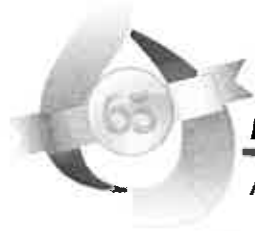


# NOTICE OF MEETING

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OF THE  
**AUDIT  
COMMITTEE**

OF THE  
BOARD OF DIRECTORS  
OF THE



*Inland Empire Utilities Agency*  
A MUNICIPAL WATER DISTRICT

IS SCHEDULED FOR  
**WEDNESDAY, SEPTEMBER 9, 2015**  
**9:00 A.M.**

AT THE ADMINISTRATION HEADQUARTERS  
6075 Kimball Avenue, Building A  
Chino, CA 91708



**AUDIT COMMITTEE MEETING  
INLAND EMPIRE UTILITIES AGENCY\*  
AGENCY HEADQUARTERS, CHINO, CA 91708**

**WEDNESDAY, SEPTEMBER 9, 2015  
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 are 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 ITEMS**

**A. MINUTES**

The Committee will be asked to approve the Audit Committee meeting minutes from June 10, 2015 and June 17, 2015.

**B. FISCAL YEAR 2015/16 ANNUAL AUDIT PLAN**

It is recommended that the Committee/Board:

1. Approve the FY 2015/16 IA Annual Audit Plan; and
2. Direct the Manager of Internal Audit to finalize the FY 2015/16 Annual Audit Plan.

**2. INFORMATION ITEMS**

**A. REGIONAL CONTRACT REVIEW UPDATE - INTERIM REPORT FOR THE CITY OF ONTARIO (WRITTEN)**

**B. FOLLOW UP ON INTERCOMPANY RECEIVABLES (WRITTEN)**

- C. EXTERNAL FINANCIAL AND SINGLE AUDIT REQUEST FOR PROPOSAL PROCESS AND AUDIT COMMITTEE FINANCIAL ADVISOR CONTRACT EXTENSION (WRITTEN)
- D. INTERNAL AUDIT DEPARTMENT QUARTERLY STATUS REPORT FOR SEPTEMBER 2015 (WRITTEN)
- 3. GENERAL MANAGER'S COMMENTS
- 4. COMMITTEE MEMBER COMMENTS
- 5. COMMITTEE MEMBER REQUESTED FUTURE AGENDA ITEMS
- 6. 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: SR

**DECLARATION OF POSTING**

I, Stephanie Riley, 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, September 3, 2015.

S. Riley  
Stephanie Riley

**ACTION  
ITEM**

**1A**



**MINUTES  
AUDIT COMMITTEE MEETING  
INLAND EMPIRE UTILITIES AGENCY\*  
AGENCY HEADQUARTERS, CHINO, CA  
WEDNESDAY, JUNE 10, 2015  
9:00 A.M.**

**COMMITTEE MEMBERS PRESENT**

None.

**STAFF PRESENT**

Stephanie Riley, Executive Assistant

**OTHERS PRESENT**

None.

The meeting was called to order at 9:00 a.m. There were no public comments received or additions to the agenda.

The meeting has been closed due to lack of quorum at 9:01 a.m. The Audit Committee is adjourned until June 17, 2015.

Respectfully submitted,

Stephanie Riley  
Recording Secretary

\*A Municipal Water District

**APPROVED: SEPTEMBER 9, 2015**



**MINUTES  
SPECIAL AUDIT COMMITTEE MEETING  
INLAND EMPIRE UTILITIES AGENCY\*  
AGENCY HEADQUARTERS, CHINO, CA  
WEDNESDAY, JUNE 17, 2015  
9:00 A.M.**

**COMMITTEE MEMBERS PRESENT**

Terry Catlin, Chair  
Jasmin A. Hall

**STAFF PRESENT**

Christina Valencia, Chief Financial Officer/Assistant General Manager  
Teresa Velarde, Manager of Internal Audit  
Craig Proctor, Pretreatment and Source Control Supervisor  
Sapna Nangia, Senior Internal Auditor  
Stephanie Riley, Executive Assistant  
Peter Soelter, Senior Internal Auditor

**OTHERS PRESENT**

Travis Hickey, Audit Committee Advisor  
Nitin Patel, White Nelson Diehl Evans

The meeting was called to order at 9:00 a.m. There were no public comments received or additions to the agenda.

**ACTION ITEMS**

The Committee:

- ◆ Approved the Audit Committee meeting minutes of March 11, 2015

**INFORMATION ITEMS**

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

- ◆ White Nelson Diehl Evans Discussion on FY 14/15 Financial Audit
- ◆ Regional Contract Review Update – Interim Report for the City of Chino Hills and the City of Ontario (Draft)
- ◆ Follow up on Outstanding Recommendations – Pretreatment & Source Control
- ◆ Report on Outstanding Recommendations
- ◆ Internal Audit Department Quarterly Status Report for June 2015

**GENERAL MANAGER'S COMMENTS**

None.

**COMMITTEE MEMBER COMMENTS**

None.

**COMMITTEE MEMBER REQUESTED FUTURE AGENDA ITEMS**

None.

Special Audit Committee  
June 17, 2015  
Page 2

With no further business, the meeting adjourned at 10:00 a.m.  
Respectfully submitted,

Stephanie Riley  
Recording Secretary

\*A Municipal Water District

**APPROVED: September 9, 2015**

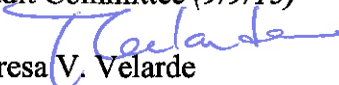
**ACTION  
ITEM**

**1B**





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Date: September 16, 2015  
To: The Honorable Board of Directors  
Through: Audit Committee (9/9/15)  
From:   
Teresa V. Velarde  
Manager of Internal Audit  
Subject: Fiscal Year 2015/16 Annual Audit Plan

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### **RECOMMENDATION**

It is recommended that the Board of Directors:

1. Approve the FY 2015/16 Internal Audit (IA) Annual Audit Plan; and
2. Direct the Manager of Internal Audit to finalize the FY 2015/16 Annual Audit Plan.

### **BACKGROUND**

The Agency's Audit Committee Charter, reconfirmed in December 2013, authorizes the Audit Committee to:

- Approve a flexible Annual Audit Plan using an appropriate risk-based methodology, and submit that plan, as well as any periodic updates, to the Audit Committee for review and approval.
- Implement the approved Annual Audit Plan, including any special tasks or projects requested by Management, the Audit Committee or the Board.

The Audit Plan and Risk Assessment are based on Section 2010 Planning and 2010.A1 of the Institute of Internal Auditors (IIA) *International Standards for the Professional Practices of Internal Auditing (Standards)* which requires:

- The chief audit executive must establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organization's goals.
- The internal audit activity's plan of engagements must be based on a risk assessment, undertaken at least annually. The input of Agency management and the Board must be considered in this process.

The IIA *Standards* define Risk and Residual Risk as follows:

- **Risk** – As the possibility of an event occurring that will have an **impact on the achievement of objectives**. Risk is measured in terms of impact and likelihood and;
- **Residual Risks** – As the risk remaining **after management takes action to reduce the impact** and likelihood of an adverse event, including control activities in responding to a risk.

#### FY 2015/16 Annual Audit Plan

In addition to several on-going projects, the major audit projects scheduled for FY 2015/16 are the following, details of which are included in the attached Annual Audit Plan:

- Chino Basin Sewage Service Regional Contract Review
- Master and Rotating Contracts Audit

The Annual Audit Plan also identifies additional audit areas. If the risk in any of the identified auditable areas increases, or the need to reprioritize audit projects arises, IA will perform an audit from the following list:

- Water Conservation Programs
- Payroll and Time System
- Accounts Payable
- Credit Cards and P-Cards
- Telephone Expense
- Recycled Water Program & Revenue
- Inter-Fund Transfers and Reserve Requirements
- Capital Projects
- Agency Contracts/Agreements & Special Agreements
- Duplicate Payments/Late Payments/Fees and Penalties
- Asset Management
- Operations

Additionally, the IA Charter requires follow-up audit work be performed on previous audit observations and recommendations to ensure that effective corrective action was implemented or alternate controls have been incorporated to mitigate the risks identified. Follow-up audit work includes detailed testing and verification by IA staff. Currently, IA staff is evaluating the implementation progress of 28 recommendations. A separate report will be issued once a status is determined. There are 39 additional outstanding audit recommendations that relate to nine different audits, requiring follow-up verification. These will be planned according to the Annual Audit Plan. IA continues to work with Agency staff and review the recommendations and will report on the results through the status reports. A list of the outstanding recommendations was submitted in June. The attached Audit Plan provides a current list by the name of the audit, the number of outstanding recommendations.

The FY 2015/16 Annual Audit Plan was developed using a general assessment, best practice recommendations, best auditor judgment, feedback from Agency management and the Audit Committee, as well as accounting for the impact on the Agency's operations if the targeted units fail to function in the most effective and efficient manner or neglect to comply with required policies and procedures.

In planning for the FY 2015/16 Annual Audit Plan and IA projects, the following were considered:

- The IA Charter
- The Audit Committee Charter
- Communications with the Audit Committee and the Board of Directors
- Communications with Executive Management and key Agency personnel
- Communications with the External Financial Auditors
- Communications with the Audit Committee Independent Advisor
- Prior audit findings and recommendations
- Assessed risks in operations
- Agency's goals and objectives, including activities, developments and changes
- Agency policies & procedures
- Key areas that affect revenue and expenses
- Identified opportunities to improve operations and add value to services
- IA resources
- New audit requirements and best practices

This Annual Audit Plan is a *flexible plan* with the goal of targeting significant Agency auditable areas and business units at some point or another, depending on priorities, risks and/or requests by the Board, Audit Committee and/or management. The plan will be used as a *guide* in selecting the audits. The Audit Plan is not a concrete plan. The IIA *Standards* recommend that periodic risk assessments be performed to ensure information captured is relevant, timely, and aligned with the Agency's changing environment, objectives, and direction. For this reason IA prepares an Annual Audit Plan and submits amendments when required.

