following information items were presented, received, or filed by the Committee:

- ◆ Agency Vehicle Operation Follow-Up Audit: Review of Vehicle Inventory Procedures
- ◆ Water Connection Fees Interim Report
- ◆ Contract Extension for Financial and Single Auditing Services for IEUA and CBRFA
- ◆ Contract Extension for Audit Advisory Services for the Audit Committee's Financial Advisor/Financial Expert
- ◆ Internal Audit Department Quarterly Status Report for December 2018

GENERAL MANAGER'S COMMENTS

There were no General Manager comments.

AUDIT COMMITTEE ADVISOR COMMENTS

Audit Committee Advisor Travis Hickey stated that receiving an unmodified opinion on the Agency's financials and not having any significant findings is a testament to the Finance and Internal Audit staff on the job they do in maintaining the Agency's books. Mr. Hickey also noted that IEUA sends the CAFR to GFOA for the Excellence in Financial Reporting Award Program.

COMMITTEE MEMBER COMMENTS

There were no Committee Member comments.

COMMITTEE MEMBER REQUESTED FUTURE AGENDA ITEMS

There were no Committee Member requested future agenda items.

With no further business, the meeting adjourned at 4:00 p.m.

Respectfully submitted,

Laura Mantilla
Executive Assistant

*A Municipal Water District

APPROVED: MARCH 11, 2019

**INFORMATION
ITEM
2A**

Date: March 20, 2019

To: The Honorable Board of Directors
Committee: Audit

From: Teresa Velarde, Manager of Internal Audit

03/11/19

Manager Contact: Teresa Velarde, Manager of Internal Audit

Subject: Water Connection Fees Audit

Executive Summary:

Internal Audit completed an audit of water connection fees for the period from January 1, 2016 to June 30, 2018. The objectives were: evaluate internal controls; determine compliance with the Agency's policies and procedures; evaluate collection, recognition and reconciliation of revenue; and identify opportunities for improvements.

The audit found the Agency has effective controls in place over collecting fees and provides recommendations related to:

- Eliminate duplicate activities & systems to streamline processes and achieve single-entry SAP.
- Reconcile transactions to building permits/water meters issued by contracting agencies & water districts and also reconcile on a regular basis on the different internal databases.
- Provide revised wording for Agency's Ordinance & Resolution for adoption to clarify and update policies and provide flexibility in payments.
- Finalize department standard operating procedure to ensure it includes all tasks & duties.
- Work with all related parties to pursue all possible approaches, to ensure all water connection fees are collected, including any delinquent fees.

The attached report provides details of all observations and recommendations.

Staff's Recommendation:

This is an information item.

Budget Impact Budgeted (Y/N): N Amendment (Y/N): N Amount for Requested Approval:

Account/Project Name:

N/A

Fiscal Impact (explain if not budgeted):

N/A

Prior Board Action:

On June 20, 2018, the Board approved the IA Annual Audit Plan. The Water Connection Fees Audit was scheduled in the Annual Audit Plan.

Environmental Determination:

Not Applicable

Business Goal:


IA's Water Connection Fees Audit is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by ensuring that IA's evaluations provide recommendations for efficiencies, improving and safeguarding the Agency's fiscal health, promoting a strong control environment and assisting Agency management in achieving organizational goals and objectives.

Attachments:

Attachment 1 - Water Connection Fees Audit Report
Attachment 2 - PowerPoint



6075 Kimball Avenue • Chino, CA 91708
P.O. Box 9020 • Chino Hills, CA 91709
TEL (909) 993-1600 • FAX (909) 993-1985
www.ieua.org

DATE: February 25, 2019
TO: Kirby Brill
Interim General Manager
FROM: 
Teresa V. Velarde
Manager of Internal Audit

SUBJECT: Water Connection Fees Audit – Audit Report

Audit Authority

The Inland Empire Utilities Agency Internal Audit Department (IA) has performed an audit of water connection fees. The audit was performed under the authority given by the Board of Directors, the Fiscal Year 2018/19 Annual Audit Plan and as requested by the Audit Committee. IA provided an Interim Audit Report at the December 10, 2018 Audit Committee meeting for review and discussion. The attached final report discusses IA's observations and recommendations.

Audit Scope:

The audit objectives were to:

- Ensure adequate internal controls are in place
- Determine compliance with the Agency's Ordinance and Resolution
- Evaluate the collection and recognition of revenue
- Determine whether there are procedures to reconcile fees collected
- Determine compliance with Agency policies and procedures
- Identify opportunities for improvements

Audit Results - Executive Summary

The Agency began collecting water connection fees on January 1, 2016. The transactions are processed by the Planning and Environmental Resources Department (Planning). Revenues are collected and recorded in the Agency's financial records by the Finance and Accounting Department (FAD). The audit found that the Agency has effective controls in place over collecting fees. It should be noted that the Agency relies on the "honor system" with local contracting agencies and water districts to ensure each cooperates and reports all new water connections. IA found opportunities for efficiencies:

Single-entry into SAP

The Agency currently relies on two systems to record and track water connection fee transactions. Agency staff should work to:

- Eliminate duplicate activities and systems to streamline processes using SAP.

Water Smart - Thinking in Terms of Tomorrow

Paul Hofer
President

Jasmin A. Hall
Vice President

Kati Parker
Secretary/Treasurer

Michael E. Camacho
Director

Steven J. Elie
Director

Kirby Brill
Interim General Manager

- Reconcile water connection fee information in the Agency records to the building permits and/or water meters that have been issued by the contracting agencies and water districts.
- Periodically reconcile connection fee transactions on the two different internal databases/systems to ensure differences are evaluated and corrected immediately.

Policy and Procedures

The Agency has been collecting water connection fees for three years and staff have identified opportunities to clarify and update policy language in the areas of payments and other; Planning staff should:

- Provide Executive Management and the Board suggestions and proposed updates to revise to the water connection fee Ordinance and Resolution
- Finalize the draft standard operating procedure and ensure it documents the tasks and procedures associated with the water connection fee processes.

Fee Collections

Since January 2016, the Agency has collected over \$14 million in water connection fee revenues through fiscal year 2017/2018. The revenue is based on the “honor system” because the Agency relies on contracting agencies’ and local water districts to inform their customers about paying the water connection fee directly to IEUA before their project is permitted and water meter is issued. IEUA relies on the cooperation of the agencies and districts to ensure collection.

- The Agency should pursue all possible approaches, including establishing written agreements to ensure all fees are collected.
- The Agency should pursue collection of delinquent water connection fees through various methods, including through tax liens as permitted under the Board-approved Ordinance.

The attached report provides complete details of the audit observations and recommendations specific to the items noted above.

Discussions with Management and Acknowledgements

Drafts of this audit report were provided to Planning and FAD on February 5, 2019 and February 13, 2019 for their review and comments prior to finalizing and their responses have been incorporated. Internal Audit would like to extend our appreciation to Planning, FAD and BIS for their cooperation and assistance during this review.

The Water Connection Fees Audit - Audit Report is consistent with the Agency’s Business Goals of Fiscal Responsibility, Workplace Environment, and Business Practices by ensuring that IA’s evaluations provide recommendations that foster a strong control environment, safeguard assets, promote a safe work environment and assist management in achieving organizational goals and objectives.

Water Connection Fees

Background:

The IEUA Board of Directors established the water connection fee as of January 1, 2016 by approving Agency Ordinance #103 (now revised as #104). The Ordinance requires that any residential or commercial real estate developer that wants to connect to a water service must pay a fee directly to IEUA based on the meter size of their water connection. In practice, IEUA must coordinate with local contracting agencies and water districts responsible for installing or issuing water meters so that IEUA is aware of each upcoming development and can collect the fee. The water connection fee process is considered to be “on the honor system”, because IEUA does not have independent information about new developments and must rely on the efforts of the contracting agencies and water districts to coordinate and verify that developers pay IEUA’s fee before permits are issued or development begins. IEUA provides each developer with a receipt or other evidence of fee payment so that the local contracting agencies and water districts can issue building permits and/or water meters for the projects.

According to the 2018 CAFR (page XXXII):

A water connection fee was established to support capital investments intended to enhance and expand the regional water distribution system and groundwater recharge facilities. The water connection fee is applicable to all potable and recycled water connections and upgrades and is based on meter size . . .

Agency’s Ordinance #104 – Establishing Water Connection Fees, page 11:

The water connection fees shall be established and collected by IEUA in order to proportionally recover the costs to create regional supplies that are available to meet the water demands of future development. Any customer requesting a new connection to a water distribution system within IEUA’s service area, or requiring an additional connection as a result of any addition, improvement, or change in use of an existing connection to a water distribution system shall pay a water connection fee. An existing customer’s request to modify an existing connection will be reviewed by IEUA’s General Manager or his/her designee on a case by case basis to determine if the customer is subject to payment of the water connection fee. The connection fee may not be sold, traded, or conveyed in a manner to another site or customer. The connection does not convey or imply ownership in or of any facilities of IEUA’s water system.

Customers subject to payment of the water connection fee shall pay 100% of the fee prior to issuance of the applicable permit to construct. Any plan changes may result in a revised connection fee payment. Assessment of the applicable connection fee will be based on the date that IEUA receives the final permit application and building plans. If full payment of all fees and charges is not received in accordance with the Resolution payment requirements, the new or additional water services will not be authorized.

And, page 12:

The connection fees have been developed in accordance with California Government Code §66013 and California Water Code §71616 and shall include, but not be limited to, components for:

- (A) The cost for the construction of capture, treatment, transmission, distribution, and injection facilities;
- (B) The cost incurred for the Water Conservation Program which includes Conservation and Drought Charges;
- (C) Providing a reasonable reserve for improvements, extensions, and enlargements for system reliability and associated debt service costs;
- (D) The cost to administer the program incurred by IEUA; and
- (E) Any other costs that are deemed appropriate and comply with governing laws.

The Board of Directors shall establish said connection fees by Resolution and shall adjust said fees from time to time by Resolution. Written notice of the proposed establishment of water rates or amendment of water rates shall be given to all local agencies not less than 15 days prior to the meeting at which such Resolution will be considered.

The Agency's Board also adopted Resolution No. 2015-5-6 which established a five-year rate structure based on the meter size of the water connection:

Meter: Size of Connection	Fiscal Year & Effective Date					
	2015/16	2016/17	2017/18	2018/19	2019/20	
	1/1/2016	7/1/2016	1/1/2017	7/1/2017	7/1/2018	7/1/2019
5/8"	\$693	\$693	\$1,455	\$1,527	\$1,604	\$1,684
3/4"	\$693	\$693	\$1,455	\$1,527	\$1,604	\$1,684
1"	\$1,733	\$1,733	\$3,638	\$3,818	\$4,011	\$4,211
1.5"	\$3,465	\$3,465	\$7,275	\$7,635	\$8,020	\$8,420
2"	\$5,544	\$5,544	\$11,640	\$12,216	\$12,832	\$13,472
3"	\$12,128	\$12,128	\$25,463	\$26,723	\$28,071	\$29,471
4"	\$21,830	\$21,830	\$45,833	\$48,101	\$50,527	\$53,047
6"	\$48,510	\$48,510	\$101,850	\$106,890	\$112,280	\$117,880
8"	\$83,160	\$83,160	\$174,600	\$183,240	\$192,480	\$202,080
10"	\$103,950	\$103,950	\$218,250	\$229,050	\$240,600	\$252,600
12"	\$121,275	\$121,275	\$254,625	\$267,225	\$280,700	\$294,700

The fees were intended to “phase-in” and achieve full “cost of service”.

Revenues

According to the Agency’s CAFR and details in SAP, the water connection fee has resulted in the following revenues:

Water Connection Fees as Reported on the CAFR/SAP				
AGENCY	2015/16	2016/17	2017/18	TOTAL
City of Chino	\$245,379	\$1,054,707	\$2,026,433	\$3,326,519
City of Chino Hills	\$82,473	\$1,280,212	\$992,302	\$2,354,987
Cucamonga Valley Water District	\$60,992	\$341,861	\$1,156,304	\$1,559,157
Fontana Water Company	\$107,075	\$740,884	\$624,903	\$1,472,862
Monte Vista Water District	\$34,654	\$138,605	\$85,512	\$258,771
City of Ontario	\$302,496	\$1,291,148	\$2,652,342	\$4,245,986
City of Upland	\$163,941	\$567,518	\$351,482	\$1,082,941
Total Amounts	\$997,010	\$5,414,935	\$7,889,278	\$14,301,223

Water connection fee transactions are processed by Planning, including providing receipts to developers. The revenues are collected, deposited in the bank and recorded in the Agency’s accounting records by the Finance and Accounting Department (FAD).

Business Information Services (BIS) developed a Building Activity Tracking database for Planning to record fee collections information and provide pre-numbered receipts. The database also provides several automated, standardized reports that are available on the Agency’s internal website under the IEUA REPORTS tab in the “Building Activity Tracking” folder. These reports provide information about transactions with details and can be sorted in a variety of ways, such as by meter size, by developer name, by responsible agency, by fiscal year, as well as including a variety of search features for analysis. Planning also maintains electronic files to document the building plans, meter sizes, check copies and other information.

When the water connection fee was initially approved by the Board, Planning staff met with each of the entities that provide permits for water meters for new development to inform them of the upcoming fee and establish procedures to notify IEUA. The agencies that IEUA interacts with are those that are responsible for issuing or installing the water meter in their community and include both contracting agencies to the Regional Contract and local water districts that are independent of IEUA (other than for wholesale purchases of Metropolitan Water District water). Those that have participated in the fee collection process are:

CONTRACTING AGENCIES

City of Chino
City of Chino Hills
Cucamonga Valley Water District
City of Ontario
City of Upland

LOCAL WATER DISTRICTS

Fontana Water Company/San Gabriel Valley Water District
(FWC/SGVWD)
Monte Vista Water District (MVWD)

There are two additional water districts within IEUA's service area that are also responsible for collecting the water connection fee. These water districts are the San Antonio Water Company (SAWCO) which serves the county area north of Upland and the West Valley Water District which serves a portion of north Fontana. Since the inception of the water connection fee program, neither of these water districts have reported any new connections. West Valley Water District has advised IEUA regarding future development in their service area in north Fontana.

The contracting agencies and local water districts are not compensated for costs they incur to assist IEUA in collecting the water connection fee. According to Planning staff, the costs incurred by the contracting agencies and local water districts to provide information to IEUA about new water connections was not included as part of the initial rate study performed in 2015 that established the water connection fee. The Agency is currently undergoing a new rate study.

Fee collection process

The fee collection process has multiple steps:

- The local permitting entities that report connections to IEUA (FWC/SGVWD, MVWD, Cucamonga Valley Water District and the cities of Chino, Chino Hills, Ontario and Upland) inform IEUA's Planning department when a developer will be issued a new water meter. The notifications are sent by e-mail and include the developer's name, the development location, the size of the meter and copies of the relevant building plans.
- The Agency has established a fee counter in Building B of the Agency's headquarters where fees are paid. Developers are met at the fee counter by Planning staff when they arrive with the fee payment. The payment can also be mailed to the Agency.
- Planning staff compare the information that they have received from the contracting agencies/water districts to what the developer has provided, enter the information into the Building Activity Tracking database created by BIS and issue a prenumbered receipt to the developer.
- The developer uses the receipt to provide verification to the contracting agency/water district to obtain the water meter for installation.