The Annual Audit Plan is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by providing a plan for the independent evaluations of Agency financial and operational activities and suggesting recommendations for improvements.

### **PRIOR BOARD ACTION**

On December 18, 2013, the Board of Directors adopted the Agency's Audit Committee Charter and the Internal Audit Department Charter.

**IMPACT ON BUDGET**

Should additional outside auditing or consulting services are required to provide assistance to IA or fulfill the responsibilities of the Audit Committee, a proposal with proposed fees will be submitted through the Audit Committee for appropriate action.



*Inland Empire Utilities Agency*  
A MUNICIPAL WATER DISTRICT

**Fiscal Year  
2015-2016**

**Internal Audit Department**  
**Annual Audit Plan**

Submitted by:  
Teresa V. Velarde  
Manager of Internal Audit Department  
September 2015

## **Annual Audit Plan Contents**

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Risk Assessment Strategy & Audit Universe	12
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## *Purpose of the Internal Audit Department*

As stated in the Board approved Charter, the purpose of the Internal Audit Department (Internal Audit) is to assist the Board of Directors and the Audit Committee in fulfilling their oversight responsibilities for reporting, internal controls, and compliance with legal and regulatory requirements applicable to Agency operations, and to provide objective assurance about the Agency's operations.

The purpose of the Internal Audit Department is also to provide consulting services, analyses, recommendations and information concerning the operations of the Agency as a service to management and as a way of adding value to improve the operations of the Agency. Internal Audit assists management and staff in achieving organizational goals and objectives by providing recommendations and advisory services based on results of analysis of the Agency's processes, procedures, governance, internal controls, financial reporting, and compliance with applicable laws and regulations.

The Internal Audit Department follows the guidance of the globally accepted *International Standards for the Professional Practice of Internal Auditing (Standards)* as documented in the International Professional Practices Framework (IPPF) and the Code of Ethics issued by the Institute of Internal Auditors (IIA). This guidance is documented in the Internal Audit Department Charter.

The Internal Audit Department reports directly to the Board of Directors through the Audit Committee. The Internal Audit Department has a dotted line reporting relationship to the General Manager and works in cooperation with the Executive Management Team but, as described in the Charter and according to the IIA *Standards* and best practices, is an independent function from Agency management. Independence is essential to the effectiveness of internal auditing and is emphasized by the Institute of Internal Auditors (IIA). The authority and responsibilities of the Internal Audit Department are specifically defined in the Internal Audit Department Charter approved by the Board of Directors.

### **Mission Statement**

*The Internal Audit Department seeks to improve the operations of the Agency by providing unbiased and objective assessments 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 accountability and integrity, improve operations and instill confidence among its employees and the citizens it serves by:*

- *Promoting a sound control environment.*
- *Providing independent, objective assurance and consulting services.*
- *Improving Agency risk management, control and governance.*
- *Promoting the Agency's vision and mission with a high degree of professionalism.*

### **Internal Audit Department Values**

The Internal Audit Department has adopted the following value statements that form the foundation for the Internal Audit Department:

#### **Independence**

As documented in the Charter the Internal Audit Department is an independent function of the Agency for the purpose of providing independent, objective, unbiased opinions.

#### **Integrity**

The Internal Audit Department staff is required to maintain the highest degree of integrity in conducting its audit work.

#### **Professionalism**

The Internal Audit Department will perform its work with professionalism at all times.

#### **Collaboration**

The Internal Audit Department will foster collaboration with all Agency personnel to promote teamwork within the various business units.



### *Purpose of the Annual Audit Plan*

The Annual Audit Plan (Audit Plan) has been prepared in accordance with recommendations and best practices provided by the Institute of Internal Auditors (IIA). The Audit Plan allows the Manager of Internal Audit to carry out the responsibilities of the Internal Audit Department by prioritizing projects and allocating necessary resources where audit efforts are deemed appropriate and necessary. The Audit Plan is created to assist management and the Board in achieving organization goals and objectives.

The Audit Plan is a flexible plan of internal audit activities and was developed using an appropriate risk-based methodology, including any risks or control concerns identified or communicated by Management, the Internal Audit Department, External Auditors, the Audit Committee or Board. The overall objective is to develop a plan consistent with the Agency's goals and objectives, to address the highest risk areas within the Agency and to evaluate and contribute to the improvement of risk management, control and governance processes, additionally to add value by recommending opportunities for improvements to increase effectiveness and efficiency of operations.

In order to provide practical guidance and an authoritative framework for the development of the Annual Audit Plan, the Internal Audit Department recognizes the following items: Achieving one hundred percent audit coverage each year is not practical or achievable. It should be noted that audit resources are limited; therefore, a system for prioritizing audits has been employed. The Annual Audit Plan must be a flexible plan and should be amended periodically as deemed necessary to reprioritize areas that require attention. In preparing the Annual Audit Plan, consideration is given to the work performed by other auditors, regulatory authorities, established rules, laws and ordinances and the Agency's system of controls. Auditable areas are ranked by knowledge of known or perceived areas of risk and understanding of the systems of internal controls. It should be noted that there are inherent risks, residual risks and limitations with any methodology applied when prioritizing risks and ranking audit projects, risk factors exist with any system of controls.

As stated in the Internal Audit Department Charter, the Manager of Internal Audit will set audit frequencies, select the subjects and set objectives, determine the scope of work and apply the techniques required to accomplish the audit objectives. The Manager of Internal Audit has the authority to deviate from the approved annual Audit Plan, when necessary, and if warranted by unforeseen issues that require immediate attention. The Manager of Internal Audit will use professional discretion and judgment in response to such unforeseen issues and resolve handle them according to the requirements of the Charter. Significant changes to or deviations from the approved Annual Audit Plan shall be reported to the Audit Committee and to the Board at the next regularly scheduled Audit Committee meeting.

Both the IAD Charter and the IIA's Code of Ethics have strict standards of ethical conduct for internal auditors. The auditors have a responsibility to maintain independence, ensure integrity, objectivity, confidentiality and competency in work performed.

### *Annual Audit Plan Methodology*

In planning for the Internal Audit projects the following were also considered:

- The Internal Audit Department Charter
- The Audit Committee Charter
- Communications with the Audit Committee and the Board of Directors
- Communications with Executive Management and key Agency personnel
- Communications with the External Financial Auditors
- Communications with the Audit Committee Independent Advisor
- Prior audit findings and recommendations
- Assessed risks in business practices and operations
- Agency's goals and objectives, including activities, developments and changes
- Agency policies & procedures
- Key areas that affect revenue and expenses
- Identified opportunities to improve operations and add value to services
- New audit requirements, audit trends and leading practices
- Audit Department resources

For the Fiscal Year 2015/16 Audit Plan, the audits were selected based on the previous year's risk assessment and results of audits previously scheduled and deferred due to other priority projects. Significant deviations and changes to the Audit Plan will be communicated to the Audit Committee through an Amended Audit Plan and progress information is provided through quarterly Status Reports.

### ***FY 2015/16 Annual Audit Plan***

For the remainder of Fiscal Year 2015/16, Internal Audit will work to finalize the Regional Contract Review and begin work on the Master Rotating Contracts Audit, as described below:

## **Chino Basin Regional Sewage Service Contract Review “Regional Contract Review”**

**(IEUA’s Planning Department & the Seven Contracting Agencies)**

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Complete a comprehensive report with recommendations for Executive Management to consider as part of renegotiating the Regional Contract and moving forward with ensuring all Regional Contracting Agencies understand and apply the provisions of the Regional Contract uniformly and consistently.

Internal Audit has already completed 10 reports with over 30 recommendations for management to consider in administering the contract. The purpose of the comprehensive report is to finalize all findings noted during the reviews of each of the member agencies and to consolidate and streamline all findings and recommendations.

Specifically the Regional Contract Review focuses on the following key areas:

- Public Service Facilities,
- Appropriate industry categories, purchased EDU’s, and discharge levels,
- Commercial business use and changes/improvements,
- Monthly Sewer Billings,
- Connection Fees, and
- CCRA Accounts

One final comprehensive audit report will be submitted by the end of calendar year 2015. Additionally, IA will provide various presentations as needed to present the recommendations resulting from this comprehensive evaluation.

## **Master and Rotating Contracts**

**(Contracts and Procurement, Engineering, and Construction Management)**

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The Agency has several master and rotating contracts for various services such as engineering services or construction services. An audit of this area would review procedures for updating the lists, opportunities for new companies to be considered for a master or rotating contract, and would review compliance with applicable laws and regulations. Additionally, the audit would evaluate the process to award contracts and projects to pre-selected/pre-qualified contractors/vendors or vendors on a “list” and ensure processes conform to legal and Board-approved practices and are documented in formal operating procedures. Audit areas include:

- Determine what procedures are in place to use the contractors on the master list
- Determine if equal opportunity is intended to use all contractors equally
- Evaluate controls in place to administer the contracts
- Evaluate response time, and customer satisfaction of work completed

### *On-Going Projects for FY 2015/16*

- ❖ Internal Audit Department Quality Assurance and Improvement Program
- ❖ Continue to assist with SAP internal control inquiries
- ❖ Assist with annual CAFR Review and Filing
- ❖ Review and update IA Department and Committee Charters
- ❖ Unannounced Petty Cash Audits
- ❖ Provide needed support related to audit topics, internal controls, Agency policy, procedure and compliance items
- ❖ Further utilize capabilities of SAP to enhance IA functions
- ❖ On-going required administrative reporting, such as, budget, goals/objectives, staff appraisals, and other administrative related items.
- ❖ Continue to review, update and document IA Policies and Procedures
- ❖ Continuous Professional Development of all auditors
- ❖ Plan, prepare and coordinate Audit Committee Meetings
- ❖ Utilize the IA site on PIPES as an Agency-wide communication tool
- ❖ Provide "audit approach" presentations to requesting departments
- ❖ Conduct special requests and/or unforeseen projects
- ❖ Provide recommendations to strengthen/streamline policies and procedures
- ❖ Update IA Annual Audit Plan and corresponding Risk Assessment
- ❖ Continue to work with auditees to resolve outstanding recommendations
- ❖ Assist with requests for internal controls questions, discussions and evaluations

### *Long Range Audit Planning Additional / Possible Audit Areas*

Internal Audit has identified additional audit areas. This list has been compiled as a preliminary list of future potential audits and as a list of additional, important audit areas where audit resources and efforts could be utilized. This is not a comprehensive/complete list. These audit areas have been selected based on identified risks at the time of completing this Audit Plan. If the risk/priority in any of the identified auditable areas increases, IA would perform an audit from the list that follows.

#### **Water Conservation Programs**

Due to the Governor's Drought declaration, a key measure included directing the California Department of Water Resources and the State board to accelerate funding for projects that enhance water supplies. Such funding is mostly in the form of grants; some received by IEUA. In partnership with other water agencies, IEUA has been at the forefront of various conservation projects working with member agencies to increase awareness about the drought and the need for conservation. Projects administered by IEUA must be carried out in accordance with the requirements of the grants, etc. This evaluation will review internal controls with contract administration/execution and proper distribution of funding.

#### **Payroll and Time System Implementation**

(Accounting and Fiscal Management, Human Resources, Business Information Systems)

To evaluate adequate internal controls and authorizations are in place in the new Payroll and Time System (myPT). With the implementation of the new Payroll and Time system which is replacing the existing IFAS system to streamline the current time, payroll and leave processes, there will be a need for auditors to check that adequate internal controls and authorizations are in place and working effectively and identify any areas for improvement.

#### **Accounts Payable Audit – Review of Credit Cards and P-Cards**

(Accounting)

Select a specific vendor or types of payments, for example credit cards and p-cards to ensure the transactions do not bypass the required procurement processes.

- Review financial transactions and supporting documents
- Evaluate internal controls
- Compliance with policies and procedures

#### **Contractual Actions (Construction Management, Contracts & Procurement, Accounting)**

For the purpose of selecting several significant construction contracts and to perform tests from before contract award through final payment and close-out. Including evaluating the process to award contracts and projects to pre-qualified contractors/vendors. Audit procedures will include: a review of internal controls; compliance with laws and regulations; compliance with Agency policies and procedures; and the effectiveness and efficiency of operations. Audit areas to include are: bidding process, contract award, invoicing, change orders, bonds, and warranties.

**Recycled Water Program – Revenue  
(Accounting and Fiscal Management, Financial Planning)**

Recycled water revenue in FY 2011/12 is almost \$10 million. An audit of this area would determine the accuracy of revenues and identify any additional revenue due the Agency.

**Capital Projects (Financial Planning, Accounting and Fiscal Management, Engineering and Construction Management.)**

The external financial auditors noted deficiencies with the process for closing completed projects. Projects were left open, long after the project had been completed, therefore, impacting the accounting value of capital assets. This audit would focus on evaluating when open capital projects have been completed and examining when the construction in progress balances are closed to capital assets.

**Inter-Fund Transfers and Reserve Requirements (Financial Planning)**

An audit of this area would determine if the Agency complies with all legal and regulatory requirements on maintaining reserves and on inter-fund transfers.

**Telephone Expense (Contracts and Procurement, Accounting and Fiscal Management)**

The Agency pays over \$85,000 annually for telephone service. Service is provided for landline phones, smartphones, and for data connections. Audit areas include the following:

- Determine efficiencies that could be achieved through consolidating billings
- Identify ways to streamline billing processes
- Comparison of charges on different bills to ensure consistency and accuracy
- Identify opportunities for savings
- Evaluating if phones issued to employees are used for the intended purpose according to Agency policies

**Bid and Selection Process for Construction Contracts  
(Engineering, Contracts and Procurement)**

To review the bid and selection process to ensure all legal and regulatory requirements are considered in the process, including grant requirements, where applicable, and that all contracts include required language. Additionally, to evaluate the process to award contracts and projects to pre-qualified contractors/vendors and ensure processes conform to legal and Board-approved requirements and are documented in formal operating procedures.

**Special Agreements (Contracts and Procurement, Accounting and Fiscal Management)**

The Agency has some "special agreements" with other agencies that may or may not be formalized under an official contract. This audit would also evaluate whether the special agreements provide preferential treatment or significant discounts/credits when compared to similar agencies for similar services.

**Duplicate Payments/Late Payments/Fees and Penalties  
(Accounting and Fiscal Management)**

This area was covered during the Accounts Payable audit. The goal for this audit is to make this a recurring evaluation to check for the three types of payments (duplicates, late payments or preventable fees and penalties). This audit would cover a greater sample and would implement an audit program to periodically check for these types of payments.

**Asset Management (Operations, Contracts and Procurement)**

The Agency currently has \$1.1 billion in total assets. An audit of this area would evaluate the accountability and controls to ensure assets are properly recorded in the Agency's financial records. Additionally, to determine if periodic inventories or other valuation processes are performed to validate the amount of assets reported in accounting records.

**Operations (Operations Department, Accounting and Fiscal Management)**

Facility Operations, Groundwater Recharge and Organics Management are programs under Operations Administration. The audit scope of any of these areas would focus on required permit compliance requirements, preventive maintenance of plants, staff training and staff certifications to operate plants/facilities, chemical and equipment use, and customer service to the service area, where applicable.



### *Outstanding Recommendations*

The Internal Audit Department Charter requires follow-up action be taken to ensure that management has effectively implemented recommendations or alternate controls have been incorporated to mitigate the risks identified. Follow-up audit work includes detailed testing and verification by Internal Audit staff.

In FY 2014/15, IA reviewed and verified the implementation status of open recommendations related to 17 different audits. Of the 72 open recommendations, five (5) recommendations have been implemented/no longer applicable, 28 recommendations are in progress of being evaluated, and 39 did not require a follow-up review as of June 2015 because they relate to audits completed during FY 2013/14. Audit guidelines suggest that an adequate amount of time be granted in order to provide auditees with sufficient time to implement corrective action plans. Follow-up audit work will be incorporated and completed along with the proposed projects for some of the open recommendations. Required follow-up audit work will include a desk review of supporting documentation, follow-up discussions with the auditee, and/or the application of testing procedures to verify implementation.

Area Audited	Report Issued Date	Follow-up review in progress by IA	No. of Recs. Remaining to be Verified by IA	Planned Follow-Up by IA
Intercompany Receivables - CDA	February 24, 2011	2		
Intercompany Receivables - RCA	March 30, 2011	2		
Intercompany Receivables - Watermaster	August 30, 2011	6		
IT Equipment	August 21, 2012	16		
IT Equipment Follow-Up	November 14, 2012	2		
Payroll Audit	August 24, 2010		1	FY2016
Human Resources Follow-Up	June 20, 2012		1	FY2016
Contracts and Procurement Follow-Up	August 29, 2012		2	FY2016
2013 Petty Cash	May 31, 2013		5	FY2016
SCE Utility Payments	August 28, 2013		3	FY2016
Accounts Payable Follow-Up	August 29, 2013		9	FY2017
Automobile Insurance Requirements	March 3, 2014		2	FY2017
Vehicle Security Procedures	March 3, 2014		3	FY2017
Vehicle Inventory Procedures	March 12, 2014		13	FY2017
<b>Total</b>		<b>28</b>	<b>39</b>	

*\*See the attached Report showing a list of all Outstanding Recommendations as of June 2015.*

In addition to the outstanding recommendations from the various audits noted above, to-date, IA has completed nine different audit reports related to the Regional Contract Review and provided 31 recommendations for IEUA to consider in moving forward with renegotiating the Regional Contract.



### *Risk Assessment Strategy*

The IIA IPPF Standard 2120 states that Internal Audit must evaluate the effectiveness and contribute to the improvement of risk management processes.

The risk assessment is a general assessment performed using best practice guidance, professional judgment and consideration for the impact on the Agency's operations if the targeted units fail to function in the most effective and efficient manner or neglect to comply with required policies. In performing the Risk Assessment for this FY 2013/14 Annual Audit Plan, the following were considered:

- Agency Policies and Procedures
- Communication with the External Auditors
- Communication with the Audit Committee and Board
- Communications with key Agency personnel
- Assessing risks and exposures that may affect the organization
- New Agency activities, developments and major changes
- Key areas that affect revenue and expenses
- Observations resulting from previous audits and reviews
- New audit requirements and trends
- Opportunities to improve operations

The IIA PPF defines Risk as follows:

- **Risk** – The possibility of an event occurring that will have an **impact on the achievement of objectives**. Risk is measured in terms of impact and likelihood and;
- **Residual Risks** – As the risk remaining **after management takes action to reduce the impact** and likelihood of an adverse event, including control activities in response to a risk.