- All cash receipts, both those received by mail and developer's check brought in to the fee counter are entered into a hand-written logbook maintained by the Agency's receptionist.
- Planning leaves the check with the logbook at the front desk and notifies FAD to pick it up for deposit.
- When Planning has processed the payment for a proposed water connection, Planning staff also notify FAD with a group e-mail and all the attachments Planning has received from the developer and/or contracting agency/water district.
- Accounts Receivable staff in FAD prepare an invoice in SAP to recognize revenue in the Agency's SAP records. This is prepared when they receive the information from Planning, generally after the cash has been delivered by the developer to the counter. In some instances (mostly related to the Fontana Water Company) FAD will prepare the billing based on information received from Planning without the Agency receiving payment. These are mostly instances, where the Agency is trying to collect fees after water meters have been installed.
- FAD staff collect the check from the receptionist for online bank deposit. One of the General Ledger Accountants prepares the deposit slip which is then approved by the department's Principal Accountant. Deposits are made as frequently as necessary.
- FAD's administrative staff then scans the deposit and transmits it electronically to the Agency's bank account. This enters the cash receipt into SAP and clears the receivable balance.
- Periodically, based on activity, FAD provides an SAP report to Planning staff listing all water connection fee activity. Planning staff compares the SAP report to their database information.
- Finally, FAD reconciles the bank account monthly to verify all deposit activity.

The fee collection process provides segregation of functions between Planning and FAD which is considered a best practice. The disadvantage of having this level of segregation of functions is the duplication of information stored multiple times (both electronically and physically) in different Agency systems. The supporting documentation and information associated with water connection fees includes:

- Copies of development plans, meter size information and local agency approvals
- Copies of the developer's check
- Copies of the prenumbered receipt
- Copies of the Agency invoice
- Copies of the bank deposit

- the receptionist's hand-written cash receipts log
- Copies of emails/correspondence
- Copies of letters and billing documents

Electronic and manual copies of some or all of these documents are stored multiple times and in multiple places in Agency records. These include:

- Planning department's internal electronic records
- E-mail and E-mail attachments to multiple recipients
- Accounts receivable scan log
- Accounts receivable invoicing attachment in SAP
- FAD department scan log – cash receipts function
- Cash receipts attachment in SAP
- Manual file cabinet in Accounts Receivable
- Bank deposit details and bank statement back-ups

Audit Approach:

IA performed the following audit techniques and procedures:

- Interviews of Planning staff, FAD staff and BIS staff
- Observations of various transactions separately with Planning and FAD staff
- A review of the Agency's Ordinance, Resolution and Planning's draft (SOP).
- An analysis of financial transactions
- Reconciliations between different recordkeeping databases and reports
- Review of supporting documents in SAP and manual and electronic files

Observations and Recommendations

Single-entry into SAP

Observation #1: Eliminate duplicate activities and systems to streamline processes

The Agency currently relies on and uses two separate systems to record, track and reconcile water connection fee transactions. Planning utilizes the BIS developed Building Activity Tracking database to record transactions and provide receipts to developers. FAD records billings, revenues and cash receipts in the Agency's SAP accounting system, which includes the same/duplicate information that Planning entered into the Building Activity Tracking database.

Although separate systems enhance segregation of duties, they have the disadvantage that information is entered and stored multiple times in Agency systems. It can also result in inconsistencies between the separate systems, requiring regular reconciliation processes.

SAP may provide the necessary controls to process water connection fees into only one system. Fully utilizing SAP can streamline business processes, record-keeping, data analysis and data storage. SAP provides features to assign “roles” and “authorizations or permissions” that can limit the types of access granted to different functions within an organization. SAP has the capability to run needed reports for analysis by different staff. The advantage would be a single database and reporting capabilities.

To improve efficiencies and move toward a paperless environment or at least a more efficient/streamlined process, SAP should be fully utilized to eliminate the need to store manual printed copies of documents (such as invoices and receipts), to reduce duplication of scanning/copying documents and any duplicate/redundant recordkeeping. Planning should be able to enter water connection fee data and print receipts directly through SAP and upload supporting documents. FAD should be able to enter and process the cash receipts and perform reconciliations. There may be a one-time implementation cost, but that should be compared to the long-term benefits for the Agency.

Recommendation #1:

Planning should take the lead to work with FAD and BIS to fully utilize SAP’s capabilities to streamline entering fee activity into only one system through a secure process. Planning should enter water connection fee transaction data and print receipts directly from SAP. FAD should enter and process the cash receipts and perform reconciliations. In addition, the system should be able to produce the necessary information reports for analysis.

Observation #2: Reconciliation between IEUA’s Planning Database and the contracting agencies/water districts’ building or water meter permit information

The audit noted there is a need to ensure all owed water connection fees are paid and reported to IEUA. The audit revealed there is a need to reconcile outside and additional information to ensure all connection fees are reported and paid according to the Ordinance requirements. This requires coordination with the agencies and water districts to share reports of water meters sold and new development in their areas.

Planning stated that there is generally adequate support from the contracting agencies to collect the fee. Planning staff have, however noted greater difficulty obtaining information from the local water districts (FWC/SGVWD and MVWD) and the two small water districts within IEUA’s service area; the San Antonio Water Company (SAWCO) and the West Valley Water District (WVWD).

Planning has mentioned the importance of preparing a reconciliation that would compare the Agency’s information about payments for water connection fees to the contracting agencies or water districts’ information about water meters issued by them. According to Planning, they have received enough information from the contracting agencies and local water districts and have completed the comparison for the first six months, from January 1, 2016 to June 30, 2016. Additional reconciliations are in progress. According to Planning, completing the reconciliations is dependent on available staff resources and

obtaining information from the contracting agencies and water districts. IA recommends these recommendations be completed periodically, preferably quarterly, but at a minimum every six months.

Recommendation #2

Planning should take the lead to continue to work with the contracting agencies and water districts to ensure the water connection fees information in the Agency's systems is reconciled to the building permits and/or water meters that have been issued by the contracting agencies and water districts (ideally quarterly, but at least semi-annually).

Planning response:

Planning stated that they requested regular annual water meter information and reports from the Agency's partners, both in preliminary discussions before the fee started and in the many meetings since then. Planning staff is doing the best they can, given this is a new program among the many other responsibilities of staff. Planning noted that collecting water connection fees and completing reconciliations has been a challenge, due to the lack of cooperation from some contracting agencies and local water districts and with the limited resources of the department and hope additional resources are shifted/provided for this program.

Observation #3: Reconciliation of Building Activity Tracking Database to SAP

If the Agency chooses to maintain two separate systems, or at least until a single SAP system approach can be implemented, FAD should prepare a regular reconciliation that compares the information logged by the Planning department in the Building Activity Tracking Database to the information entered into SAP by FAD.

As part of the audit, IA obtained "crystal" reports from the Building Activity Tracking database. IA also obtained reports generated from the Agency's SAP financial system. IA compared the transactions in both reports, and additionally compared these to the information recorded in the manual cash receipts journal maintained at the front desk by the receptionist who logs all checks received. IA noted differences that should be resolved with periodic reconciliations and communication among the three areas.

IA worked with Planning and FAD to identify the reasons for the differences noted between the various reports for water connection fees.

As a result of these audit steps, the reconciliation was recently completed by FAD for the 2 ½ years from January 1, 2016 to June 30, 2018 and FAD has committed to continuing to perform this reconciliation on a regular quarterly basis.

FAD and Planning evaluated the reconciling items and resolved them. The reconciliation found that the building activity tracking database is not generally updated for activity after the initial transactions are recorded resulting in most of the reconciling items. It also found a number of instances where a billing in one fiscal year was not corrected until a subsequent fiscal year and some instances of corrections that had yet to be made. The reconciliation found \$9,010 in additional corrections to be made in SAP for fiscal year

2015/16 errors. This is in addition to the \$26,723 for fiscal year 2016/17 errors already corrected in SAP in the 2018/19 fiscal year. A best practice is to prepare reconciliations on a timely basis so that corrections can be made in the same fiscal year as the initial transaction.

The amounts noted showing which fiscal year that they were billed and which fiscal year that they were corrected or credited were:

TOTAL AMOUNT	FISCAL YEAR BILLED	FISCAL YEAR OF CREDIT
\$4,365	2015/16	2016/17
\$160,765	2016/17	2017/18
\$26,723	2017/18	2018/19
\$9,010	2015/16	2018/19
\$200,863	TOTAL CORRECTIONS/CREDITS	

The credits and corrections are for a variety of reasons. These include billings for locations that are not in the Agency’s service area and refunds for overpayments such as downgrades in meter size, etc.

Recommendation #3:

If the Agency chooses to maintain two separate systems or until a single system can be implemented, FAD should take the lead to work with Planning to establish a process to ensure reconciliations are completed on a regular and timely basis between the information in the Agency’s Building Activity Tracking Database to information in the Agency’s SAP financial system. The reconciliations should be performed preferably at least quarterly and the departments should work together to resolve any items immediately.

FAD response:

FAD had already started considering how to reconcile SAP to the Building Activity Tracking Database information, beginning with the first quarter of the current fiscal year.

Policy and Procedures

Observation #4: There is a need to update the Ordinance and Resolution

Now that the Agency has been collecting water connection fees for three years, there are opportunities to clarify and update policy language:

The water connection fee is governed by Ordinance #104 adopted on June 15, 2016 and Resolution No. 2015-5-6 adopted on May 20, 2015 both approved by the Agency’s Board of Directors. Planning staff have suggestions and updates to the Ordinance and Resolution for Executive Management and the Board of Directors to consider. In particular, updated suggestions include:

- Flexibility with the timing of the fee payment: The Ordinance currently states in Division II, Part II-Water Rates, Section 202 that customers “shall pay 100% of the fee prior to issuance of the applicable permit to construct”. It is Planning’s position that because the scope of new construction can vary, development may occur in several phases or in individual units. This may result in changes to applicable permits, to planned sizes of water connections and/or changes to the timing of development and changes in fee amounts. Additional wording could provide flexibility for which connections fees are due at which times and allow for payment to be made in phases or at different stages of development.
- Additional wording to address refunds/credits: The Ordinance mentions in Division II, Part II-Water Rates, Section 202 that a “request to modify an existing connection will be reviewed by IEUA’s General Manager or his/her designee” but does not specifically mention refunds or under what circumstances refunds would be authorized. Currently, it is Planning’s practice to issue full refund to customers when they request a change. The Ordinance does not address administrative fees necessary to process the original payment or the refund or credit.

The current authorized rate structure expires June 30, 2020, the Agency is currently working with a consultant on a rate study that will evaluate current rates and other items and make recommendations for future rates.

Recommendation #4:

Based on their experience in collecting fees Planning staff should provide Executive Management and the Board their suggestions and proposed updates for revised wording to the water connection fee Ordinance and Resolution for their consideration.

Planning response:

Planning staff already has suggestions for changes to the Ordinance to ensure the objectives of the fees are met, including revisions for timing and calculation of water connection fees and opportunities for refunds. Prior to the completion of the internal audit, FAD staff developed an RFP and the Agency’s Board of Director’s approved a contract with an independent consultant to perform a rate study to use as a basis for establishing rates for future years to include in a revised Resolution.

Observation #5: There is a need to update and finalize the draft Standard Operating Procedures used by Planning

Planning has prepared a draft of a Standard Operating Procedure (SOP) that would provide guidance about the different activities involved in the water connection fees revenue collection process, but it has not been finalized. The draft SOP that IA reviewed included information about what information should be provided by contracting agencies and water districts and the specific steps in the revenue collection process, including the receipt given to the customer and the meter release form provided to the customer and the contracting agency or water district. The draft SOP also calls for Planning to request that contracting agencies and water districts to provide details of all water connections

they have processed on a quarterly spreadsheet so that IEUA can reconcile that information to what is included in IEUA's records.

Since Planning has been collecting connection fees since 2016, staff should use their experience to update, document and finalize the SOP. SOPs serve as a manual that can be applied during staff absences and changes or for back-up employees and as a tool for training and cross training.

Recommendation #5:

Planning staff should work to update and finalize their draft SOP to document various tasks and procedures associated with the water connection fee process, including the processes to work with FAD and the contracting agencies/water districts.

Planning response:

Planning indicated they are doing the best they can, given that this is a new program among the many other responsibilities of staff. Planning noted that completing the SOP has been a challenge with the limited resources of the department and hope additional resources are provided for this program. Planning plans to have an SOP completed in the next fiscal year.

Fee Collections

Observation #6: There is a need to work closer with the contracting agencies and local water districts to verify that all water connection fees are collected as required by the Board-approved Ordinance.

The water connection fee is an Agency revenue source where the Agency interacts directly with retail customers. To ensure that the Agency receives the water connection fees as required by the Ordinance, the Agency uses the "honor system" with contracting agencies and local water districts to inform customers about the need to pay the fee to IEUA before their project is permitted or their water meter issued. Planning staff has met several times with the contracting agencies and water districts and continues to hold regular "check-in meetings" to obtain the needed cooperation. Their efforts have resulted in cooperative relationships with the contracting agencies. However, some local water districts (in particular FWC/SGVWC, SAWCO and WVWD) have not been as responsive as IEUA's contracting agencies. IA found opportunities for improvements:

Planning stated that there is generally adequate support from the contracting agencies to collect the fee, but noted greater difficulty obtaining information from the local water districts. The water districts are regulated by the Public Utilities Commission and subject to different requirements than the contracting agencies. The water districts have informed Planning that they will not include the IEUA water connection fee as part of their own notifications. They have indicated they are willing to distribute IEUA's FAQ sheet (included as Attachment #1) as a separate document, but Planning is not sure this is being done consistently.

Planning staff stated that FWC/SGVWC has not been responsive to the Agency's information requests and has not consistently informed the Agency of new water connections in their service area. FWC/SGVWC has also been uncooperative/ non-responsive in the reconciliation process with the Agency. In addition, according to Planning, FWC/SGVWC staff have cancelled meetings and been generally unavailable for discussions about cooperation.

In addition, the two small water districts within IEUA's service area that have responsibility for water meters, the San Antonio Water Company (SAWCO) and the West Valley Water District (WVWD) have not been cooperative with IEUA for information about new water connections and neither of them have reported any new water connections in their communities since the inception of IEUA's water connection fee. SAWCO has stated that the fee is not their responsibility and has written IEUA to state that the fee does not apply to them and IEUA should work with San Bernardino County instead. WVWD has brushed off information requests about new development.

IA examined a sample of 30 individual water connection fee transactions to determine whether the transactions are adequately supported with the required documentation and accurately recorded. Audit testing included observing the original source documentation from the developer and the contracting agency, the copy of the check, the deposit information and tracing the cash receipt to the relevant bank statement. This evaluation noted that even when IEUA received information from water districts about new connections, in some cases the fees remained outstanding. IA also noted that the Agency's SAP system showed no revenues had been collected from SAWCO or WVWD

To mitigate the lack of responsiveness from FWC/SGVW and WVWD, Planning staff has suggested that the Agency should consider requesting assistance from the City of Fontana to ensure the water connection fee is collected prior to the issuance of the relevant building permit. The Agency's problems with SAWCO are currently insoluble.

Recommendation #6:

Planning should continue to work with the Agency's executive management to pursue all possible approaches, including establishing agreements or other methods to ensure water connection fees are collected as intended by the Board approved Ordinance.

Observation #7: Delinquent fees should be pursued using various methods, including liens.

The Board approved Ordinance #104 requires that any new development or change in meter size be subject to the water connection fee; in Division II, Part II-Water Rates, Section 204 states that "Charges fixed by IEUA shall be a lien on all the property benefitted thereby . . . and shall have the same force and effect as other liens for taxes and may be enforced by the same means as provided for the enforcement of liens for state and county taxes."

It is FAD's responsibility to ensure that all fees due to the Agency are pursued and every attempt is made at collection. As indicated by Planning staff, there are several obstacles that prevent ensuring that all new development in areas serviced by local water districts has been reported to IEUA and that those developers have paid their fees. This results in the Agency potentially not receiving all the fees to which the Agency is entitled. According to Planning staff this was an issue when the fee was first instituted. Planning staff believe that several water connections in the City of Fontana may have been permitted without paying fees.

There have been instances when IEUA staff has attempted to collect connection fees after the fact by invoicing the developer or the address of the project if the Agency determined that fees that were owed had not been paid. However, Planning staff noted that developers have ignored invoices and receivable balances have remained outstanding for extended periods of time. Additionally, the developer may have sold the property and the new property owner may be unaware of the fee and will dispute their responsibility for it.

FAD staff stated that they have developed a Request for Proposal to find a collection agency that would pursue these amounts on the Agency's behalf for a fee amounting to 5% to 10% of the outstanding balance. If these efforts are unsuccessful, FAD believes the last potential step would be to have a lien placed on the property.

Recommendation #7:

FAD should take the lead and work to pursue the collection of delinquent fees through various methods, including the lien process as provided under the Board approved Ordinance.

FAD and Planning response:

FAD notes that there have been no delinquencies in the current fiscal year. Both departments have discussed pursuing delinquent fees through property tax bills but have not actually implemented the right to pursue through liens. FAD commits to following-up with Planning on the next steps in pursuing delinquencies.

Other Matters for Consideration

In addition to the items noted above, IA made additional observations during the course of the audit. These observations were not subjected to the same level of audit testing as the information discussed above and, therefore, are presented only for consideration.

Consider the cost to local agencies and consider reimbursement for costs

Wastewater Capital Connection Fees are held by the contracting agencies as deposits on the Agency's behalf until called by the Agency for specific construction project needs. The Regional Contract specifies that any interest income earned on these deposits remains with the Contracting Agencies, indirectly providing a level of compensation to the contracting agencies for their work collecting the fees on the Agency's behalf.

The water connection fee was instituted beginning January 2016. The fee creates an additional responsibility for the contracting agencies and for the local water districts to coordinate and transmit information to the Agency's Planning department to ensure they have adequate information to calculate fee amounts and subsequently to verify with the developer that they have a receipt for payment to IEUA. There is no compensation to them for their additional efforts and the additional workload. According to Planning the initial rate study that established the fee structure did not consider costs incurred by the contracting agencies and water districts. To meet Proposition 218's mandate that fees cover the costs of service and not more or less, the Agency should consider whether the costs incurred by the Agency's partners should be included in the water connection fee rate calculations and/or consider that reimbursing contracting agencies and districts would provide greater cooperation to provide information.

Reconcile water connections and wastewater connections

Each month the contracting agencies submit the Building Activity Report (BAR) and provide information about all wastewater connections. The BAR details the amount collected, geographical location details and other information. IEUA tracks this information in the Agency's Geographic Information System (GIS). Wastewater connections are not necessary to begin construction and may be paid for at different points in the building process, as allowed per the Regional Contract.

The water connection fee on the other hand, is paid during the initial stage of construction. Therefore, there may be a time lag of months or in rare cases, even years between obtaining the water connection information and obtaining the wastewater connection information, making a reconciliation of the two, for the same property, difficult. But in most instances, both connections are necessary.

There are a variety of reasons why a water connection or a wastewater connection are not both included at a specific location. A wastewater connection may not be necessary because the water meters are intended for irrigation, landscaping, recycled water uses or other similar purposes. Also, some locations may have a water connection but no wastewater connection if the location still uses a septic system. Comparing the data about the locations of the two types of connections and logging and understanding these exceptions can provide a tool for determining where fees have not been paid and provide other useful information to the Agency.

This reconciliation would provide information about how complete IEUA's revenue collection has been and potentially any information that may be missing from local contracting agencies and water districts.

**ATTACHMENT #1:
 WATER CONNECTION FEE FACT SHEET**



**INLAND EMPIRE UTILITIES AGENCY
 WATER CONNECTION FEE FACT SHEET**

The Inland Empire Utilities Agency (IEUA) is a regional wastewater treatment agency and wholesale distributor of imported water and recycled water. The water connection fee is a one-time fee paid to IEUA for any new or upsized water meter connection to a water distribution system within the IEUA service areas. For inquiries regarding the fee, please call (909) 313-9604 or watermeterfee@ieua.org.

- What types of meters are subject to this one-time fee?
- Potable Water, Recycled Water, & Landscape
 - Temporary, fire & parallel service meters are not subject to the fee
- What if I change out the water meter to a different size?
- The fee is determined based on the difference between the original and upsized meter. There is no fee for downsizing a meter.
- How do I calculate the fee?
- Fees are determined by the size and number of water meters being installed for your particular project as provided in the table below.
- When do I pay the fee?
- Fees are paid at the time you pay your local water agency meter fees prior to meter installation
- How do I pay the fee?
- Paid to IEUA located at 6075 Kimball Avenue, Chino Monday-Thursday 8:00 am - 11:30 am and 1:30 pm to 5:00 pm or by mail to: P.O. Box 9020, Chino Hills, CA 91709 Attn: Water Connection Fee
- What types of payment are accepted?
- Personal check & Cashier's check only
 - If sending payment by mail, include site address and Tract/Parcel# along with information cited below
- What paperwork is required to pay the fee?
- Signed paperwork (receipt) from the City or local water agency
 - Stamped/approved plans showing location of meters

WATER METER CONNECTION FEE RATES - EFFECTIVE JULY 1, 2018

5/8"-3/4"	1"	1.5"	2"	3"	4"	6"	8"	10"	12"
\$1,604	\$4,011	\$8,020	\$12,832	\$28,071	\$50,527	\$112,280	\$192,480	\$240,600	\$280,700

*Adopted future rates are available on the IEUA website at www.ieua.org

**ATTACHMENT #2:
 SUMMARY OF RECOMMENDATIONS**

#	DESCRIPTION
1	Planning should take the lead to work with FAD and BIS to fully utilize SAP's capabilities to streamline entering fee activity into only one system through a secure process. Planning should enter water connection fee transaction data and print receipts directly from SAP. FAD should enter and process the cash receipts and perform reconciliations. In addition, the system should be able to produce the necessary information reports for analysis.
2	Planning should take the lead to continue to work with the contracting agencies and water districts to ensure the water connection fees information in the Agency's systems is reconciled to the building permits and/or water meters that have been issued by the contracting agencies and water districts (ideally quarterly, but at least semi-annually).
3	If the Agency chooses to maintain two separate systems or until a single system can be implemented, FAD should take the lead to work with Planning to establish a process to ensure reconciliations are completed on a regular and timely basis between the information in the Agency's Building Activity Tracking Database to information in the Agency's SAP financial system. The reconciliations should be performed preferably at least quarterly and the departments should work together to resolve any items immediately.
4	Based on their experience in collecting fees Planning staff should provide Executive Management and the Board their suggestions and proposed updates for revised wording to the water connection fee Ordinance and Resolution for their consideration.
5	Planning staff should work to update and finalize their draft SOP to document various tasks and procedures associated with the water connection fee process, including the processes to work with FAD and the contracting agencies/water districts.
6	Planning should continue to work with the Agency's executive management to pursue all possible approaches, including establishing agreements or other methods to ensure water connection fees are collected as intended by the Board approved Ordinance.
7	FAD should take the lead and work to pursue the collection of delinquent fees through various methods, including the lien process as provided under the Board approved Ordinance.

Water Connection Fees Audit Final Report



Water Connection Fees Revenues

Water Connection Fees as Reported on the CAFR/SAP

AGENCY	2015/16	2016/17	2017/18	TOTAL
City of Chino	\$245,379	\$1,054,707	\$2,026,433	\$3,326,519
City of Chino Hills	\$82,473	\$1,280,212	\$992,302	\$2,354,987
Cucamonga Valley Water District	\$60,992	\$341,861	\$1,156,304	\$1,559,157
Fontana Water Company	\$107,075	\$740,884	\$624,903	\$1,472,862
Monte Vista Water District	\$34,654	\$138,605	\$85,512	\$258,771
City of Ontario	\$302,496	\$1,291,148	\$2,652,342	\$4,245,986
City of Upland	\$163,941	\$567,518	\$351,482	\$1,082,941
Total Amounts	\$997,010	\$5,414,935	\$7,889,278	\$14,301,223

Water Connection Fee Rates

Meter Size of Connection	Fiscal Year & Effective Date					
	2015/16	2016/17		2017/18	2018/19	2019/20
	1/1/2016	7/1/2016	1/1/2017	7/1/2017	7/1/2018	7/1/2019
5/8"	\$693	\$693	\$1,455	\$1,527	\$1,604	\$1,684
3/4"	\$693	\$693	\$1,455	\$1,527	\$1,604	\$1,684
1"	\$1,733	\$1,733	\$3,638	\$3,818	\$4,011	\$4,211
1.5"	\$3,465	\$3,465	\$7,275	\$7,635	\$8,020	\$8,420
2"	\$5,544	\$5,544	\$11,640	\$12,216	\$12,832	\$13,472
3"	\$12,128	\$12,128	\$25,463	\$26,723	\$28,071	\$29,471
4"	\$21,830	\$21,830	\$45,833	\$48,101	\$50,527	\$53,047
6"	\$48,510	\$48,510	\$101,850	\$106,890	\$112,280	\$117,880
8"	\$83,160	\$83,160	\$174,600	\$183,240	\$192,480	\$202,080
10"	\$103,950	\$103,950	\$218,250	\$229,050	\$240,600	\$252,600
12"	\$121,275	\$121,275	\$254,625	\$267,225	\$280,700	\$294,700

RATES

The Agency's Board of Directors approved Resolution No. 2015-5-6. The resolution provided a five-year rate schedule for fees based on the meter size of the water connection. A new rate study is currently in progress.

Water Connection Fee Audit

MEMBER AGENCIES

- City of Chino
- City of Chino Hills
- Cucamonga Valley Water District
- City of Ontario
- City of Upland

LOCAL WATER DISTRICTS

Fontana Water Company

Monte Vista Water District

NOTE: There are also two small water districts within IEUA's service area that have responsibility for water meters. These are the San Antonio Water Company (SAWCO) which has responsibility for water meters in the county area north of Upland and the West Valley Water District (WVWD) which has responsibility for a small area within the IEUA service area in north Fontana.

RECOMMENDATIONS

Streamline Processes

- Separate databases/systems
- Single entry using SAP.
 - SAP and Building Activity Tracking Database
 - Agency records and information from contracting agencies and water districts

Policy and Procedures

Staff have already identified opportunities to clarify and update policy language.

- Flexibility in timing of payments
- Finalize the draft SOP

Fee Collections

Pursue all possible approaches for collecting fees

- Relationships and agreements
- Pursue collection of delinquent water connection fees through various methods, including through tax liens as permitted under the Board-approved Ordinance



Questions & Discussion

The Water Connection Fees audit is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment, and Business Practices by ensuring that the recommendations provided foster a strong control environment, safeguard assets, provide a safe work environment and assist management in achieving organizational goals and objectives.

Audit Committee

**INFORMATION
ITEM
2B**

Date: March 20, 2019

To: The Honorable Board of Directors

From: Teresa Velarde, Manager of Internal Audit

Committee: Audit

03/11/19


Manager Contact: Teresa Velarde, Manager of Internal Audit

Subject: Accounts Receivable Follow-Up Audit - Watermaster Agreement

Executive Summary:

The Internal Audit Department Charter, requires Internal Audit (IA) follow-up on outstanding recommendations to determine if corrective actions have been taken. IA performed a follow-up a review of one outstanding recommendation from the Accounts Receivable Audit for the Chino Basin Watermaster completed in 2011. The current agreement requires IEUA to be paid "quarterly, in advance..." for reimbursable O&M costs. The original recommendation was provided because the Agency's practice for billing and collecting payment from Watermaster was done after the beginning of the quarter not in advance as documented in the agreement. Finance and Accounting staff had stated they would implement processes to ensure the contract language was followed. A 2015 follow-up review found that there was improvement but additional time was necessary for full implementation. The 2019 follow-up review found that improvements were made, and still found instances where the quarterly billing and payment are completed after the start of the quarter. FAD stated they will process billings before the end of the quarter for two of the four quarters because current accounting practices require that two of the four billings be completed after the start of the quarter. IA will close-out this recommendation because improvements have been made and the risk of billing after appears low. The attached report provides details of the follow-up review and FAD's response.

Staff's Recommendation:

This is an information item.

Budget Impact *Budgeted* (Y/N): N *Amendment* (Y/N): N *Amount for Requested Approval:*

Account/Project Name:

N/A

Fiscal Impact (explain if not budgeted):

N/A

Prior Board Action:

On June 20, 2018, the Board approved the IA Annual Audit Plan. The Accounts Receivable Follow-Up Audit - Watermaster Agreement was scheduled in the Annual Audit Plan.

On September 16, 2015, the Board received and filed the first Intercompany Accounts Receivables Follow-Up Review, which included Chino Basin Watermaster.

On September 21, 2011 the Board received and filed the original Accounts Receivable Audit for the Chino Basin Watermaster.

Environmental Determination:

Not Applicable

Business Goal:

The Accounts Receivable Follow-Up Audit for Watermaster is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment, and Business Practices by providing independent evaluations and audit services of Agency activities and making recommendations to foster a strong ethical and internal control environment, provide efficiencies, safeguard assets and assist management in achieving organizational goals.


Attachments:

Attachment 1 - Accounts Receivable Follow-Up Audit - Watermaster Agreement Report



6075 Kimball Avenue • Chino, CA 91708
P.O. Box 9020 • Chino Hills, CA 91709
TEL (909) 993-1600 • FAX (909) 993-1985
www.ieua.org

DATE: February 26, 2019
TO: Kirby Brill
Interim General Manager

FROM: 
Teresa V. Velarde
Manager of Internal Audit

SUBJECT: Accounts Receivable Follow-Up Audit – Watermaster Agreement

Audit Authority

The Internal Audit (IA) Department’s Charter requires that IA follow-up on the status of audit recommendations to determine if corrective actions were taken. This follow-up review was performed under the authority provided by the Inland Empire Utilities Agency (IEUA or Agency) Board of Directors and the Fiscal Year 2018/19 Annual Audit Plan. IA completed a follow-up review of one remaining recommendation related to the Accounts Receivable Audit for the Chino Basin Watermaster report, dated August 30, 2011.

Audit Objective and Scope

The purpose of this follow-up review was to evaluate whether the original recommendation has been implemented. IA determined the recommendation is now closed. IA did not expand the scope of the review to evaluate additional areas, further reviews will be scheduled through the Board-approved Annual Audit Plan. The attached report provides details of our review.

Acknowledgements

IA would like to extend our appreciation to the Finance and Accounting Department (FAD) staff for their cooperation and assistance during this follow-up review.

Discussions with Management

IA provided the results of this follow-up review to FAD for their review and comments prior to finalizing this report.

Water Smart - Thinking in Terms of Tomorrow

Paul Hofer
President

Jasmin A. Hall
Vice President

Kati Parker
Secretary/Treasurer

Michael E. Camacho
Director

Steven J. Elle
Director

Kirby Brill
Interim General Manager

Background

The Agency has two recurring receivables from Chino Basin Watermaster (Watermaster), one is for Operations and Maintenance (O&M) costs, while the other is for Debt Service related to the issuance of bonds. This follow-up recommendation is related to the receivable associated with the O&M costs.