### *Audit Universe*

The IIA PPF defines Universe as all possible auditable areas. For the purposes of this Annual Audit Plan, the universe includes all Agency Departments, operations, contracts, transactions, processes, and activities.

***Internal Audit Department  
Quality Assurance and Improvement Program***

The Institute of Internal Auditing (IIA), International Professional Practices Framework (IPPF) defines a Quality Assurance and Improvement Program: “A quality assurance and improvement Program is designed to enable an evaluation of internal audit activity’s conformance with the Definition of Internal Auditing and the *Standards* and an evaluation of whether internal auditors apply the Code of Ethics. The program also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement.”

Standard 1311 of the IPPF requires that internal assessments include ongoing monitoring of the performance of internal audit activity; and periodic reviews performed through self-assessments.

Standard 1312 of the IPPF requires that external assessments be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organization.

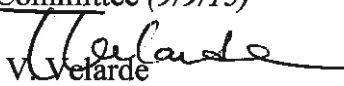
As part of IA’s commitment for continued quality audit services, beginning FY 2016/17, IAD will perform internal assessments of the IAD. An external assessment by an independent reviewer is planned for FY 2017/18. Results will be presented and discussed at the regularly scheduled Audit Committee meetings.

**INFORMATION  
ITEM  
2A**

Date: September 16, 2015

To: The Honorable Board of Directors

Through: Audit Committee (9/9/15)

From: Teresa V. Vefarde   
Manager of Internal Audit

Subject: Regional Contract Review - Interim Audit Report for the City of Ontario

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### **RECOMMENDATION**

This is an information item for the Board of Directors.

### **BACKGROUND**

At the request of the Board of Directors and Executive Management, Internal Audit (IA) has been performing a review of the Agency's Regional Sewage Service Contract (Regional Contract Review) as implemented with the seven Regional Contracting Agencies. The objectives of the Regional Contract Review include:

- Evaluate of how each of the seven agencies apply the Regional Contract provisions
- Determine whether processes are in compliance with the Regional Contract requirements
- Determine opportunities to improve processes and procedures
- Identify opportunities and make recommendations for consideration as part of the Regional Contract renegotiation

The Interim Audit Report for the City of Ontario (Ontario) is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by providing independent evaluations of the financial and operational activities of one of IEUA's Contracting Agency's implementation of the Regional Contract and suggesting recommendations for improvements.

### **ATTACHMENTS**

The interim report for the Ontario is attached. IA previously submitted the report of the Ontario in draft form for discussion purposes, to provide a status of the review, and to extend the Ontario additional time and every opportunity to provide additional supporting information to finalize the evaluation.

IA identified observations and recommendations to strengthen administrative, accounting, recording, and reporting controls to ensure the intent of the Regional Contract is achieved. As with the previous six Regional Contract reports, most of the IA recommendations could be applied

to all Contracting Agencies going-forward, as an amendment and/or as part of the Regional Contract review and renegotiation process; in order to ensure all Regional Contracting Agencies apply and administer the Regional Contract in a uniform and consistent manner. A summary of IA’s recommendations is provided separately in Exhibit A. A summary of the most significant observations is provided below. The attached report provides additional details.

City of Ontario

- Ontario’s Calculation Worksheet does not match Exhibit J; therefore creating differences in the Connection Fees that should be collected. For the items tested, Ontario under-collected approximately \$84,000 in Connection Fees. The review found that the City of Ontario’s automated calculation worksheet, built into their permits system, utilized to calculate Connection Fees does not always coincide with the descriptions and/or associated fixture unit values as outlined in Table 1 of Exhibit J of the Regional Contract; therefore generating differences in the Connection Fees Collected.
- Ontario asks permit applicants to self-assess their fixture units and determine the Connection Fees they owe. This process differs from what most Contracting Agencies have implemented, where a calculation worksheet is completed by the Building Department staff having expert knowledge related to the Regional Contract and Connection Fees. Subsequently, during the site inspection process Ontario staff confirm that the actual structure agrees to the plans that were submitted. Ontario’s process does not verify that the Connection Fee calculation [worksheet] agrees to the building/plumbing plans, giving oversight (and potential under-calculation and under-collection) of the Connection Fee process to the customer. In addition, the Ontario is not fully utilizing the expertise of its Building Department staff in collecting Connection Fees, according to the Regional Contract requirements.
- Ontario has not collected fees for public schools construction:

Name of School	School District	Type of Construction	When completed	Fees Collected
Richard Haynes Elementary	Ontario Montclair	Addition of a Multi-purpose room with multiple restrooms and warming kitchen. (CVWD collected \$10,809 for a new elementary school cafeteria and Montclair collected \$24,021 for a new elementary school multipurpose room with kitchen and restroom.)	Summer 2012	\$ 0
Ray Wiltsey Middle	Ontario Montclair	13 classroom modular facility with multiple restrooms, outdoor areas. (CVWD collected \$62,958 for a new 14 room classroom building with restrooms.)	Summer 2013	\$ 0
Ontario High	Chaffey Joint Union High School	New classroom building, restrooms, football stadium and pool. (CVWD collected \$42,792 in Connection Fees for a new high school classroom wing/building, gymnasium expansion and athletic field complex.)	In Process	\$ 0

- Approximately a fourth of the monthly sewerage billing items tested during this review, had erroneous rates, were not found in the billing system or showed that the monthly billing

is appropriately done, or were industrial entities with unusual rate structures as described in the next paragraph.

- A wide range of new manufacturing and industrial businesses have located in Ontario. The Connection Fees and monthly sewerage charges for these enterprises varied widely. In addition, there appears to be a need to improve guidelines for industrial enterprises to ensure that Connection Fees and monthly sewerage charges are assessed correctly, are fair and equitable, and are determined in accordance with the intent of the Regional Contract.

IA would like to extend its appreciation to staff at the Ontario, as well as the IEUA Planning and Environmental Resources Department for their cooperation and assistance during this review.

To-date, IA has submitted as information items the following reports:

- Interim Audit Report for the City of Chino Hills (June 2015)
- Interim Audit Report for the Cucamonga Valley Water District (March 2015)
- Interim Audit Report for the City of Chino (December 2014)
- Interim Audit Report for the City of Fontana (December 2014)
- Interim Audit Report for the City of Montclair (September 2014)
- Interim Audit Report for the City of Upland (September 2014)
- “Survey of Comparative Information of the Seven Contracting Agencies” (September 2014)
- “Regional Contract Review – Review of the Ten Year Forecast” (June 2014)
- “Regional Contract Review – Survey of Comparable Agencies (June 2014)

### **PRIOR BOARD ACTION**

On September 17, 2014, the Board of Directors approved the Fiscal Year 2014/15 Annual Audit Plan.

On December 18, 2013, the Board of Directors reconfirmed the approved Internal Audit Department Charter.

### **IMPACT ON BUDGET**

None




## ***Inland Empire Utilities Agency***

**A MUNICIPAL WATER DISTRICT**

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P.O. Box 9020 • Chino, Hills, CA 91709  
TEL (909) 993-1600 • FAX (909) 597-8875  
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DATE: July 22, 2015

TO: Joe Grindstaff  
General Manager

FROM:   
Teresa V. Velarde  
Manager of Internal Audit

**SUBJECT: REGIONAL CONTRACT REVIEW  
Interim Audit Report  
City of Ontario**

### **Audit Authority**

The Inland Empire Utilities Agency (IEUA or Agency) Internal Audit Department (IA) performed a review of the Agency's Regional Sewage Service Contract (Regional Contract) as implemented with the Regional Contracting Agencies (RCA or Contracting Agency). The review was performed under the authority given by the IEUA Board of Directors as documented in the Internal Audit Department Charter and according to the Fiscal Year 2013/14 Annual Audit Plan.

### **Audit Objective and Scope**

The objectives of the Regional Contract Review are to evaluate how each of the seven Contracting Agencies apply the Regional Contract provisions, determine whether processes are in compliance with Regional Contract requirements, determine opportunities to improve processes and procedures and make recommendations to consider as part of the Regional Contract renegotiation or amendment. The review covered the period from July 1, 2012 through December 31, 2013 and where possible considered events subsequent to that period.

The review included procedures to evaluate compliance with the Regional Contract, Exhibit J Initial Connection Fees provisions as well as the recurring sewer service fees billing for the various types of land uses (commercial, industrial, residential, public service and extra-territorial). IA performed a variety of review procedures at each Contracting Agency to evaluate:

- Connection Fees
- Public Service Facilities Connection Fees
- Monthly Volumetric Sewerage Charges
- Extra-Territorial Fees
- Reconciliations of fees collected and paid to IEUA
- Overall Recordkeeping

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**Jasmin A. Hall**  
Director

**Gene Koopman**  
Director

**P. Joseph Grindstaff**  
General Manager

This report describes the results of the procedures performed at the City of Ontario.

### City of Ontario – Background

The City of Ontario (Contracting Agency, Ontario or City) was incorporated on December 10, 1891 and utilizes a Council-Manager form of government. The City has a population of 166,866 and encompasses 50 square miles which is 21% of the 242-square-miles covered by IEUA's service area<sup>1</sup>.

As well as other municipal services, the City provides water, trash and local sewer service to residential, commercial and other properties within its boundaries.