The Chino Basin Recharge Master Plan Agreement (O&M agreement) is a 30-year contract that defines the terms and conditions for reimbursement of the O&M costs to IEUA (agreement will expire on December 31, 2032). According to the O&M agreement, Watermaster is required to pay IEUA quarterly, in advance, the estimated amount of the total budget that is expected to be expended during the quarter. Thus, IEUA will receive four quarterly payments from Watermaster for reimbursable O&M costs during the fiscal year (FY).

The original 2011 Accounts Receivable Audit report provided six recommendations to tighten controls and improve billing and receivable functions. After a 2015 follow-up review one recommendation remained outstanding and it is associated with the quarterly billing and payment from Watermaster.

This report provides a status on the outstanding recommendation.

Original 2011 Recommendation #1:

Fiscal Management Department should establish procedures to prepare and submit invoices to Watermaster prior to the beginning of the quarter to allow payment by Watermaster before the quarter begins.

Status: Recommendation Closed

During the 2011 original audit, IA identified that the payments made by Watermaster to IEUA were not timely according to the O&M agreement. The agreement states:

“Quarterly, in advance, Watermaster will pay to IEUA the portion, as shown by the Consolidated Budget, of the estimated amount needed to fund the portion of the total budget to be expended during the quarter.”

The original observation noted that IEUA was not billing “in advance” of the quarter, therefore, Watermaster was not able to remit payment “in advance” as required by the agreement. IA noted payments were received between 11-113 days **after** the start of the quarter with an average per fiscal year of between 17 and 60 days after the start of the quarter for the 3 years from FY 2008 to 2010.

The O&M agreement does not provide any guidelines and/or procedures on invoicing but stipulates that Watermaster should pay IEUA “in advance”. To submit payment, Watermaster relies on the invoices prepared by IEUA. In all instances Watermaster paid within the Agency’s net terms of 15 days. The original recommendation was provided

because the Agency's practice for billing and receipt of payment from Watermaster was not "in advance" of the corresponding quarter. IA determined that not billing and receiving payment "in advance" does not comply with the requirements of the O&M agreement and therefore, may present a potential risk to the Agency for non-compliance with the agreement language.

For this 2019 follow-up evaluation, IA evaluated the billing and receipt of payment from Watermaster for reimbursable O&M costs during the three fiscal years FY 2016/17 through the most current payment (quarter 3 of FY 2018/19). The review identified that improvements have been made in billing Watermaster "in advance" of the quarter. However, IA identified instances where billing and receipt of payment continues to be *after* the start of the quarter. Watermaster payments were received between 4 days in advance to 80 days after the start of the quarter, with an overall average of 16 days after the start of the quarter and a "per fiscal year average" of 7 to 25 days *after* the start of the quarter. Of the 11 payments evaluated, 2 were received "in advance of the quarter".

The analysis shows this is an improvement over prior reviews performed by IA. In comparison to more recent years, the attachment (**Attachment 1**) shows that billings were ranging from 11 to 113 days after the start of the quarter (and "a per fiscal year average" range between 17 days and 60 days after the start of the quarter) for 2008 to 2010.

For the current fiscal year, FY 2018/19, IA noted significant improvements. For Quarter 1 FAD completed the billing only one day after the beginning of the quarter. For Quarter 2, Finance and Accounting completed the billing 4 days in advance of the quarter but since the net payment terms are 15 days, the payment was received after the quarter. Lastly, for Quarter 3, both the billing and payment were both completed in advance of the quarter. At the time of our review, Quarter 4 was not yet due.

FAD has made improvements and is now billing sooner and in some cases in advance of the quarter. IA recommends FAD continue to work to implement additional controls and processes to ensure payments are received in advance of the quarter. Based on these improvements and analysis in FY 2018/19, it appears that FAD can implement processes to bill and collect in advance as required by the agreement.

Response by Finance and Accounting:

Finance and Accounting agreed to implement processes to ensure the billing for two of the four quarters (3rd and 4th quarters) is completed two weeks before the end of the previous quarter to allow Watermaster time to make the payment within IEUA's payment terms of 15 days; therefore, in those quarters the payment would be received "in advance" of the quarter.

Additionally, Finance and Accounting stated that they are not able to process the billing and receive payment "in advance" of the quarter for the 1st quarter because accounting staff require an adopted budget from the Board of Directors to determine the basis for the

quarterly billing amounts. Also, Finance and Accounting stated that they are not able to process the billing and receive payment “in advance” of the quarter for the 2nd quarter because they must complete a reconciliation of the prior fiscal year’s billings and apply any credits for prior year overbillings in comparison to actual results.

FAD is aware of options discussed with Internal Audit to address the potential risk exposure of what may appear to be non-compliance with the agreement when the billing and receiving of payment is not “in advance” of the quarter. One option is for FAD to take the lead to amend the language and the requirement of the agreement to provide flexibility in the time frame of billing and payments so that it agrees with the Agency’s current billing practice. Another option is for FAD to seek legal guidance/interpretation and clarification on the current language of the agreement to compare and evaluate the current practice of the Agency’s billings, to ensure there is no risk exposure with the current billing methodology or with billing after the quarter. FAD indicated that they will not pursue either option because seeking legal guidance or amending the agreement may be costly and not necessary.

As noted in this report, FAD has made positive efforts to implement and minimize the number of days the Agency bills and collects after the quarter and FAD stated they will continue to ensure billings are timely during two of the four quarters. IA will close-out this recommendation unless the Audit Committee provides guidance for further review and evaluation. As required by the Charter and professional auditing standards, IA has communicated the potential risk of non-compliance with the O&M agreement for instances when the billing and payment are not completed “in advance” of the quarter. IA determines that the risk is low to the Agency. IA acknowledges FAD’s response above, indicating FAD’s acceptance of potential risk of non-compliance and that the potential risk lies within the Agency’s risk tolerance for this specific agreement. Based on the results of this review and the two prior reviews (2011, 2015) all received and filed by the Audit Committee and the Board of Directors, IA has complied with its reporting requirements.

The Accounts Receivable Follow-Up Audit – Watermaster Agreement is consistent with the Agency’s Business Goals of Fiscal Responsibility, Workplace Environment, and Business Practices by ensuring that the recommendations foster a strong control environment and assist management in achieving organizational goals and objectives.

Attachment 1: IA's review of the O&M Billing and Receipt of Payment from Chino Basin Watermaster

Observation	Fiscal Year	Quarter	Months	Invoice Amount	First day of the Quarter (1)	Invoice Date (2)	Number of Days between First day of the Quarter and Invoice Date (1) - (2)	Invoice Due Date (3)	Date Payment Received (4)	Number of Days Payment received after the 1st day of the Quarter (1) - (4)	Average Number of Days Payment received after the 1st day of the Quarter
Original Audit	2007/08	1Q	July 1 - Sept 30	\$190,000.00	7/1/2007	7/2/2007	1	7/17/2007	7/30/2007	29	17
		2Q	Oct 1 - Dec 31	\$190,000.00	10/1/2007	10/1/2007	0	10/16/2007	10/12/2007	11	
		3Q	Jan 1 - March 31	\$190,000.00	1/1/2008	1/2/2008	1	1/17/2008	1/16/2008	15	
		4Q	April 1 - June 30	\$190,000.00	4/1/2008	4/1/2008	0	4/16/2008	4/14/2008	13	
	2008/09	1Q	July 1 - Sept 30	\$159,441.73	7/1/2008	7/30/2008	29	7/30/2008	8/12/2008	41	60
		2Q	Oct 1 - Dec 31	\$140,388.41	10/1/2008	12/22/2008	82	12/22/2008	1/14/2009	103	
		3Q	Jan 1 - March 31	\$149,915.07	1/1/2009	3/2/2009	60	3/2/2009	3/11/2009	70	
		4Q	April 1 - June 30	\$149,915.07	4/1/2009	4/8/2009	7	4/8/2009	4/28/2009	27	
	2009/10	1Q	July 1 - Sept 30	\$161,886.25	7/1/2009	8/5/2009	35	8/5/2009	8/28/2009	57	33
		2Q	Oct 1 - Dec 31	\$166,828.59	10/1/2009	10/1/2009	0	10/16/2009	10/19/2009	18	
		3Q	Jan 1 - March 31	\$161,886.25	1/1/2010	1/7/2010	6	1/22/2010	2/1/2010	30	
		4Q	April 1 - June 30	\$161,886.25	4/1/2010	4/1/2010	0	4/16/2010	4/26/2010	25	
Continuous Follow-up review	2010/11	1Q	July 1 - Sept 30	\$171,158.01	7/1/2010	7/13/2010	12	7/28/2010	8/2/2010	31	31
		2Q	Oct 1 - Dec 31	\$173,527.31	10/1/2010	10/20/2010	19	11/4/2010	11/1/2010	30	
		3Q	Jan 1 - March 31	\$171,158.01	1/1/2011	1/13/2011	12	1/28/2011	2/2/2011	31	
		4Q	April 1 - June 30	\$171,158.01	4/1/2011	4/4/2011	3	4/19/2011	N/A	N/A	
	2011/12	1Q	July 1 - Sept 30	\$180,656.82	7/1/2011	7/28/2011	27	8/12/2011	8/16/2011	45	28
		2Q	Oct 1 - Dec 31	\$180,656.82	10/1/2011	10/10/2011	9	10/25/2011	10/24/2011	23	
		3Q	Jan 1 - March 31	\$177,576.69	1/1/2012	1/18/2012	17	2/2/2012	N/A	N/A	
		4Q	April 1 - June 30	\$180,656.82	4/1/2012	4/2/2012	1	4/17/2012	4/17/2012	16	
	2012/13	1Q	July 1 - Sept 30	\$208,488.25	7/1/2012	7/22/2012	21	8/6/2012	7/30/2012	29	48
		2Q	Oct 1 - Dec 31	\$208,488.25	10/1/2012	10/15/2012	14	10/30/2012	10/29/2012	28	
		3Q	Jan 1 - March 31	\$131,623.60	1/1/2013	4/10/2013	99	4/25/2013	4/24/2013	113	
		4Q	April 1 - June 30	\$208,488.25	4/1/2013	4/10/2013	9	4/25/2013	4/24/2013	23	
	2013/14	1Q	July 1 - Sept 30	\$198,694.00	7/1/2013	8/21/2013	51	9/5/2013	9/5/2013	64	52
		2Q	Oct 1 - Dec 31	\$198,694.00	10/1/2013	10/28/2013	27	11/12/2013	11/8/2013	37	
		3Q	Jan 1 - March 31	\$198,694.00	1/1/2014	3/6/2014	64	3/21/2014	3/20/2014	79	
		4Q	April 1 - June 30	\$122,705.66	4/1/2014	4/14/2014	13	4/29/2014	4/29/2014	28	
	2014/15	1Q	July 1 - Sept 30	\$185,423.12	7/1/2014	7/2/2014	1	7/17/2014	7/14/2014	13	40
		2Q	Oct 1 - Dec 31	\$38,447.36	10/1/2014	10/27/2014	26	11/11/2014	1/21/2015	110	
		3Q	Jan 1 - March 31	\$185,423.12	1/1/2015	1/5/2015	4	1/20/2015	1/21/2015	20	
		4Q	April 1 - June 30	\$185,423.12	4/1/2015	4/1/2015	0	4/16/2015	4/16/2015	15	
	2015/16	1Q	July 1 - Sept 30	\$197,976.87	7/1/2015	7/1/2015	0	7/16/2015	7/13/2015	12	5
		2Q	Oct 1 - Dec 31	\$197,976.87	10/1/2015	9/9/2015	(22)	9/24/2015	9/25/2015	(6)	
		3Q	Jan 1 - March 31	\$(108,234.23)	1/1/2016	12/9/2015	(23)	12/24/2015	N/A	N/A	
		4Q	April 1 - June 30	\$197,976.87	4/1/2016	3/28/2016	(4)	4/12/2016	4/11/2016	10	

Accounts Receivable Follow-Up Audit – Watermaster Agreement

February 26, 2019

Page 6 of 6

Observation	Fiscal Year	Quarter	Months	Invoice Amount	First day of the Quarter (1)	Invoice Date (2)	Number of Days between First day of the Quarter and Invoice Date (1) - (2)	Invoice Due Date (3)	Date Payment Received (4)	Number of Days Payment received after the 1st day of the Quarter (1) - (4)	Average Number of Days Payment received after the 1st day of the Quarter
2019 Follow-up review	2016/17	1Q	July 1 - Sept 30	\$243,510.82	7/1/2016	7/11/2016	10	7/26/2016	7/25/2016	24	25
		2Q	Oct 1 - Dec 31	\$243,510.82	10/1/2016	9/19/2016	(12)	10/4/2016	9/30/2016	(1)	
		3Q	Jan 1 - March 31	\$217,185.73	1/1/2017	3/6/2017	64	3/21/2017	3/21/2017	80	
		4Q	April 1 - June 30	\$243,510.82	4/1/2017	3/15/2017	(17)	3/30/2017	3/29/2017	(2)	
	2017/18	1Q	July 1 - Sept 30	\$264,407.72	7/1/2017	7/6/2017	5	7/21/2017	7/17/2017	16	14
		2Q	Oct 1 - Dec 31	\$64,407.72	10/1/2017	9/17/2017	(14)	10/2/2017	10/2/2017	1	
		3Q	Jan 1 - March 31	\$71,090.89	1/1/2018	1/17/2018	16	2/1/2018	2/8/2018	37	
		4Q	April 1 - June 30	\$264,407.93	4/1/2018	3/15/2018	(17)	3/30/2018	4/2/2018	1	
	2018/19	1Q	July 1 - Sept 30	\$293,578.73	7/1/2018	7/2/2018	1	7/17/2018	7/16/2018	15	7
		2Q	Oct 1 - Dec 31	\$293,578.73	10/1/2018	9/27/2018	(4)	10/12/2018	10/11/2018	10	
		3Q	Jan 1 - March 31	\$2,068.38	1/1/2019	12/20/2018	(12)	1/4/2019	12/27/2018	(4)	
		4Q	April 1 - June 30								
Billing in Progress											

Audit Committee

INFORMATION
ITEM
2C

Date: March 20, 2019

To: The Honorable Board of Directors

From: Teresa Velarde, Manager of Internal Audit

Committee: Audit

03/11/19

Manager Contact: Teresa Velarde, Manager of Internal Audit

Subject: Southern California Edison Utility Payments Follow-Up Audit

Executive Summary:

The Internal Audit Department Charter, requires Internal Audit (IA) follow-up on outstanding recommendations to determine if corrective actions have been taken. The follow-up reviews are scheduled through the Board-approved Annual Audit Plan and Executive Management supports the implementation efforts of the recommendations.

IA performed a follow-up review of one outstanding recommendation from the Southern California Edison (SCE) Utility Payments Audit completed in 2013. The follow-up review found that Agency staff worked and finalized with the City of Chino (City) and SCE to transfer the utility account for street lighting services located in front of the Headquarters Buildings. The responsibility for the billing shifted from IEUA to the City because it is the City's expense. As of April 30, 2018, the City of Chino took the responsibility for the account. IA verified that IEUA is no longer billed for the street lighting services. Since the audit finding was noted in 2013, the Agency paid approximately \$4,000 for the street light. The Agency had been paying the account since Headquarters was built. The change provides the Agency a savings of approximately \$900/year.

Staff's Recommendation:

This is an information item.

Budget Impact Budgeted (Y/N): N Amendment (Y/N): N Amount for Requested Approval:

Account/Project Name:

N/A

Fiscal Impact (explain if not budgeted):

N/A

Prior Board Action:

On June 20, 2018, the Board approved the IA Annual Audit Plan. The SCE Utility Payments Follow-Up audit was scheduled in the Annual Audit Plan.