### Financial Information

Under the terms of the Regional Contract, the City of Ontario is required to report Connection Fees and Sewer Service Fees on a monthly basis.

**Connection Fees** are one-time fees levied on new development connecting to the Regional Sewerage System, as well as existing users who expand their number of fixture units. These fees are reported in the monthly Building Activity Reports (BAR) to the IEUA Planning and Environmental Compliance Department and are recorded in the Agency's financial system.

The amount of Connection Fees collected varies from year to year depending on the construction activity occurring within the Contracting Agency's boundaries. Equivalent Dwelling Units (EDU's) purchased and fees collected by the City during the last two fiscal years are:

Fiscal Year	EDU's	Fees collected
2012/13	157	\$ 770,709
2013/14	334	\$ 1,674,395

EDU's and fees collected reflect the amounts reported in the BAR. The fees for FY 2013/14 were substantially higher than the prior year due to fees collected in connection with the construction of new residential gated communities in the City.

### CCRA Account

Connection Fees are collected by the City and held in a Capital Connection Reimbursement Account (CCRA) until called by IEUA. The CCRA balance for the City of Ontario as reported by IEUA in the June 30, 2013 and 2014 CAFR's was \$3,337,338 and \$5,011,733 respectively.

<sup>1</sup> Ontario statistics from City of Ontario website: "About Ontario – City Facts"



**Sewer Service Fees (Volumetric Sewerage Fees)** are recurring fees assessed and collected from users that discharge into the Agency's Regional Sewerage System. According to the Regional Contract, Contracting Agencies must pay IEUA for sewer services each month. The City of Ontario self-reports the number of EDU's to IEUA for all its customers on a monthly basis, since the City bills monthly. The EDU's reported are comprised of the following: one EDU for residential, 0.7 EDU for multi-family residential, fixed EDU's for schools (based on student enrollment) and industrial (recalculated annually), and variable EDU's for commercial entities (based on water consumption).

The table below outlines the total number of EDU's reported and Volumetric Sewerage Fees paid to IEUA by the City of Ontario for the last two fiscal years. This information is reported in the Agency's accounting system (SAP).

**City of Ontario  
 Sewer Service Fees**

Fiscal Year	EDU's <sup>(1)</sup>	Fees <sup>(1)</sup>
2012/13	707,904	\$ 8,770,935
2013/14	711,899	\$ 9,532,321

(1) = From IEUA monthly billing invoices.

As part of reporting Sewer Service Fees, the City of Ontario provides additional detail as shown below. The Regional Contract does not require this information and the amount of information provided varies by Contracting Agency.

As of June 30, 2014 the City of Ontario's total number of EDU's consisted of the following (from the June 2014 monthly billing information provided to IEUA):

Type of Account	Number of EDU's	% of Total
Single Family Residential (1 EDU per dwelling)	26,492	41.70
Multi-Family Residential (.7 EDU per dwelling)	13,047	20.53
Public Authority	947	1.49
Interdepartmental	127	0.20
Industrial	4,208	6.62
Hotel/Motel	831	1.31
Commercial	17,884	28.15
<b>Total</b>	<b>63,536</b>	<b>100%</b>

*This information is reported by the City of Ontario. IEUA does not verify these totals.*

**Connection Fees**

Each Contracting Agency is required to assess, collect, and report Connection Fees for any new development that connects to the Regional Sewerage System, or users who expand their fixture unit count. The fees are to be assessed and collected by the Contracting Agency in accordance with the provisions of Exhibit J in the Regional Contract.

IA selected various businesses to test whether Connection Fees were accurately calculated, collected and reported to IEUA in accordance with Exhibit J of the Regional Contract. IA judgmentally selected 73 different businesses from the following sources to verify the Contracting Agency applied and collected the correct EDU rate according to the Board-approved rates and to determine the accuracy of the categorization type used per Exhibit J of the Regional Contract:

- The new business license report provided by City staff
- IA conducted physical observations of the City's commercial districts
- Building Activity Reports submitted to IEUA
- Input received from IEUA's Planning & Environmental Compliance Department

Due to the wide range of sources used to select businesses to test, the Connection Fees that were tested covered a larger time period, with most permits tested ranging from 2010 to the present. In addition, two business' most recent permits were from 2006 and two others were from 2008. The Board approved Internal Audit Charter authorizes Internal Audit to expand the scope of work when deemed necessary. The review found:

1. **Ontario's Calculation Worksheet does not match Exhibit J creating differences in the Connection Fees that should be collected. For the items tested, Ontario under-collected approximately \$84,000 in Connection Fees.**

The review found that the City of Ontario's automated calculation worksheet, built into their permits system, utilized to calculate Connection Fees does not always coincide with the descriptions and/or associated fixture unit values as outlined in Table 1 of Exhibit J of the Regional Contract. Ontario established a worksheet based on their interpretation of the California Plumbing Code, however, some of the descriptions for the type of fixture installed and associated fixture unit value differ from the types and values provided under Exhibit J creating differences when compared to the Regional Contract Fixture Unit values and Connection Fees assessed:

COMPARISON OF ONTARIO CALCULATION WORKSHEET TO EXHIBIT J			
City of Ontario's Worksheet		Regional Contract Exhibit J (Table 1)	
Type of Fixture	Unit	Type of Fixture	Fixture Unit
Water Closet-Commercial Qty	1	Water Closet, 1.6 GPF	4.0
Urinal Qty	4	Urinal	2.0
Sink-Service Mop Qty	2	Kitchen, Service or Mop Basin	3.0
Drinking Fountain Qty	1	Drinking Fountain or Water Cooler	0.5

The impact of using fixture unit values that vary from Exhibit J affects the dollar amount of Connection Fees assessed and collected by the Contracting Agency. Of the 73 items selected, 28 paid Connection Fees for new fixture units since 2006. Exhibit J did not provide a table of fixture unit values until its revision June 19, 2013. Therefore, there was no authoritative guidance prior to that revision and individual Contracting Agencies relied on the Plumbing Code to determine fixture unit values. IA analyzed the selected items to isolate only the impact of using fixture unit values that differ from the values required by Exhibit J under the Regional Contract, both for all items tested and for only those items tested during the period since Exhibit J was revised. Ten of the items tested were in the period since Exhibit J was revised:

<b>CALCULATION WORKSHEET DIFFERENCES: EXHIBIT J COMPARED TO ONTARIO</b>				
<b>Business/Permit Tested</b>	<b>Exh J F. U.</b>	<b>Exh J Fees</b>	<b>Ontario F. U.</b>	<b>Ontario Fees</b>
FAST 5 PIZZA	14	\$ 3,112.35	13	\$ 2,890.04
Continental Funeral Home	14	\$ 3,051.43	14	\$ 3,051.43
Cardenas Markets Inc.	7	\$ 1,556.18	7	\$ 1,556.18
Office Building	105	\$ 23,342.63	107	\$ 23,787.26
Office Building	97.5	\$ 21,675.30	60	\$ 13,338.65
Magic Hawaiian Barbecue also Pizza Palace, etc.	25	\$ 5,668.77	24	\$ 5,442.02
Charter school resource center	14	\$ 4,416.17	16	\$ 5,047.06
B201302744	32.5	\$ 10,251.83	30	\$ 9,463.23
B201301578	48	\$ 17,808.90	26	\$ 9,646.49
B201302547	61.5	\$ 13,672.11	62	\$ 13,783.27
<b>TOTALS</b>	<b>418.5</b>	<b>\$ 104,555.69</b>	<b>359</b>	<b>\$ 88,005.62</b>

The City of Ontario under-collected \$16,550 for the 10 items tested for the period since Exhibit J was revised on June 19, 2013 (\$104,555 - \$88,005). In comparison, had the 2013 Exhibit J revision been in effect for all items tested, the City of Ontario under-collected a total of \$83,882 in Connection Fees on total collections of \$441,705 for all 28 items tested during this review. These under-collections result solely from Fixture Unit differences in the calculation worksheet. This does not consider any other differences that might have resulted from business classification differences or differences from variances in the number of fixtures shown on the building plans.

In the 2013-14 fiscal year the City of Ontario reported a total of \$768,586 in Connection Fees for non-residential building activity in the Building Activity Reports. The Calculation Worksheet differences being tested arise solely from the difference in Fixture Unit Values between Exhibit J and the City of Ontario's automated worksheet, a factor that remains constant across the entire universe of building activity reported in 2013-14. Since this variation is constant for all items tested, it is reasonable to extrapolate the impact of this variation. Thus, extrapolating solely the impact resulting from differences in fixture unit values between Exhibit J and Ontario's calculation worksheet by using the error rate in the sample tested in the period since Exhibit J was revised and comparing it to the total non-residential fees reported: Connection Fees

could have been under-reported by as much as approximately \$145,000 (calculated as: \$16,550 / \$88,006 x \$768,586 or “error rate” times “reported fees”) for the 2013-14 fiscal year. In comparison, if all tested sample items were included in the extrapolation, under-reported fees could have been as much as approximately \$146,000 (calculated as \$83,882 / \$441,705 x \$768,586). Both approaches to extrapolate potential under-collections yield similar results. The actual amount under-collected would, however, require recalculation of all calculation worksheets during the period since Exhibit J was revised.

The City of Ontario **recently revised** their calculation worksheet to align it with Table 1 of the revised Exhibit J, but kept the limited number of categories and naming conventions from the prior version (**See Exhibit A – City of Ontario Revised Calculation Worksheet**) and stated that the “City’s Building Department is using the Fixture Units from the Plumbing Code following State Law” (IEUA’s Planning and Environmental Resources Department, however, confirmed that Ontario staff participated in the 2013 meetings resulting in the most recent revisions to Exhibit J). There are still differences between the revised worksheet and Exhibit J:

<b>EXHIBIT J CATEGORIES NOT INCLUDED ON ONTARIO WORKSHEET</b>	
<b>DESCRIPTION</b>	<b>F.U.</b>
High efficiency clothes washer	2.0
Food waste grinder (commercial)	3.0
Floor drain, emergency	0.0
Shower, multi-head, each additional	1.0
Lavatory, in sets of two or three	2.0
Washfountain (1.5-in minimum fixture branch size)	2.0
Washfountain (2-in minimum fixture branch size)	3.0
Receptor, indirect waste – Bar	2.0
Receptor, indirect waste – Clinical	6.0
Receptor, commercial with food waste (1.5-in minimum fixture branch size)	3.0
Receptor, commercial with food waste (2-in minimum fixture branch size)	4.0
Receptor, commercial with food waste (3-in minimum fixture branch size)	6.0
Receptor, kitchen, domestic	2.0
Receptor, Service, flushing rim	6.0
Waterless Urinal	1.0

<b>ONTARIO CATEGORIES NOT SPECIFIED IN EXHIBIT J</b>	
<b>DESCRIPTION</b>	<b>F.U.</b>
Floor sinks	2.0
MH park trap - one trailer	6.0
Sink-food waste	3.0

*IA recommends that calculation worksheets be standardized region-wide and that Contracting Agencies prepare separate calculation worksheets for the individual categories when businesses operate in multiple segments as described in Exhibit J.*

**2. Private residential community centers have varying interpretations by the different contracting agencies.**

IA noted a recent trend where new housing developments include a community center with amenities such as fitness centers, swimming pools, meeting rooms and gathering places. This is an instance that can create varying interpretations and applications of Exhibit J of the Regional Contract. In the March, 2014 BAR, the City of Ontario reported such a facility as commercial category III, which includes "Health Spa with Pool" as one of the descriptions and has a Sewage Factor of 0.1081. This compares to the finding in IA's Interim Report for the City of Chino where that City's practice is to use commercial category I which includes retail, office and fast food and has a Sewage Factor of 0.0444 resulting in lower Connection Fees. Although, Ontario's categorization may be more aligned with the Exhibit J category with the most relevant description, additional guidance in Exhibit J would create greater uniformity in categorizing these centers in the region.

	Exhibit J	Exhibit J Description	Sewage Factor	Fees
City of Chino categorization	Category Type I	Retail, office, motel/hotel and similar businesses	0.0444	\$28,011
City of Ontario categorization	Category Type III	Health spa with pool	0.1780	\$112,297

*Although Exhibit J was recently updated and now provides greater detailed definitions for many business types, there still appears to be room for varying interpretation and application. Businesses continue to evolve and new types of businesses emerge and the Regional Contract should be updated regularly to provide additional language, definitions and guidance to ensure all types of commercial businesses are classified consistently. Additionally, the Contracting Agencies should look for IEUA's guidance.*

**Plumbing Plans – Fixture Unit Recount**

In attempting to perform a fixture unit recount at the City of Ontario, IA determined that Ontario's procedure in assessing Connection Fees differs from the other Contracting Agencies. According to Ontario's Building Department staff, the City of Ontario asks permit applicants to self-assess their fixture units and determine the Connection Fees that they owe. The City then performs its own review during the site inspection process to confirm that the actual structure conforms to the plans that were submitted. In IA's opinion this procedure omits the step of verifying that the actual Connection Fee calculation conforms to the building/plumbing plans. In addition, the City of Ontario is not fully utilizing the expertise of its Building Department staff in collecting fees.

*IA recommends that the City of Ontario examines and restructures the Connection Fee calculation and collection process to ensure that the fixture unit counts are correctly tallied, the categorization of businesses is appropriate and that connection fees are not under-collected.*

IA performed an extended walk-through of the fixture count process by reviewing the plumbing plans for five of the originally selected 73 items to verify the accuracy of the fixture count and the application of the required fees. At all other Contracting Agencies the recount was performed by Contracting Agency staff, witnessed/verified by IA and the results of the recount agreed upon by both parties. However, since the City of Ontario requires permit applicants to self-assess fixture units the Building Department officials indicated that they would not be able to provide assistance for the plumbing plans recount. Although IA staff have no plan-check experience and do not have the technical expertise of an actual plan-checker or someone familiar with the Plumbing Code and Exhibit J, IA attempted to independently examine the five sets of building/plumbing plans to determine the accuracy of the fees that were collected. IA's review noted:

- Jogue, Inc: The City's permitting files reference Permit #'s 201203421 and 201302705, neither of which were found to have been included in Building Activity Reports to IEUA. The only relevant permit that was reported is #2142 which shows 30 fixture units. IA's fixture unit count totaled 73 domestic industrial fixture units rather than the 30 that were reported, resulting in under-collection of \$15,642.
- Continental Funeral Home: The calculation worksheet used the general commercial category I sewage factor (0.0444) rather than the category II that includes mortuaries (0.1081), resulting in under-collection of \$4,378.
- Office Building, 150 E. Holt: One of the two sets of plans associated with this location was unavailable. The other set that was made available to IA indicated that the building houses medical clinics, facilities, and offices. IA performed additional "Google" research which shows a Women/Infant/Children (WIC) clinic on the 1<sup>st</sup> floor and the Ontario Public Health Clinic on the second floor. IA's fixture unit count totaled 122 fixture units rather than the 107 that were reported. The calculation worksheet also used the commercial category I sewage factor (0.0444) rather than category III that includes hospitals and convalescent homes (0.1780). Overall, this resulted in an under-collection of \$14,697.
- Haliburton: IA attempted to recount the fixture units on this set of building plans. However, without the technical expertise and knowledge that Building Officials have, IA was unable to validate the fixture unit count. See additional discussion of Haliburton later in this report.
- Excelsior Charter School Resource Center: IA's fixture count matched the calculation worksheet and the City did use the correct category VI sewage factor (0.0630) for a Public Service Facility.

The impact of these findings is summarized as follows:

<b>FIXTURE UNIT RECOUNT SUMMARY</b>			
<b>BUSINESS</b>	<b>ERROR TYPE (Information is for specific calculation worksheet tested)</b>	<b>CONNECTION FEES COLLECTED</b>	<b>IMPACT (Under Collected)</b>
Jogue, Inc.	Fixture Unit difference	\$ 10,913	(\$ 15,642)
Continental Funeral Home	Classification difference	\$ 3,051	(\$ 4,378)
150 E. Holt	Fixture Unit & Classification differences	\$ 23,787	(\$ 14,697)
Haliburton	Industrial Calculation difference (addressed separately)	\$ 38,558	unknown
Excelsior Charter	No differences noted	\$ 5,047	\$ 0
	<b>TOTAL</b>		<b>(\$ 34,717)</b>

*IEUA and the Contracting Agency should work together to ensure the calculation of connection fees and fixture units is in compliance with Exhibit J of the Regional Contract in order to prevent over/under collections and to ensure all Contracting Agencies apply the values required under the Regional Contract in a consistent and uniform manner.*

*IEUA should work with the Contracting Agency to establish, as part of the permitting and plan check process, the requirement to have an IEUA representative provide a final sign-off and approval, prior to the Contracting Agency issuing a permit to a business or industry and allowing a connection to the system. This added approval step will ensure IEUA is in agreement with the interpretation of the Contract and that the appropriate category type and sewage factor has been applied so that the correct Connection Fees are assessed and collected.*

**Public Service Facilities**

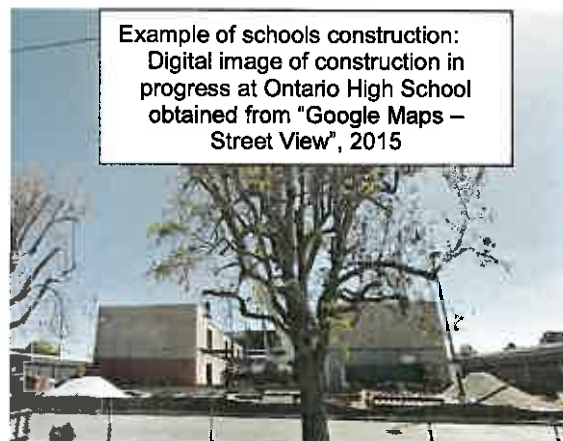
Exhibit J includes for purposes of fee calculation: *“All structures designed for the purpose of providing permanent housing for enterprises engaged in exchange of good and services. This shall include, but not be limited to, all private business and service establishments, **schools, churches, and public facilities.**”* (emphasis added)

The Division of the State Architect’s Office (DSA) of the State of California provides design and construction oversight for public schools (Kindergarten through 12th grade), community colleges, and various other state-owned and leased facilities. Likewise, the Office of Statewide Health Planning and Development (OSHPD) regulates hospital construction. Entities that fall under the DSA or OSHPD have a permit and plan check process that is separate and includes limited or no coordination with the local jurisdiction. The DSA and OSHPD do not collect Connection Fees on IEUA’s behalf as part of their oversight process, even though the construction projects reviewed could be new construction or expansions that result in additional discharge into the regional infrastructure. It is the responsibility of each individual local jurisdiction to ensure collection of the Connection Fees from entities that fall under the DSA or OSHPD and reside within their service area.