On December 20, 2017, the Board received and filed the first SCE Utility Payments Follow-Up Audit Report.

On November 20, 2013, the Board received and filed the original SCE Utility Payment Audit Report.

Environmental Determination:

Not Applicable

Business Goal:

The SCE Utilities Payment Follow-up Audit is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment, and Business Practices by providing independent evaluations and audit services of Agency activities and making recommendations to foster a strong ethical and internal control environment, provide efficiencies, safeguard assets and assist management in achieving organizational goals and objectives.

Attachments:

Attachment 1 - SCE Utility Payments Follow-Up Audit Report



6075 Kimball Avenue • Chino, CA 91708
P.O. Box 9020 • Chino Hills, CA 91709
TEL (909) 993-1600 • FAX (909) 993-1985
www.ieua.org

DATE: February 22, 2019
TO: Kirby Brill
Interim General Manager
Teresa V. Velarde
FROM: Teresa V. Velarde
Manager of Internal Audit

SUBJECT: Southern California Edison Utility Payments Follow-Up Audit

Audit Authority

The Internal Audit (IA) Department's Charter and the Fiscal Year 2018/19 Annual Audit Plan require that IA follow-up on the status of audit recommendations to determine if corrective actions were taken. This follow-up review was performed under the authority provided by the Inland Empire Utilities Agency (IEUA or Agency) Board of Directors. IA completed a follow-up review of the one remaining outstanding recommendation related to the Southern California Edison Utility Payments Audit.

Audit Objective

The original SCE Utility Payments Audit report was issued in August 2013 and provided a total of four recommendations. In November 2017, a follow-up review found that one recommendation remained in progress as detailed below. The purpose of this follow-up review was to evaluate the implementation status for the one outstanding recommendation, which has now been implemented. The recommendation required Agency staff to work with the City of Chino and Southern California Edison to transfer the financial responsibility for a utility account from IEUA to the City of Chino because it belonged to the city. IA did not expand the scope of the review to evaluate additional areas, further reviews will be scheduled through the Board-approved Annual Audit Plan. The attached provides details of our review.

Acknowledgements

IA would like to extend our appreciation to the Planning & Environmental Resources and Finance and Accounting Department staff for their cooperation and assistance during this follow-up review.

Discussions with Management

IA provided the results of this follow-up review to respective managers and staff for their review and comments prior to finalizing this report.

Water Smart - Thinking in Terms of Tomorrow

Background

Southern California Edison (SCE) provides electricity services to the Agency to power and operate its buildings, facilities, and treatment plants. As of February 2019, the Agency has approximately 46 accounts with SCE. For Fiscal Year 2018, the Agency paid \$5.8 million to SCE for expenses related to electricity.

2013 Original Recommendation #1:

IA recommends that the Planning & Environmental Compliance and the Maintenance departments work with the City of Chino and SCE to resolve the billing issue related to the street lights in front of IEUA's HQ-A building as the street lights have been identified as the financial responsibility of the City of Chino.

Status: Implemented

The 2013 original audit identified that SCE billed IEUA for the electricity used to power the street lights located in front of the Agency's Headquarter Buildings. Staff noted the financial responsibility for these services belongs to the City of Chino, not IEUA. However, the expenses have been billed to and paid by IEUA since the completion of the current headquarters building. During the original audit, Planning & Environmental Resources (Planning) staff had initiated discussions to transfer the utility account to the City of Chino. Planning staff wanted to pursue the item until completely resolved. IA's role was to follow up and provide a report.

IEUA was billed for the street lights under SCE Service Account # 3-026-1435-32, and the average monthly expense was approximately \$72 per month or \$865 for FY 2017/18. Since the time of our original audit in 2013, the expense added up to over \$4,000.

As of August 1, 2018, the SCE Service Account # 3-026-1435-32 has been closed and IEUA is no longer billed for these electricity services. On December 10, 2018, the Agency received a refund check from SCE in the amount of \$222.31 for the billing period, April 30th to August 1st, 2018. Therefore, making the account the responsibility of Chino, effective April 30th, 2018.

Having the SCE account transferred to the City of Chino provides an annual savings of approximately \$900 per year to the Agency. The amount paid for the street lighting services is minimal when compared to the total annual costs incurred for electricity services; however, it is important that IEUA pay only for its direct electricity expenses and not subsidize any expenses.

No further work is required, and IA considers this recommendation to be implemented.

The SCE Utilities Payment Follow-up Audit is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment, and Business Practices by ensuring that the recommendations foster a strong control environment and assist management in achieving organizational goals and objectives.

Audit Committee

INFORMATION
ITEM
2D

Date: March 20, 2019

To: The Honorable Board of Directors

From: Teresa Velarde, Manager of Internal Audit

Committee: Audit

03/11/19

Manager Contact: Teresa Velarde, Manager of Internal Audit

Subject: The Audit Function

Executive Summary:

The Agency's Internal Audit Department (IAD) and the Audit Committee were established by Board action on April 21, 2004 as a response to increased responsibilities for financial reporting and audit compliance requirements for various regulatory agencies. The Audit Function is composed of the Audit Committee, the IAD, the External Financial Auditors and the Audit Committee Advisor. Its purpose is to assist Agency management in achieving organizational goals and objectives and assist the Board in fulfilling their oversight responsibilities for financial reporting, internal controls, and compliance with regulatory requirements. Annually, the Board approves the IAD Charter and the Annual Audit Plan which document the authority and responsibilities of the IAD, as well as any amendments to proposed audit plans/projects and all audit reports and updates. The current structure of the Audit Function follows best practices and guidelines promoted by nationally recognized professional associations and auditing standards. The IAD seeks to promote a strong internal control and ethical environment, add value and improve the Agency's operations, safeguard assets, and improve efficiencies through independent and objective audits and recommendations. The attached report and reference material provides information about the purpose of the Audit Function and tools to use in evaluating the Audit Function components.

Staff's Recommendation:

This is an information item.

Budget Impact Budgeted (Y/N): N Amendment (Y/N): N Amount for Requested Approval:

Account/Project Name:

N/A

Fiscal Impact (explain if not budgeted):

N/A

Prior Board Action:

On December 19, 2018, the Board of Directors reconfirmed the approved Audit Committee and Internal Audit Department Charters.

On June 20, 2018, the Board of Directors approved the Fiscal Year 2018/19 Annual Audit Plan. The plan was in accordance with auditing standards and the Charter requirements.

On March 15, 2017, the Board received and filed the report on IEUA's Internal Audit Function.

Environmental Determination:

Not Applicable

Business Goal:

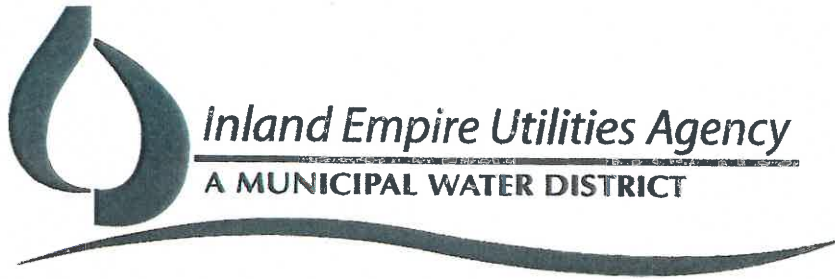
This report describing the IEUA Audit Function is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by describing the functions, roles, authority and responsibilities of the Audit Committee of the Board of Directors, the Internal Audit Department, the External Financial Auditors and the Audit Committee Financial Advisor and their responsibilities assisting the Agency in achieving its goals.

Attachments:

Attachment 1 - The Audit Function - Report

Attachment 2 - Reference Material (link) - <https://ieua.sharefile.com/d-se154bd1bc314bfa>

Attachment 3 - Powerpoint



The Audit Function

This report describing the IEUA Audit Function is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by describing the functions, roles, authority and responsibilities of the Audit Committee of the Board of Directors, the Internal Audit Department, the External Financial Auditors and the Audit Committee Financial Advisor and their responsibilities assisting the Agency in achieving its goals.

**Prepared by:
Internal Audit Department
March 11, 2019**



6075 Kimball Avenue • Chino, CA 91708
P.O. Box 9020 • Chino Hills, CA 91709
TEL (909) 993-1600 • FAX (909) 993-1985
www.ieua.org

DATE: March 11, 2019
TO: Honorable Board of Directors

Kirby Brill
Interim General Manager

FROM: Teresa V. Velarde
Manager of Internal Audit

SUBJECT: The Audit Function

The Inland Empire Utilities Agency (IEUA or Agency) Internal Audit Department (IA) and the Audit Committee were established by Board action on April 21, 2004. The Audit Function was established as a response to increased responsibilities for financial reporting and audit compliance requirements of various regulatory agencies, specifically related to the financial growth of the Agency associated with the issuance of bonds and receipt of increasing grant funding, along with the administration of rebate programs and the active roles and projects with various joint powers and member agencies. As documented in the March 17, 2004 Board Letter, the Audit Function was the staff recommendation to provide greater Board oversight of External Auditor activities, to perform internal audits and prepare/submit audit reports, to adopt Government Finance Officers Association (GFOA) and Institute of Internal Auditors (IIA) guidance and comply with California legislation modifying audit reporting. Additionally, to ensure the Agency maintains the highest standards of fiscal integrity and accountability, provide a system of sound checks and balances, and ensure a truly independent view of Agency operations.

For purposes of this report, "the Audit Function" refers to: the Internal Audit Department, the External Auditors, the Audit Committee Financial Expert and the Audit Committee. The purpose of the Audit Function is to assist the Agency in achieving its goals and objectives. The Internal Audit Department is charged with the responsibility to ensure the oversight obligations of the Audit Function are met. The Internal Audit Department seeks to add value and improve the organization's operations through independent, objective audits, reviews and evaluations and recommendations provided. Internal Auditors must adhere to a strict Code of Conduct, professional standards and principles and follow a systematic, disciplined approach in performing internal audits, evaluating operations and make recommendations.

The current structure of the Agency's Internal Audit Department follows best practices and guidelines as recommended by the nationally recognized professional associations

Water Smart - Thinking in Terms of Tomorrow

that provide guidance and standards for the functions of Accounting and Auditing, including: Government Finance Officers Association (GFOA), the Institute of Internal Auditors (IIA) and the American Institute of Certified Public Accountants (AICPA). Consistent with those best practices, the Internal Audit Department reports functionally to the Board through the Audit Committee to establish independence and objectivity and as a means to minimize or eliminate any pressures from management or eliminate any perception of not being independent. Also, consistent with best practices, the Internal Audit Department reports administratively to the General Manager for planning and coordinating audit projects, establishing the department's budget and staffing needs and other administrative items. The purpose, authority and responsibilities of the Internal Audit Department are documented in the Board-approved Charter.

The purpose of the Internal Audit Department is summarized as:

- Assists the Agency achieve its goals
- Evaluates risks
- Assesses the reliability of internal controls
- Provides recommendations for improving operations and compliance
- Promotes a strong ethical culture
- Reviews processes and procedures
- Provides on-going monitoring and follow-up reviews
- Provides recommendations to safeguard assets
- Raises potential red flags to appropriate Agency management and the Board
- Communicates results to management, the Audit Committee and the Board
- Serves as the "eyes and ears" of the Board of Directors

The IEUA Audit Committee is composed of two members of the Board and an outside member that serves as the Financial Expert and Advisor to the Audit Committee, as prescribed by best practices. GFOA, AICPA and the IIA recommend the Audit Committee meet at minimum quarterly and discuss audit matters with Executive Management, the Internal Auditor, the Financial Advisor and the External Auditors and report to the Board any significant issues that warrant attention. IEUA has followed this prescribed model since 2004 and is continuously praised by outside organizations for following the most independent model prescribed.

This report provides additional detail and information about the Audit Function including:

- Background and historical information
- Internal Audit Department
- Audit Committee
- Audit Committee Financial Advisor
- External Financial Auditor
- Types of Audits performed by IA
- The Annual Audit Plan
- Best Practices for the Audit Function as recommended by:
 - Government Finance Officers Association (GFOA)

- Institute of Internal Auditors (IIA)
- American Institute of Certified Public Accountants (AICPA)
- Additional Reference Material

IEUA has adopted best practices in structuring and establishing an effective Audit Function. The report that follows provides details about the Audit Function at IEUA with greater discussion focused on the Internal Audit Department.

The documents attached are additional reference material and relevant information gathered from best practice guidance related to the Audit Function, including the following:

- AICPA Audit Committee Toolkit
 - A toolkit for evaluating the various resources of the Audit Committee
- The Charters: Audit Committee and Internal Audit Department Charters
- 2004 Board Letter regarding the establishment of the Audit Function
- The IIA's Guidance on the Audit Committee
- GFOAs best practice guidance/information
- AICPA's best practice guidance/information
- Association of Certified Fraud Examiner's (ACFE) Report to the Nations on Occupational Fraud and Abuse

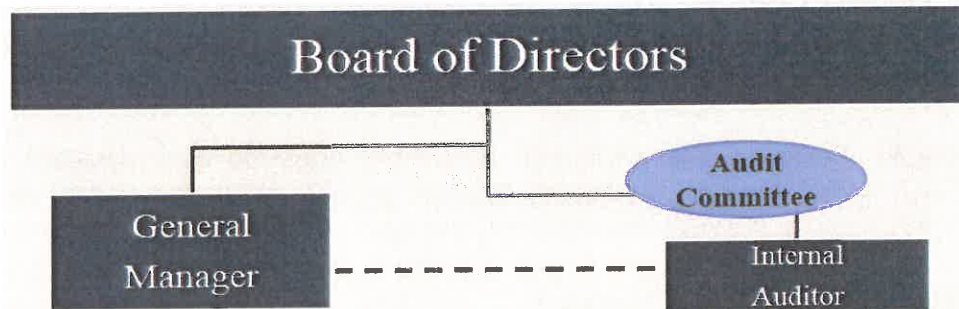
The Internal Audit Department appreciates the opportunity to provide this comprehensive report on the Audit Function of IEUA and request direction, feedback and/or changes for the fulfillment of audit responsibilities and future Audit Committee Meetings. The Manager of Internal Audit is available to provide additional information or answer any questions.

This report describing the IEUA Audit Function is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by describing the functions, roles, authority and responsibilities of the Audit Committee of the Board of Directors, the Internal Audit Department, the External Financial Auditors and the Audit Committee Financial Advisor and their responsibilities assisting the Agency in achieving its goals.

TV:ps:sn

The Audit Function

This diagram illustrates the reporting lines of the Internal Auditor.



Background

IEUA's Internal Audit Department was established by the Agency's Board of Directors on April 21, 2004. The Board of Directors asked Agency staff to conduct research and provide recommendations on the best structure for the Internal Audit Department and the Audit Committee. Based on the research completed and recommendations by staff, the Board approved the "best practices" model suggested by the Government Finance Officers Association (GFOA), the Institute of Internal Auditors (IIA), and the Agency's General Counsel. This has remained the model since its establishment:

- An Audit Committee composed of three committee members, two members of the Board of Directors and an Audit Committee Member, with no voting rights, to serve as the Financial Expert with experience in conducting financial audits, as suggested by best practices.
- The position of Internal Auditor reporting functionally to the Board through the Audit Committee and reporting administratively to the General Manager.

The Board report presented in 2004, documents that this structure was recommended and established:

"to address this increase in responsibility" (from increased auditing requirements and reporting of expenditures for special districts by the California Legislature), "to ensure administrative and financial accountability to standards required by federal and state regulatory agencies and bondholders, to better define staff's administrative responsibilities, and to provide the Board with a consistent means of monitoring the Agency's financial responsibilities".