For purposes of this review, several approaches were used to determine Public Service Facilities in the City of Ontario. IA reviewed the OSHPD website for information about hospital and similar construction in the City of Ontario. This review noted that the Kaiser Ontario facility opened in November of 2011. The medical facility is located on a 28-acre master-planned campus and the construction project included a 386,000 sq. ft. Hospital Medical Center with two patient towers that hold 260 beds and a diagnostic and treatment wing, a new three-story 160,000 sq. ft. hospital support building that has medical offices, and major additions to the existing Central Utility Plant. The City of Ontario collected Connection Fees in the amount of \$1,409,106 in May 2012.

IA also reviewed the websites of school districts that service the City of Ontario. This included looking at bond measure construction update reports and the annual school accountability report cards of individual schools. As a result of these procedures one elementary school (Richard Haynes Elementary School), one middle school (Ray Wiltsey Middle School) and one high school (Ontario High School) were chosen for testing. IA noted:

Name of School	School District	Type of Construction	Bond Measure	When completed	Fees Collected
Richard Haynes Elementary	Ontario Montclair	Addition of a Multi-purpose room with multiple restrooms and warming kitchen	"T"	Summer 2012	\$ 0
Ray Wiltsey Middle	Ontario Montclair	13 classroom modular facility with multiple restrooms, outdoor areas	"T"	Summer 2013	\$ 0
Ontario High	Chaffey Joint Union High School	New classroom building, restrooms, football stadium and pool	"P"	In Process	\$ 0



1. Richard Haynes Elementary School: Per staff, the City has no record of any fees collected. For comparison purposes Cucamonga Valley Water District collected \$10,809 in Connection Fees for a new elementary school cafeteria and the City of Montclair collected \$24,021 in Connection Fees for a new elementary school multipurpose room with kitchen and restrooms.



2. Ray Wiltsey Middle School: Per staff, the City has no record of any fees collected. For comparison purposes Cucamonga Valley Water District collected \$62,958 in fees for a new 14 room classroom building with restrooms.
3. Chaffey Joint Union High School District – Ontario High School: Per staff, the City has no record of any fees collected. For comparison purposes, the City of Upland collected \$22,506 in Connection Fees for a new high school gymnasium and the Cucamonga Valley Water District collected \$42,792 in Connection Fees for a new high school classroom wing/building, gymnasium expansion and athletic field complex.

Based on the comparison to what other Contracting Agencies collected, the City of Ontario may have failed to collect over \$120,000 for the construction of additional facilities at these three school sites.

*Approximately half of the Contracting Agencies are collecting Connection Fees for school construction. However, even those that collect Connection Fees do not do so in all instances. In moving forward with renegotiating the Regional Contract, IEUA and the Contracting Agencies should consider the following options:*

1. *IEUA should provide guidance and assistance to the Contracting Agency to adopt a collaborative approach and foster a relationship with the School District and any other PSF to ensure Connection Fees are charged and collected for any future planned projects with new construction or expansion. For example, the City of Ontario could consider and adopt the collaborative approach utilized at the City of Upland. The City of Upland has formed an inclusive group from all city departments that meets regularly to review new development. The group includes representatives from the Planning, Building, Public Works, Police and Fire departments. Since planning for fire safety is required for new construction to ensure access and egress, Fire department representatives are often the first to know about new PSF construction. This will trigger Public Works and Building department representatives to be involved resulting in the assessment of Connection Fees, including those for IEUA in accordance with Exhibit J.*
2. *In connection with a renegotiation of the Regional Contract, IEUA and the Contracting Agencies should consider the legal and financial impacts of eliminating the requirement for collecting Connection Fees and monthly sewerage charges from some types of Public Service Facilities. As documented under the audit report "Comparison of the Regional Sewage Service Contract and Program with similar contracts and programs", IA found that some Agencies (for example, the Los Angeles County Sanitation Districts) exclude local governmental agencies such as public schools and City governments from these charges.*

### **Volumetric Sewerage Fees**

Section 18 of the Regional Contract states:

*“Concurrently with the adoption of the Regional Sewerage System budget, the Board of Directors of CBMWD shall fix the service charge rate for the fiscal year. The rate shall be expressed in dollars and cents for each Equivalent Dwelling Unit (EDU) of sewage and shall be computed . . . as set forth in the Regional Sewerage System budget adopted for the fiscal year. The estimated EDU’s of sewage delivered into the Regional Sewerage System shall be determined based on a standard daily measurement or contribution of sewage per EDU agreed to from time to time by CBMWD and the Regional Technical Committee.”*

Thus, the Regional Contract delegates the details of determining monthly sewerage billing to the Regional Technical Committee. The most recent information about monthly sewerage billing is from a memorandum entitled “Procedures for Establishing a Regional Sewer Billing Formula” which was adopted by the Regional Technical and Policy Committees for monthly/bimonthly billing processes in 1997.

*IA notes that documentation approving and mandating the billing methodology is not available. Any revision should be presented to the IEUA Board of Directors and formally adopted, based upon the recommendation of the Regional Technical Committee.*

The City of Ontario bills customers each month for water and the City’s and IEUA’s regular sewerage charges. For IEUA sewerage billing purposes EDU’s in most categories are calculated in accordance with the 1997 memorandum: One EDU for residential, 0.7 EDU for multi-family residential, fixed EDU’s for schools (based on student enrollment) and variable EDU’s for commercial entities (based on water consumption). However, Industrial customers are billed in a variety of ways (see below). Payments made to IEUA are based on the amounts billed.

Although only 28 of the 73 entities originally selected for review paid Connection Fees in recent years, all of the entities were presumed to pay monthly sewerage charges, so IA tested the monthly sewerage billing system for all 73 entities to determine whether monthly billing is in fact taking place and the appropriate categories and rates for monthly volumetric fees are used. IA noted:

#### **Entity with no sewerage billing (1 of 73 items tested):**

Although not technically a monthly sewerage billing error, Fuji Natural Foods, Inc. was found to have paid Connection Fees in 2011 but was not being billed for monthly sewerage. City of Ontario representatives indicated that this entity uses well water and a septic system and is located in the Jurupa Community Services District, not IEUA’s. Ontario representatives indicated that they would perform additional research on the Connection Fees that were collected.

**Monthly Sewerage Findings:**

ISSUE		DESCRIPTION	# OF ITEMS	% OF TOTAL
<b>Errors and anomalies:</b>				
a	Restaurants not billed at restaurant rate	Master meter or different prior use (See table below for impact on fees)	4	5.48%
b	Funeral home & health clinic	Commercial factor used (See table below for impact on fees)	2	2.74%
c	Bakery	Billed at Laundromat factor (See table below for impact on fees)	1	1.37%
d	For-Profit college	Used medical office rate (Category 7 - .0671 HCF) rather than Schools rate (Category 9 - .0185 x # of students)	1	1.37%
e	Church in a commercial complex	Included on commercial master meter (Category 1 - .0729 HCF rate) rather than Church rate (Category 3 - .0626)	1	1.37%
<b>New industrial and manufacturing entities in Ontario:</b>				
	Commercial/Industrial businesses with fixed or other unusual rate structures	Additional information provided below	9	12.33%
Tested with no exceptions:			55	75.34%
<b>TOTAL TESTED</b>			<b>73</b>	<b>100.00%</b>

**Errors and anomalies:** The table above shows that in nine (or 13%) of the 73 items, an inaccurate billing factor was used.

Although the findings were confirmed only for the individual billing period examined (April 2014 monthly billing), all of these findings become magnified over time impacting the volumetric sewerage fees paid to IEUA. IA was able to recalculate the billings for seven of the items noted (a through c above):

	Businesses for which adequate information was available for recalculation of monthly sewerage billing	Estimated Monthly Amount Should Have Been	Monthly Amount Actually Billed	Estimated annualized bill (multiply by 12 months)	Estimated annualized actual fees (multiply by 12 months)	Estimated Amount (under-collected) and (underpaid) IEUA for 12 months
a	Fast 5 Pizza	\$ 23.72	\$ 16.60	\$ 284.64	\$ 199.20	(\$ 85.44)
a	Home Pie Bakery/Cafe	\$ 366.95	\$ 256.69	\$ 4,403.40	\$ 3,080.28	(\$ 1,323.12)
a	Miguel's Jr.	\$189.75	\$132.69	\$ 2,277.00	\$ 1,592.28	(\$ 684.72)
a	J & R Deli	\$ 62.79	\$ 43.92	\$ 753.48	\$ 527.04	(\$ 226.44)
b	Continental Funeral Home	\$ 107.06	\$ 74.18	\$ 1,284.72	\$ 890.16	(\$ 394.56)
b	Office/Medical Building	\$ 115.87	\$ 125.91	\$ 1,390.44	\$ 1,510.92	\$ 120.48
c	Camacho's Bakery	\$ 189.75	\$ 113.95	\$ 2,277.00	\$ 1,367.40	(\$ 909.60)
<b>TOTAL ESTIMATED ANNUALIZED DIFFERENCE (for 7 items):</b>						<b>(\$ 3,503.40)</b>

Enrollment information was not obtained for the For-Profit College (d), so an alternate monthly sewerage amount could not be estimated. The church in the commercial complex (e) is included under a commercial master meter, so the church's individual billing amount could not be estimated.