GFOA recommends that every government consider the feasibility of establishing a formal internal audit function (GFOA recommended practice, 1997). Further, GFOA recommends the internal audit function be established formally by charter. IEUA has adopted best practices and has established the Internal Audit Department by Board-approved Charter.

The Internal Audit Department is currently staffed with one full-time Manager of Internal Audit and two full-time Senior Internal Auditors. As required by the Board-approved Charter, the Manager of Internal Audit, reports functionally to the Board through the Audit Committee, and administratively to the General Manager. This independent reporting line establishes the Internal Audit Department as a separate, independent entity to assist management in achieving organizational goals and to assist the Board in fulfilling its oversight responsibilities. This reporting line supports IA and ensures that audit work is performed objectively and independently.

The Role of the Internal Audit Department

Mission Statement

The Internal Audit Department seeks to improve the operations of the Agency by providing unbiased and objective assessments and recommendations to ensure Agency resources are efficiently and effectively managed in order to achieve Agency goals and objectives. The Internal Audit Department will help the Agency achieve its goals and objectives, improve operations, and instill confidence among its employees and the citizens it serves by providing independent, objective assurance and consulting services and provide management and the Board of Directors with recommendations to:

- *Promote and strengthen a sound control environment.*
- *Improve Agency risk management, control and governance.*
- *Promote the Agency's vision and mission through a high degree of professionalism.*
- *Establish adequate policies and procedures and to comply with them.*
- *Encourage efficient use of Agency resources.*
- *Protect and safeguard Agency assets.*
- *Mitigate risks related to fraud, waste and abuse.*
- *Hold staff accountable for the resolution of audit recommendations.*

Internal Audit Department Charter

The purpose, authority and responsibilities of the Internal Audit Department are documented in the Board-approved Charter. The Internal Audit Department Charter states that the purpose of the Internal Audit Department is to assist the Board of Directors and the Audit Committee in fulfilling their oversight responsibilities for financial reporting, internal controls and compliance with legal and regulatory requirements applicable to Agency operations and to provide objective assurance about Agency operations. Those responsibilities are fulfilled through the various planned audit projects, discussions with Executive Management, the External Financial Auditor and the Audit Committee Financial Expert, as well as discussions with the Audit Committee. The Charter is provided for Audit Committee and Board review and/or discussion each year. The Internal Audit Department evaluates changes in best practices and suggestions by the External Financial Advisor and the External Auditor in making changes/edits to the Charters. The Charters are posted on the Internal Audit Department webpage on the Agency's intranet website.

Annual Audit Plan

The Annual Audit Plan is a flexible plan of audit projects proposed for the succeeding year. The proposed audit projects are selected based on risks considered, requests by management and inquiries of the Agency's management, External Auditors, the Audit Committee Advisor, general counsel and others. The plan is intended to provide information about the proposed scope of work for each project. The plan is meant to address risk areas and to evaluate and contribute to improving effectiveness of operations. The Annual Audit Plan is submitted for Audit Committee review and discussion Board approval in June. The current Annual Audit Plan in effect, can be found under Board-approved documents and located on the Internal Audit Department webpage on the Agency's intranet website.

Types of Audits

The Internal Audit Department performs operational audits of the various business units of the Agency. An operational audit is designed to evaluate an activity's effectiveness and efficiency of operations. IA's operational audits also incorporate elements of program, financial and compliance audits to evaluate financial transactions and overall compliance of the activity with specific requirements. Prior to finalizing an audit, discussions take place between IA and the auditee about the audit results and resulting audit findings and recommendations. Then, the auditee has opportunities to provide resolutions, responses or additional information prior to IA finalizing the audit report. Results of audits are documented in a formal audit report and discussed during Audit Committee meetings. Auditees can provide a written response and include corrective action plans. Any resulting open/outstanding audit recommendations are followed-up as scheduled through the Annual Audit Plan until full implementation is achieved or alternate controls are incorporated.

IA has completed audits in multiple areas of the Agency, including:

- Warehouse Operations
- Human Resources
- Finance & Accounting
- Inter-company Receivables
- Construction Management
- Contracts and Procurement
- Laboratory
- Environmental Compliance
- Pre-Treatment and Source Control
- Integrated Systems Services
- Vehicle Operational Audits
- Energy/Utility Bills
- Regional Contract Audits of the 7 contracting agencies

- Water Connection Fee
- Miscellaneous projects and special requests

All audit reports are discussed during the regular Audit Committee Meetings and can be accessed through the Agency Information Management (AIM), the Agency's intranet site, also available on the Internal Audit Department webpage on AIM, through the Board Reports on the main IEUA webpage or available upon request from the Manager of IA.

Standards

In performing audit work, internal auditors abide by the Code of Ethics and the *Standards* as promulgated by the Institute of Internal Auditors (IIA) as documented in the International Professional Practice Framework (IPPF) or "Red Book."

BEST PRACTICES RECOMMENDATIONS FOR INTERNAL AUDIT STRUCTURE

Government Finance Officers Association (GFOA)

- *"Every government should consider the feasibility of establishing a formal internal audit function because such a function can play an important role in helping management to maintain a comprehensive framework of internal controls. As a rule, a formal internal audit function is particularly valuable for those activities involving a high degree of risk (e.g., complex accounting systems, contracts with outside parties, a rapidly changing environment). If it is not feasible to establish a separate internal audit function, a government is encouraged to consider either 1) assigning internal audit responsibilities to its regular employees or 2) obtaining the services of an accounting firm (other than the independent auditor) for this purpose;*
- *The internal audit function should be established formally by charter, enabling resolution, or other appropriate legal means;*
- *It is recommended that internal auditors of state and local governments conduct their work in accordance with the professional standards relevant to internal auditing contained in the U.S. General Accounting Office's publication Government Auditing Standards, including those applicable to the independence of internal auditors;*
- *At a minimum, the head of the internal audit function should possess a college degree and appropriate relevant experience. It also is highly desirable that the head of the internal audit function hold some appropriate form of professional certification (e.g., certified internal auditor, certified public accountant, certified information systems auditor) ; and*

- *All reports of internal auditors, as well as the annual internal audit work plan, should be made available to the government’s audit committee or its equivalent.”*

American Institute of Certified Public Accountants (AICPA)

“First and foremost, the internal audit department will understand that its responsibilities are primarily to the audit committee. A strong internal audit function may also include audit committee oversight of the internal audit group’s budget approval process and its policies regarding hiring, evaluation, training, and termination of internal audit staff. Terminating or transferring high level internal audit personnel will be ultimately determined by the audit committee.

Executive sessions with the head of the internal audit function at every audit committee meeting provide the audit committee a unique opportunity to engage in candid discussions with him or her about the possible risk of management override of internal control and any indications of improper conduct by senior management.

The audit committee, by understanding and assisting in developing the internal auditors’ annual audit plan, will influence the internal auditors’ agenda by directing the plan’s emphasis to areas of particular interest to the audit committee. These areas might include fraud risks—particularly matters that surfaced during the brainstorming session—and controls over judgments and estimates and key information processes. A properly directed internal audit staff can serve as the “eyes and ears” of the audit committee.”

The Institute of Internal Auditors (IIA)

“Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization’s operations. It helps an organization accomplish its objectives by bringing a systematic disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Reporting to executive management and having direct access to the audit committee well positions the internal audit activity within an organization. Internal audit independence is furthered by periodic private meetings between the audit committee and the CAE, during which time sensitive issues are discussed without management’s presence.”

The Audit Committee

The IEUA Audit Committee structure follows recommended best practices and professional standards. The April, 2004 Board report included the following structural

recommendation about the creation of an Audit Committee as a separate committee of the Board of Directors:

“An Audit Committee of the Board of Directors be established to oversee the audit and grants’ responsibilities of the current Chief Financial Officer position. The Committee would be responsible to meet at least quarterly with the Agency’s Internal Auditor and Agency staff, for overseeing the acquisition of the Agency’s outside Auditor, developing the scope of work for the annual audit, approving the annual audit work plan, directing special internal audits, reviewing and approving the internal auditing work plans, evaluating the performance of the internal audit activities, and providing policy direction to the Agency’s Audit and Grants Department. The Audit Committee would meet at least quarterly with the Internal Auditor to review work plans, audit activities and the draft/final audit reports. The Audit Committee would submit all audit management reports to the Board for review and policy direction, as appropriate.”

This recommendation was developed based upon research performed by IEUA staff. IEUA staff discussed the structure of the Audit Committee and Internal Audit Department with the “Agency’s bond counsel, investment banker, the External Auditor, The Agency’s General Counsel, and the Metropolitan Water District’s Chief Financial Officer who suggested the proposed reorganization was in the best interests of the Agency.”

The Audit Committee meets quarterly and is comprised of three members: two Board Members and one External Financial Expert. The Manager of IA is responsible for preparing all agenda items for the Audit Committee meetings.

Audit Committee Charter

The Audit Committee Charter documents the purpose, composition, authority and responsibility of the Audit Committee. The Charter is reviewed and discussed annually and any changes must be approved by the Board. The Charter follows best practice recommendations by GFOA, IIA and AICPA. The Charter also states that the Audit Committee shall delegate fulfilling those responsibilities to the Internal Audit Department. Those responsibilities are fulfilled through various evaluations and discussions with Executive Management, the Internal Auditor, the External Auditor and the Audit Committee Financial Advisor.

BEST PRACTICES RECOMMENDATIONS FOR AUDIT COMMITTEE STRUCTURE

Government Finance Officers Association

- *“The governing body of every state and local government should establish an audit committee or its equivalent.*
- *The audit committee should be . . . made directly responsible for the appointment, compensation, retention, and oversight of the work of any independent accountants engaged for the purpose of preparing or issuing an independent audit report or performing other independent audit, review, or attest services.*

- *All members of the audit committee should be members of the governing body.*
- *It is the responsibility of the audit committee to provide independent review and oversight of a government's financial reporting processes, internal controls and independent auditors.*
- *The audit committee should have access to the reports of internal auditors, as well as access to annual internal audit work plans."*

American Institute of Certified Public Accountants

"Government entities are faced with ongoing challenges related to the governance of their organization, risks associated with achieving their organization's objectives, and compliance with revised and emerging laws and regulations. Responsibilities are ultimately identified by the governing body and assigned to various governing committees, including the audit committee . . .

The audit committee assists the governing body in its oversight of

- *integrity of the organization's financial statements;*
- *internal control including internal control over financial reporting;*
- *independent auditor's qualifications, independence, and performance;*
- *internal audit function's qualifications, independence, and performance;*
- *the organization's risk management and overall governance process; and*
- *the organization's ethics and compliance program, which includes legal and regulatory requirements."*

The Institute of Internal Auditors

"The cornerstones of effective governance are the board of directors, executive management, the internal auditors, and the external auditors. No single committee of the board is more focused on or better in tune with governance than the audit committee.

What is the audit committee's role in governance? In a nutshell, the audit committee should provide oversight of financial reporting, risk management, internal control, compliance, ethics, management, internal auditors, and the external auditors.

Some detailed audit committee responsibilities include:

- *Ensuring that financial statements are understandable, transparent, and reliable.*
- *Ensuring the risk management process is comprehensive and ongoing, rather than partial and periodic.*
- *Helping achieve an organization-wide commitment to strong and effective internal controls, emanating from the tone at the top.*
- *Reviewing corporate policies relating to compliance with laws and regulations, ethics, conflicts of interest, and the investigation of misconduct and fraud.*

- *Reviewing current and pending corporate-governance-related litigation or regulatory proceedings to which the organization is a party.*
- *Continually communicating with senior management regarding status, progress, and new developments, as well as problematic areas.*
- *Ensuring the internal auditors' access to the audit committee, encouraging communication beyond scheduled committee meetings.*
- *Reviewing internal audit plans, reports, and significant findings.*
- *Establishing a direct reporting relationship with the external auditors."*

Role of the Audit Committee Advisor/Financial Expert

The April, 2004 recommendation that established the Audit Committee and the Internal Audit Department did not discuss the role of an external financial expert in providing counsel and advice to the Audit Committee. The Audit Committee Advisor/Financial Expert serves as a resource to the Audit Committee, the Internal Audit Department and Executive Management. The Financial Advisor serves as a checks and balance for the Internal Audit Department for the Audit Committee and serves as an interpreter for the Audit Committee. Professional best practices provide the following:

BEST PRACTICES RECOMMENDATIONS FOR AUDIT COMMITTEE FINANCIAL EXPERT

Government Finance Officers Association

"The audit committee also should have access to the services of at least one financial expert, either a committee member or an outside party engaged by the committee for this purpose. Such a financial expert should through both education and experience, and in a manner specifically relevant to the government sector, possess 1) an understanding of generally accepted accounting principles and financial statements; 2) experience in preparing or auditing financial statements of comparable entities; 3) experience in applying such principles in connection with the accounting for estimates, accruals, and reserves; 4) experience with internal accounting controls; and 5) an understanding of audit committee functions"

American Institute of Certified Public Accountants

"If no individual member of the audit committee possesses the attributes required for financial expertise, and the committee members collectively do not possess such attributes, two options might be considered:

- *Engage a financial professional to provide financial expertise as a consultant to the audit committee. Such an individual must otherwise be independent with respect to*

the entity (that is, must have no other financial arrangements with the government entity).

- *Pursue a training program for audit committee members to develop the financial expertise. Such training can include participation in professional development classes or programs offered by the AICPA, associations, or the specific sector in which the government entity participates, or in-house training programs led by members of the government entity's financial management team."*

The Institute of Internal Auditors

"The audit committee charter should define membership requirements, include a provision for a financial expert, allow for yearly reviews and changes . . . "

IEUA has contracted with Travis C. Hickey, CPA consultant with Rogers, Anderson, Malody, and Scott, LLP to be the Audit Committee Advisor. Over the past nine years, Mr. Hickey has been a valuable resource to the Audit Committee and the Internal Audit Department by providing consulting and advisory services, along with professional audit advice and information.

Role of the External Financial Auditor

State law and the Agency's Fiscal Ordinance requires that an independent certified public accountant audit the Financial Statements of the Agency. The purpose of a financial audit is to demonstrate that the Agency's financial statements were prepared in conformity with generally accepted accounting principles in the United States of America (GAAP), as set forth by the Governmental Accounting Standards Board (GASB). Responsibility for both the accuracy of the presented data, and the completeness and fairness of the presentation, including all disclosures, rests with the management of the Agency. The role of the External Auditors is also to evaluate the adequacy and accuracy of the accounts, test internal controls and complete the audit in accordance with generally accepted auditing standards. The auditors are only providing an opinion as to the representations provided by the Agency. The purpose of the annual financial audit is to receive an independent audit opinion as to the fairness of the financial statements. The opinion is relied upon by readers of the financial statements such as lenders, rating agencies and other stakeholders. The scope of the audit and the materiality threshold set for the audit testing and procedures are determined based on the auditor's risk assessment, professional guidelines and their professional judgment. The audit is not meant to detect fraud. The External Financial Auditors must be licensed as Certified Public Accountants in the State of California and follow a rigorous set of guidelines established by the American Institute of Certified Public Accountants for the performance of financial audits. The Agency currently has a contract with Lance, Soll & Lunghard, LLP, located in Brea, CA for financial auditing and single audit services.

Charters

The professional standards describe two separate charters that provide guidance to the Internal Audit function. One is the Internal Audit Department's charter that defines the activity's purpose and the other is the Audit Committee's charter which provides information about the Committee's governance responsibilities, goals and purpose. IEUA follows best practices and has adopted both Charters for the IAD and the Audit Committee.

Internal Audit Department Charter

The IPPF Standards states that "the internal audit activity must be formally defined in an internal audit charter, consistent with the "Mission of Internal Audit and the mandatory elements of the Framework". The IPPF Standards clarify this responsibility by stating:

"The internal audit charter is a formal document that defines the internal audit activity's purpose, authority and responsibility. The internal audit charter establishes the internal audit activity's position within the organization, reporting relationship with the board; authorizes access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal audit activities. Final approval of the internal audit charter resides with the board."

BEST PRACTICES RECOMMENDATIONS FOR INTERNAL AUDIT CHARTER **Government Finance Officers Association**

"The internal audit function should be established formally by charter, enabling resolution, or other appropriate legal means."

American Institute of Certified Public Accountants

The AICPA also recommends that one aspect of the audit committee's oversight responsibilities for Internal Audit includes: *"Approve the internal audit department charter."*

Audit Committee Charter

BEST PRACTICES RECOMMENDATIONS FOR AUDIT COMMITTEE CHARTER

Government Finance Officers Association

"The audit committee should be formally established by charter, enabling resolution or other appropriate legal means and . . . the written documentation establishing the audit committee should proscribe the scope of the committee's responsibilities, as well as its structure, processes, and membership requirements. The audit committee should itself periodically review such documentation, no less than once every five years, to assess its continued adequacy."

American Institute of Certified Public Accountants

“Specific responsibilities assigned to an audit committee are set forth in an audit committee charter . . . that is approved by the governing body. An audit committee charter should address the audit committee process, procedures, and responsibilities. Audit committee responsibilities can vary by government entity due to factors such as size of the entity, the type of entity, and the complexity of the government entity’s service or business model.”

American Institute of Certified Public Accountants

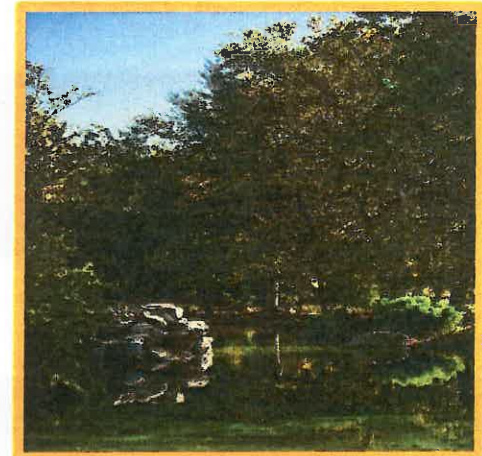
“The audit committee’s charter is its blueprint for operations. Highly customized to best meet the needs of an organization’s industry, mission, and culture, the charter should clearly delineate audit committee processes, procedures, and responsibilities that have been sanctioned by the entire board.”

The document goes on to provide specific recommendations for what to include in an Audit Committee Charter and provides a sample document for reference.

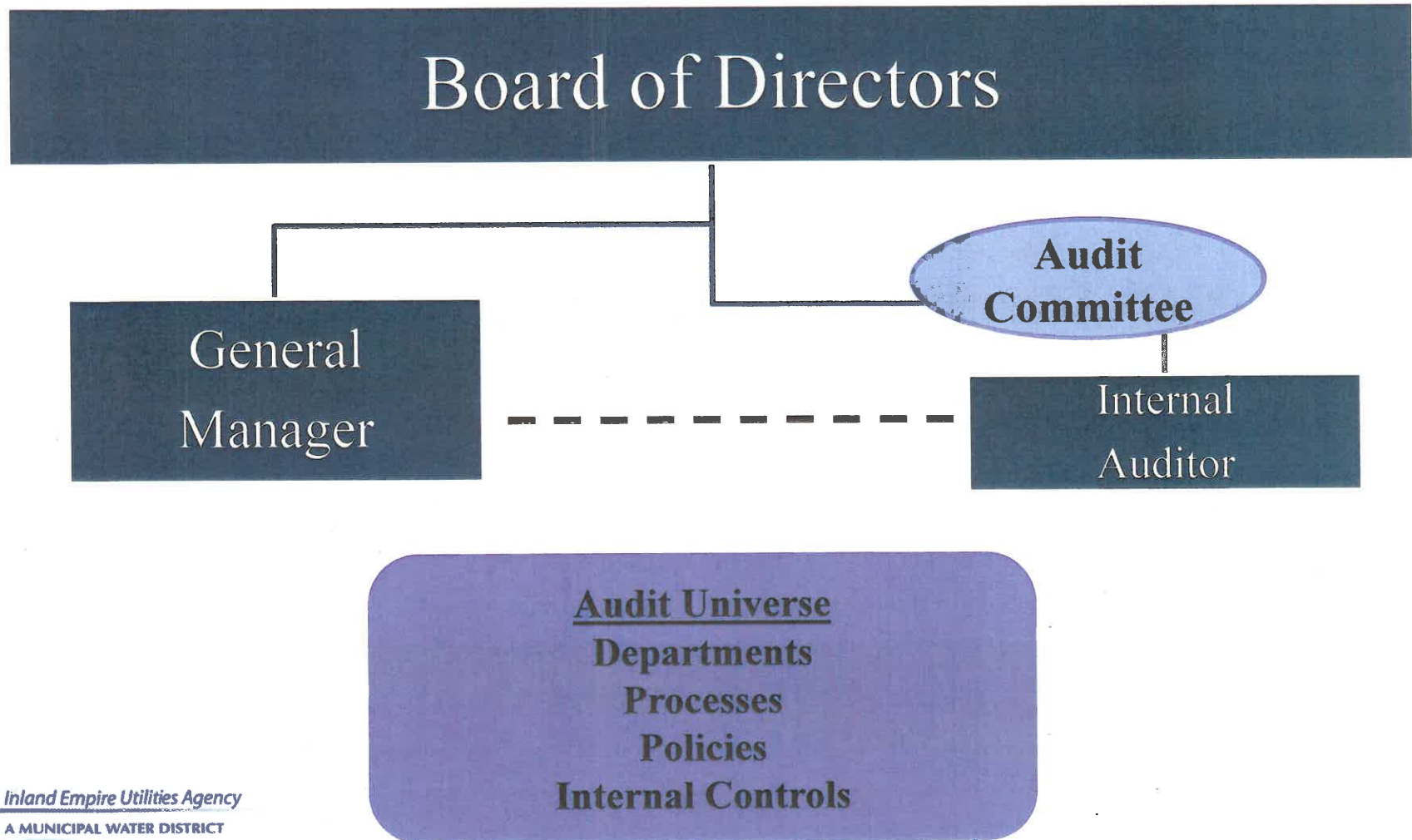
The Internal Audit Department appreciates the opportunity to provide this comprehensive report on the Audit Function of IEUA.



The Audit Function at Inland Empire Utilities Agency



The Audit Function & The Reporting Line for the Internal Auditor



The Audit Function & Audit Committee Resources



- Guidance over audit activities
 - GFOA: Government Finance Officers Association
 - IIA: Institute of Internal Auditors
 - AICPA: American Institute of Certified Public Accountants

Auditor Contracts & Fees

YEAR	2016	2017	2018	2019
Audit Committee Advisor	\$6,190	\$6,190	\$6,190	\$6,190
External Financial Auditor	\$37,100	\$37,750	\$38,430	\$39,680
Total	\$43,290	\$43,940	\$44,620	\$45,870

Charter Requirements



The Role of the Internal Audit Department

- Serve as the “Eyes and ears” of the Board
- Objective and independent evaluations and reviews
- Assist the Agency in achieving its goals and objectives
- Assess internal controls
- Provide assurance on processes and procedures
- Promote strong ethical culture
- On-going monitoring and compliance
- Assist in safeguarding assets
- Raise any potential red flags
- Make recommendations to improve operations
- Follow up on prior recommendations
- Communicate results & provide Audit Reports

Types of Audits Performed by Internal Audit



Annual Audit Plan

- Long Range Audit Planning – Additional Audit Areas
 - Payroll & Time System
 - Accounts Payable – Review of Credit Cards & P-cards
 - Construction Contracts – award through final payment
 - Recycled Water Program
 - Accounts Payable - Duplicate Payments/Late Payments
 - Inter-Fund Transfers and Reserve Requirements
 - Capital Projects
 - Asset Management
 - Operations

Internal Audit Department Responsibilities:

- Operational Audits
- Make recommendations to improve operations
- Follow-ups Reviews
- Agency Policy reviews
- Special Requests
- Quality Control Review of CAFR, Disclosures and GFOA recommendations
- Ethics Point
- Annual Audit Plan
- RFP for External Financial Audit Services
- Charters & Standard Operating Procedures
- Continuous Professional Development
- IAD Website on AIM



Provide direction for Audit Responsibilities and future Audit Committee Meetings

This workshop is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by describing the functions, roles and responsibilities of the Internal Audit Department and providing an overview of the components which make up the Audit Function.

Audit Committee

INFORMATION
ITEM
2E



Date: March 20, 2019

To: The Honorable Board of Directors

From: Teresa Velarde, Manager of Internal Audit

Committee: Audit

03/11/19

Manager Contact: Teresa Velarde, Manager of Internal Audit

Subject: Internal Audit Department Quarterly Status Report for March 2019

Executive Summary:

The Audit Committee Charter requires that a written status report be prepared and submitted each quarter. The Internal Audit Department Status Report includes a summary of significant internal and external audit activities for the reporting period.

During this quarter, Internal Audit (IA) staff worked primarily on the Water Connection Fee audit, performed a follow-up review for one recommendation from the Southern California Edison Utility Payments Follow-Up audit and one recommendation for the Accounts Receivable Follow-Up audit - Watermaster. Additionally, IA worked on audit projects that are in progress and on-going/required items such as the budget process tasks, and completed training as required by the IA Department's Charter, among other duties.

IA continues to assist with any requests for audit work, review of Agency policies and procedures and recommendations for internal controls as well as work on routine audit projects as specified in the Annual Audit Plan. The attached report provides information and highlights of the audit projects.

Staff's Recommendation:

This is an information item.

Budget Impact Budgeted (Y/N): N Amendment (Y/N): N Amount for Requested Approval:

Account/Project Name:

N/A

Fiscal Impact (explain if not budgeted):

N/A

Prior Board Action:

On June 20, 2018, the Board of Directors approved the Fiscal Year 2018/19 Annual Audit Plan. The plan was in accordance with auditing standards and the Charter requirements.

On December 19, 2018, the Board of Directors reconfirmed the approved Audit Committee and the Internal Audit Department Charters.

Environmental Determination:

Not Applicable

Business Goal:

The Status Report is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by describing IA's progress in providing independent evaluations and audit services of Agency financial and operational activities and making recommendations for improvement, to promote a strong ethical and internal control environment, safeguarding assets and fiscal health, providing recommendations to improve efficiencies and to assist management in achieving organizational goals and objectives.

Attachments:

Attachment 1 - Internal Audit Department Status Report for March 2019

Internal Audit Department Status Report for March 2019

Projects Completed This Period

Project: **Water Connection Fees Audit**

Scope:

To purpose of the audit is to:

- Ensure adequate internal controls are in place
- Determine compliance with the Agency's Ordinance and Resolution
- Evaluate the collection and recognition of revenue
- Determine whether there are procedures to reconcile fees collected
- Determine compliance with Agency policies and procedures
- Identify opportunities for improvements

Status: **Complete**

The Planning and Environmental Resources Department (Planning) has responsibility for processing water connection fee transactions and the Finance and Accounting Department (FAD) has responsibility for ensuring the transactions are recorded in the Agency's financial records. In December 2018, IA provided an interim audit report where we prefaced and discussed the preliminary observations and recommendations. This report is now in final form and the audit report provides recommendations for consideration.

- Streamlining the two systems currently used to track and process transactions to a single-entry process in SAP to eliminate duplication of data entry and the need for continuous reconciliations.
- Update the Agency's Ordinance and Resolution to ensure practices are updated, provide flexibility in payments for developers and address other items noted since the inception of the program as well as update and document Departmental policies and procedures.
- Pursue collection of fees due as permitted under the Board-approved Ordinance.

Detailed observations and recommendations are included in the audit report, presented separately.

Project: **Southern California Edison (SCE) Utility Payments Follow-Up Audit**

Scope:

IA completed a follow-up audit to determine the status of one remaining recommendation provided in the SCE Utility Payments Follow-Up audit, dated August 29, 2013.

Status: **Complete**

The one outstanding recommendation has been fully implemented. The recommendation was related to a SCE charge of approximately \$900/year for the street lighting that is technically the responsibility of the City of Chino, and not IEUA.

The Agency has paid for this expense since the initial construction of the current Headquarters location. During the original audit in 2013, Agency staff had already initiated discussions and was working to transfer the utility account and related expense to the City of Chino. IA reported on this item to assist staff in moving forward on the change. Effective, May 1, 2018, the City of Chino became responsible for the street lighting expense. As of August 1, 2018, the SCE account has now been closed and IA validated that IEUA is no longer billed for these lighting services. This change will generate a savings of approximately \$900/year. Since the item was reported by IA, the Agency incurred and paid approximately \$4,000 for this expense. Since the account is under the responsibility of the City of Chino, this too eliminates any perception that IEUA is subsidizing costs for another organization. A final report is presented under separate cover.

Internal Audit Department Status Report for March 2019

Project: **Accounts Receivable Follow-Up - Watermaster Agreement**

Scope: To evaluate whether the Agency bills and receives payment according to the requirements set forth in the Chino Basin Recharge Master Plan Agreement (O&M agreement).

Status: **Complete**

IA evaluated the status of the one remaining recommendation for the Agency to bill and receive payment for the reimbursement of the Operations & Maintenance costs (O&M) from Watermaster "in advance" of each quarter. In the original August 2011 audit, IA noted that billing was completed by IEUA's FAD staff **after** the quarter and payments were received on average between 17 days and 60 days **after** the start of the quarter for FY 2008 to 2010. Billing and collecting payment after the quarter begins is not in agreement with the contract requirements. FAD responded that efforts and controls would be implemented to ensure compliance with the agreement. IA performed a follow up review in 2015 and noted billing continues to be on or after the start of the quarter with payment received from 28 to 52 days **after** the start of the quarter for FY 2011 to 2015.

In the 2019 follow-up review, IA evaluated the three fiscal years from FY2017 to FY2019 (including the FY currently in progress) and noted that payments were received from Watermaster from 4 days early and up to 80 days late and on average (for each FY) from 7 days to 25 days **after** the start of the quarter. Over the three years evaluated 8 of 11 payments were received **after** the start of the quarter and the overall average was 16 days after the start of the quarter. FAD has made improvements in billing Watermaster "in advance" of the quarter. however, IA identified instances where billing and payment continues to be on or after the start of the quarter. This does not comply with the terms of the agreement. IA is currently working with FAD to determine whether there are circumstances that prevent billing and collecting prior to the quarter, or if there are additional controls that can be incorporated to ensure billing and receipt of payment prior to the start of the quarter. As a result, additional time is required to address the original recommendation. Therefore, IA has restated the recommendation as a 2019 Recommendation. IA will continue to monitor this as scheduled through the Board-approved Annual Audit Plan or until FAD provides a response and accepts any potential risk. A final report is submitted under separate cover.

Project: **Report on Outstanding Recommendations as of March 2019**

Scope:

The Internal Audit Department Charter requires IA to follow-up on the status of outstanding recommendations to determine if corrective actions have been implemented. The follow-up reviews are scheduled through the Board-approved Annual Audit Plan. Executive Management supports the implementation efforts of the recommendations previously provided and/or the development of alternative controls to address the original risks identified.

Status: **Complete** - Status of outstanding recommendations as of March 2019.

The table below provides the number of recommendations outstanding as of this Status Report. Additional details about each of the outstanding recommendations is submitted with the Annual Audit Plan in June each year. This summary provides an update on the status of follow up audits and the related outstanding recommendations. It includes new recommendations provided during this fiscal year as well as considers any recommendations cleared during the year. Follow up reviews are part of the on-going monitoring activities IA performs according to the requirements of the IAD Charter. A follow up review is typically scheduled between 12 – 18 months from the date of the original audit, to allow time for full implementation. If a recommendation is deemed not to be implemented, the recommendation remains outstanding or alternate controls to mitigate any risks are evaluated to determine if the risk has been addressed and the recommendation is no longer applicable. A follow up review is also scheduled sooner, if requested by the Audit Committee or Executive Management. The audited business units are encouraged to submit additional information for IA review if they determine the recommendation has been satisfied.

Internal Audit Department Status Report for March 2019

Area Audited	Report Issued Date	No. of Recs. Remaining to be Verified by IA*	Planned Follow-Up
Payroll Audit	August 24, 2010	1	Annually
Intercompany Receivables - Watermaster	August 30, 2011	1	FY 2019
SCE Utility Payments	August 28, 2013	1	FY 2019
Accounts Payable Follow-Up	August 29, 2013	9	FY 2019
Vehicle Security Procedures	March 3, 2014	2	FY 2020
Follow-Up – IT Equipment Audit – ISS	February 29, 2016	2	FY 2020
Master Trade Contracts	September 1, 2016	6	FY 2020
Follow-Up – IT Equipment Audit – FAD	December 5, 2016	6	FY 2020
Audit of Master Services Contracts	December 5, 2016	3	FY 2020
2017 Petty Cash Audit & Follow-Up Review	June 5, 2017	7	FY 2020
Water Use Efficiency Programs Audit	June 5, 2017	6	FY 2020
Contracts and Procurement Follow-Up Audit	August 30, 2017	1	FY 2020
Payroll Operations Audit	August 30, 2017	6	FY 2020
Procurement Card Audit	March 1, 2018	7	FY 2021
Wire Transfers Audit	March 1, 2018	5	FY 2021
Garden in Every School	May 31, 2018	7	FY 2022
Warehouse Annual Physical Inventory – IA Inventory Observation Report	August 22, 2018	4	FY 2022
Inter-fund Transactions Audit	August 30, 2018	3	FY 2022
Agency Vehicle Operational Follow-up audit: Review of Vehicle Inventory Procedures	November 29, 2018	3	FY 2022
Total Outstanding Audit Recommendations		80	
Recommendations related to the Regional Contract Review (these recommendations are planned for full implementation with the renegotiation of the Regional Contract IA will not follow up on these items until the renegotiation has been finalized)			
Regional Contract Review – Final Audit Report	December 16, 2015	31	Pending – Renegotiation of the Regional Contract

*Table above does not include the status of and/or any new recommendations resulting from the projects completed during this quarter (as noted in this Status Report). The status of those recommendations will be added to this table once all items have been received by the Audit Committee and the Board of Directors.

Project: Budget Process for Internal Audit Department

Scope: To prepare the Internal Audit Department's budget for Fiscal Years 2019/20 and 2020/21.

Status: Complete

As required by Fiscal Ordinance #102, the Agency adopts a biennial budget, which is a strategic and financial plan that estimates the revenues and expenses to be incurred by the Agency during the next two consecutive fiscal years. The biennial budget is comprised of all the Agency's individual department budgets and projects and presented as one comprehensive budget to be adopted by the Board of Directors.

This year, Sapna Nangia, Senior Internal Audit, took a hands-on role to learn the Internal Audit Department's budget process, attended all information and training sessions and had one-on-one training with the Manager to complete all the required forms and budget documents. This was done 1) as part of goals independently set through her Career Management program, to learn and be more aware of Agency programs and processes and 2) to serve as a back up to the Manager for this process.

As part of the biennial budget preparation process, IA attended several meetings and trainings provided by the Finance and Accounting Department (FAD). The budget is to be completed as required by the guidelines set forth during the budget preparation process as approved by the GM. To complete the IA department's budget, the following reports were completed:

- **Projected costs:** Using SAP, Sapna worked closely with the manager to estimate department controllable expenses, i.e. supplies, training, subscriptions & publications, memberships, and

Internal Audit Department Status Report for March 2019

professional fees, audit fees & other services for the next two fiscal years. Amounts were established for FY 2019/20 and 2020/21 and additional estimates were forecast and projected for the next 10 years (FY 2022 to 2032).

- List of Training/Conference Requests, Subscriptions & Memberships, and Professional Fees & Services: An itemized list was submitted for all planned/proposed expenses related to trainings, conferences, seminars, subscriptions & publications, memberships, and professional services that are expected to be spent during the next 2 fiscal years. The list submitted contained conference/seminar names, the name of the professional association and estimated costs for each to justify the anticipated/planned expense.
- Quarterly Budget Variance: This is a reporting tool that serves as a “Check-in” point and shows the funds that have been expended to-date at each quarter in the fiscal year in comparison to the budget. Throughout the fiscal year, each Agency department must review their budgeted amounts and compare them to the actual amounts that have been incurred (Budget Vs. Actual). Differences were identified, and justifications were noted where necessary.
- Labor Distribution Report: Completed a forecast of staff’s hours to allocate to the various funds and projects. For example, to project the number of hours that will be used by staff for training and/or Safety Tailgate meetings and other programs and projects.

Preparation of the department’s budget is a complex process, but it is beneficial for staff to understand the resources that have been committed and ensure the alignment of the department’s goals and objectives to the Agency’s Top Initiatives, Business Goals and Objectives. IA completed and submitted the above reports to FAD by the required deadlines and answered pertinent questions as adjustments were made as necessary.

Project: Internal Audit Department - Required Continuous Professional Education & Training

Scope:

According to the Internal Audit Department Board-approved Charter and the *International Standards for the Professional Practice of Internal Auditing (Red Book Standards)* Internal Auditors must regularly and continuously work to enhance their knowledge, skills, and other competencies through continuing professional education. During this quarter, staff attended two training meetings and a local seminar.

Status: Complete

One Senior Internal Auditor attended two trainings offered through the Government Finance Officers Association (GFOA), a recognized professional association that represents public finance officials throughout the United States and Canada. GFOA’s mission is to advance excellence in state and local government financial management.

Advanced Governmental Accounting

This was a 2-day training that covered governmental accounting and financial reporting. The topics covered included: capital assets, debt, investments and derivatives, pensions and other postemployment benefits, grants, risk-financing, compensated absences, lease accounting, government pronouncements (i.e., No. 84 - *Fiduciary activities*, No. 86 - *Certain Debt Extinguishment issues*, etc.), and other related topics.

Accounting Academy: An Intensive Introduction to Governmental Accounting, Auditing, and Financial Reporting

This was a 3-day training. The objectives included: generally accepted accounting principles (GAAP) for state and local governments, unique factors that led to specialized accounting and financial reporting for state and local governments, fund accounting, government-wide financial reporting, measurement focus and basis of accounting, categorization and measurement of transactions and events, component units, budgetary reporting, and elements of a comprehensive annual financial report (CAFR).

Internal Audit Department Status Report for March 2019

The two trainings combined provided a total of 40 continuing professional education hours for this IA staff member. Because the Senior Auditor is a Certified Government Audit Professional, 20 hours of training are required each year.

Institute of Internal Auditors San Gabriel Valley Chapter seminar: A Study on Corruption

All IA staff members attended a 1-hour seminar that discussed the causes and warning signs of corruption based on research and findings from the Association of Certified Fraud Examiners (ACFE) 2018 biennial global study on occupational fraud and abuse.

Projects in Process

Project: Assisting with the audit and revision of IEUA's Sewer System Management Plan (SSMP)

Scope:

Assist the Operations Division in completing the State-required 2-year audit and submit for Board approval the revised 5-year SSMP. The SSMP is a state-required plan for any wastewater agency with at least 100 miles of wastewater infrastructure. The plan contains 13 required elements that must be readily available to provide training and serve as a manual/guide to the Agency's employees in the event of a Sewer overflow.

Status: In Progress

IA was asked to assist in the project to review, revise and update the Agency's 5-year SSMP that must be Board approved and submitted to the State. The review includes an audit to determine if goals and the elements within each of the 13 areas were satisfied and met. Additionally, the review is required to revise and update the SSMP to ensure it is a "living document". IA assisted with evaluating the document, conducted interviews, researched information from other SSMPs and guides and provided recommendations, changes and edits to the current version. This document is planned for completion by April 2019. The next steps are finalizing the information and providing a workshop to the Board before requesting full approval.

Project: Fuel Card Program Audit (Voyager)

Scope:

To evaluate the internal controls over the Voyager Fuel Card program to ensure safeguards are in place to protect the Agency from loss, theft, and misuse and to evaluate whether the program meets the requirements of the Agency's policies. In addition, to determine whether the program meets the Agency's business goals and identify opportunities to improve the effectiveness and efficiency of operations.

Status: In Progress

IA met with key representatives from the Operations & Maintenance Department (North), in late January 2019 to kick-off the Voyager Fuel Card audit. At this initial meeting, IA obtained an understanding of the Voyager Fuel Card program and processes, along with receipt of the Internal Control Questionnaire (ICQ) completed by the department. The ICQ provides IA with information about how the Voyager Fuel Card program is currently administered and the control procedures employed and provides a starting point for auditors to develop audit procedures.

IA obtained access to the US Bank Fleet Commander® Online system, an online portal that provides fuel and maintenance data management, access to account information, monthly statements, and customized reporting. Fieldwork will be on-going and includes plans to perform various types of financial analysis on the fuel card data, and review of supporting documentation.

Additionally, IA plans to meet with representatives of the Accounting department to gain an understanding of the review and payment process for the Voyager Fuel Card program. IA will continue to work closely with the Fuel Card administrator and other Agency departments throughout the audit process. Any items requiring attention will be discussed with the departments before finalizing the audit tests.

The Voyager Fuel Card Audit was proposed for completion in March; however, due to staff scheduling, priorities with the goals/objectives and budget preparation processes and other follow-up audit projects, this

Internal Audit Department Status Report for March 2019

review has been delayed and is now anticipated to be completed by June 2019. Additional delays were caused due to meeting scheduling conflicts and having audit access to the system for view and report access.

Project: **Accounts Payable Follow-up audit**

Scope:

IA is completing a follow-up evaluation to determine the status of 7 of the 9 outstanding recommendations from the Accounts Payable Audit Report completed on August 29, 2013. FAD is responsible for the implementation of these recommendations. The 2 recommendations that have been deferred pertain to Agency policies that are not the responsibility of FAD.

Status: **In Progress**

IA is currently in the initial planning and investigation phases of this project. IA has met with FAD staff to discuss the current status of the recommendations and obtained documentation of FAD desk policies. IA has also obtained information from BIS about SAP roles and responsibilities. IA will perform additional follow-up procedures to verify whether the recommendations have been implemented and/or alternative controls have been established to address the original risks that were identified.

Planned/Future/Additional Projects

Project: **Recycled Water Program Revenue Audit**

Scope:

Recycled water revenue in FY 2016/17 was almost \$16.4 million. An audit of this area would determine the internal controls over revenue recognition and identify any additional revenue due the Agency. The Finance and Accounting and the Planning departments will be the primary contact departments. This was a request by the Audit Committee to move this audit up in priority. After the conclusion of the Voyager Audit and the Accounts Payable Audit, IA will focus on this review. Anticipated for completion by September 2019.

Project: **Annual Audit Plan**

Scope: The Board approved Charter requires that IA submit for review and approval an Annual Audit Plan of proposed and plan audit projects for the year. IA will request input and ideas for future audit projects from the Audit Committee, the External Auditor, the Audit Committee Advisor, the General Manager, Executive Management, Department Managers and General Counsel. IA also relies on professional audit trends to determine audit areas. IA also completes a general risk assessment about Agency risk areas to propose audit projects. A complete Annual Audit Plan is submitted for Audit Committee and Board of Directors approval in June each year along with a detailed report of all outstanding audit recommendations that require IA follow up review and evaluation.

Project: **Management Requests**

Scope: Assist Agency Management with requests for analysis, evaluations and verification of information, assist with the interpretation of policies and procedures, and/or provide review and feedback on new policies or procedures. These services are provided according to the IA Charter, the Annual Audit Plan, and best practices. The management request projects are short-term projects, typically lasting no more than 60 – 75 hours each where IA determines it has the necessary staff, skills and resources to provide the requested assistance without having to delay/defer scheduled audits and priority projects. The scope of each review is agreed upon between the department manager requesting the evaluation, review, analysis or assistance, the Manager of IA and when deemed appropriate by Executive Management.

During this quarter, IA was working on the following "Management Requests":

- Continue to assist with requests related to the findings and recommendations from the Regional Contract Review.

Internal Audit Department Status Report for March 2019

- Continued to assist with policy language interpretation.
- Participated in Safety Committee and IT Security Committee

Project: Special Projects

Scope:

Perform special reviews and projects including analyzing transactions, evaluating documents and policies, verifying information, assisting with interpretation of Agency Policies or other required procedures, and providing recommendations and feedback on results of the analysis, engaging necessary assistance if and/or when necessary, reporting to the General Manager and the Audit Committee. These services are provided according to the IA and Audit Committee Charters, the Annual Audit Plan, and/or best practices.

Special Projects can be short or long-term projects, typically requiring more than 80 hours of staff time and requiring setting aside or delaying work on scheduled audit projects. The scope of the review is not generally known, and the work must be handled with the highest degree of confidentiality and care, as with all audit projects. Special Projects are usually considered highly confidential.

Internal Audit Department Staffing

The Internal Audit Department is staffed as follows:

- 1 Full-time Manager of Internal Audit
- 2 Full-time Senior Internal Auditors

Internal Audit Staff Professional Development Activities:

As required by the *International Standards for the Professional Practice of Internal Auditing*, and the IA Charter, auditors should continue to enhance their knowledge, skills, and other competencies through continuing professional development. During the past quarter, IA staff has continued to stay abreast of industry developments through attending seminars, review of industry periodicals and participation in free IIA sponsored, on-line webinars.

The Internal Audit Manager is a member of the governing board of the Inland Empire Chapter of the Institute of Internal Auditors (IIA). The governing board sets direction for the chapter.

Two IA members are preparing for the 3-part Certified Internal Auditor (CIA) examination and certification. The CIA is the only globally-recognized certification for internal audit professionals and is the highest certification that can be attained by an internal auditor.

In December 2018, One Senior Internal Auditor passed the third part of the Certified Internal Auditor (CIA) examination and has been awarded the CIA certification.

The Manager of IA has a Master's degree in Public Administration and has obtained the Certification in Control Self-Assessment® (CCSA®). The CCSA® certification program is designed for auditors that have knowledge of CCSA fundamentals, processes and other topics such as risk, controls, and business objectives. The Manager of IA and One Senior Auditor are Certified Government Audit Professionals (CGAP®). The CGAP® certification program is designed for auditors working in the public sector and demonstrates government knowledge and expertise. One Senior Auditor is a Certified Public Accountant (CPA) and Certified Internal Auditor (CIA).

Future Audit Committee Meetings:

- Monday, June 10, 2019 – Regularly Scheduled Audit Committee Meeting
 - Monday, September 9, 2019 – Regularly Scheduled Audit Committee Meeting
 - Monday, December 9, 2019 – Regularly Scheduled Audit Committee Meeting
-