*Contracting Agencies should review their Utility Billing Systems on a regular basis to ensure that all business and residential properties are being billed for sewer services and make any needed corrections. The City of Ontario should review its Utility Billing system from time to time to verify all active sewer accounts have been captured and billing is in alignment with those receiving sewer services. Additionally, the City should*

*ensure that any residential or commercial properties connected to the sewerage system are included in the reporting of EDU's to IEUA as part of the Volumetric Sewerage Fees according to the requirements of the Regional Contract.*

*IEUA should consider including language in the Regional Contract regarding recourse for non-payment for services provided and work closely with the Contracting Agencies to ensure there are reconciliation and verification controls to ensure all sewer services are reported and paid accurately and according to the requirements of the Regional Contract.*

**New industrial and manufacturing entities in Ontario:** There is a need to provide clarity and improve guidelines for industrial enterprises to ensure that Connection Fees and monthly sewerage charges are assessed correctly, are fair and equitable, and are determined in accordance with the intent of the Regional Contract.

IA noted 9 industrial entities (12.33% of the items tested) with fixed or other unusual monthly sewerage rate structures. In addition to requesting additional information about monthly sewerage rates from Ontario staff, IA also considered the Connection Fees collected from these entities.

**Connection Fees:** A purpose of the Regional Contract is to ensure Connection Fees are assessed and collected consistently and uniformly by all Contracting Agencies. Exhibit J was revised as of June 19, 2013, to provide clarity and guidance in selecting category types and collecting Connection Fees more consistently throughout the region.

Exhibit J states that Connection Fees for industrial enterprises are calculated based on a two-part formula. The domestic wastewater EDUs are calculated in the traditional manner according to the number of fixture units multiplied by an assigned sewage factor (0.0741). The second part of the formula is for industrial wastewater (non-domestic) and utilizes a calculation based on sewer flow, Biochemical Oxygen Demand (BOD) and Total Suspended Solids (TSS) levels shown on the industrial waste permit:

**Exhibit "J" (Amended 6/19/13):  
Equivalent Dwelling Unit Computations  
General: Paragraph 3. Industrial**

3. Industrial. All structures designed for the purpose of providing permanent housing for an enterprise engaged in the production, manufacturing, or processing of material. EDU's for industrial users shall be determined as follows:

a. For domestic type wastewater, multiply the fixture units (as defined by Table 1) shown on the approved building plans by a sewage factor of 0.0741, based on a 20 gallons per fixture unit flow per day.

b. For non-domestic wastewater, compute from information contained on the industrial waste permit, using the following formula:

$$\text{EDU} = \frac{\text{Estimated non-domestic flow}}{270} \left[ .37 + .31 \frac{\text{BOD}}{230} + .32 \frac{\text{SS}}{220} \right]$$

c. Combine the resultant EDU's derived from a and b above.

As an example, Evolution Fresh is a juice manufacturer owned by Starbucks located in the Cucamonga Valley Water District (CVWD). As described in the interim report for CVWD this entity was assessed a total of 233.96 EDUs and fees of \$1,148,510 using the methodology from Exhibit J. The domestic EDU calculation amounted to 9.67 EDUs and fees of \$47,470 and the industrial BOD/TSS calculation amounted to 224.29 EDUS and fees of \$1,101,040.

**Monthly sewerage charges:** The 1997 Sewerage Billing memorandum states that monthly sewerage charges for industrial enterprises are also calculated based on a two-part formula. The domestic wastewater EDUs are calculated in the traditional manner according to the amount of water consumption multiplied by an assigned sewage factor (0.0729). The second part of the formula is for industrial wastewater (non-domestic) and utilizes a calculation based on sewer flow, BOD and TSS levels shown on the industrial waste permit recalculated on a yearly basis:

**Procedures for Establishing a Regional Sewer Billing Formula (1997)  
 Chino Basin Regional Sewer Service Program  
 Volumetric Equivalent Dwelling Unit (EDU) Calculation  
 Industrial Users**

**CHINO BASIN REGIONAL SEWER SERVICE PROGRAM  
 Volumetric Equivalent Dwelling Unit (EDU) Calculation  
 Industrial Users**

1. Industry: Shall be defined for purposes of this exhibit, as those industries identified in the Standard Industrial Classification Manual, Bureau of the Budget, 1967, as amended and supplemented, under the category "Division D - Manufacturing" and such other classes of significant waste product as, by regulation, the Administrator deems appropriate. EDU's shall be determined as follows:

Total EDU's = a + b

a. Domestic Wastewater EDU's are calculated using Category #1 on Table 1.

b. Non-domestic Wastewater EDU's are calculated as follows:

<u>Non-Domestic Flow</u>	(0.37 + 0.31 BOD + 0.32 SS)
270	230    220

2. Procedures for establishing industrial wastewater strength charges shall be as follows:

a. If required by the Contracting Agency, any Non-residential User may be required to submit on a yearly basis (on or before the first of July of every year), a 24-hour composite wastewater analysis performed by a certified laboratory. Said analysis shall be for BOD, SS and/or any other parameter as may be required by Contracting Agency Ordinance. The results of this analysis may be used to adjust the equivalent dwelling units for any category of the Non-residential User. The frequency of wastewater analysis samples submitted may vary depending on the type of industrial discharge as determined by the Contracting Agency.

Continuing with the Evolution Fresh example; CVWD bills customers on a bi-monthly basis. In Spring of 2014 the Evolution Fresh paid domestic sewerage fees of \$72 (\$36 monthly equivalent) and industrial sewerage fees of \$14,976 (\$7,488 monthly equivalent).

In selecting items for testing, IA found that Ontario is home to the largest number of industrial entities in the region. IA selected a total of 10 industrial entities in Ontario. The Connection Fees and monthly sewerage charges for these enterprises varied widely and were generally much lower than those of similar entities located in other Contracting Agencies, such as Evolution Fresh.

Ontario staff provided IA with copies of the "Uniform Industrial Wastewater Survey" reports that had been prepared to support the BOD and TSS calculations for the

Connection Fee payments for the selected entities tested by IA, other than Haliburton. IA noted that in all cases these fee calculations were significantly lower than the calculation in the example of Evolution Fresh. According to City staff additional Connection Fees based on industrial factors are still being negotiated with Haliburton (see also additional information later in this report).

In response to IA's questions, Ontario staff provided some information about the monthly sewerage fee calculations for the industrial entities tested which is included in the table below. IA discussed the responses with IEUA's Planning and Environmental Resources staff, but concludes that there is not enough information to replicate Ontario's calculations.

Without additional information it is impossible for IA to determine whether the monthly sewerage fees are being applied in accordance with the 1997 Sewerage Billing memorandum. However, based on the information obtained from the City's staff it appears that there are inconsistencies in the billing practices between the different industrial entities.

IA and Planning and Environmental Resources staff noted that responsibility for setting monthly sewerage rates for industrial customers varies at the individual Contracting Agencies and requires judgment using sampling results. Additionally the information IEUA receives about monthly sewerage billing practices at the individual Contracting Agencies is too limited to make it possible for IEUA to perform any oversight.

*As part of renegotiating the Regional Contract, the Agency should standardize the Monthly Sewage report to require that Contracting Agencies provide sufficient information to track customer history from the time of initial connection through on-going/monthly services. The standardized monthly information should require that each non-residential business be identified with the total number of EDUs reported for the month.*

*IEUA Planning and Pre-Treatment groups should take the lead to exercise the authority provided under Regional Contract Section 26 Inspection of Facilities, and establish an on-going monitoring program to inspect random facilities or those where there is a suspected discrepancy in order to ensure the intent of the Regional Contract is applied and ensure the integrity of the Regional Program.*

**THE CITY OF ONTARIO: INDUSTRIAL AND MANUFACTURING BUSINESSES  
INITIAL CONNECTION FEES AND MONTHLY SEWERAGE BILLING**

Business	Address	Description	Connection Fees Noted	Monthly Billing Example	April 2014	Ontario Comment
Niagara Bottling <sup>(a)</sup>	2560 E. Philadelphia Ave.	Water bottling company	Commercial from 3/2006 to 6/2013: \$33,331	April 2014: Fixed 66 EDUs rate	\$883.74	Fixed EDU determined by permit, measurement and inspection. If use the NRW, then usually use a fixed factor.
New-Indy Ontario llc <sup>(a)</sup>	5100 E Jurupa St.	Paperboard Mill	In existence for extended period <sup>(b)</sup>	April 2014: Fixed 47 EDUs rate	\$629.33	Same as above.
Greif	3042 E. Inland Empire Blvd.	Packaging supply	In existence for extended period <sup>(b)</sup>	No April 2014 billing for water or wastewater.	\$0.00	Part of a master meter.
Zurn Industries	3690 E. Jurupa St.	Liquid waste disposal systems supplier	Per building permit fixtures established in 2001 <sup>(b)</sup>	April 2014: 2 meters: one with 5 HCF @ .0401 Factor & other with 0.	\$2.68	Use landscape factor (55%). Recently converted to recycled water.
Jogue, Inc.	4142 E Pacific Privado	Flavoring Syrups & Concentrates	June 2013: Domestic Industrial- \$10,313 Industrial-\$63,884	April 2014: 88 HCF @ .0202 Factor	\$23.80	Monthly based on 68% flow to sewer, 2,100 BOD and 31 TSS per lab data.
Wing Hing Foods	2539 E. Philadelphia St. (former Haliburton site.)	manufacturer of Chinese foods & noodles	March 2007: \$5,967 (originally purchased by Haliburton) April 2013: Industrial \$31,518	April 2014: 221 HCF @ .0087 Factor	\$25.74	Monthly based on lab data showing BOD=530mg/l, TSS=50mg/l and water to waste factor of 8.25%.
Haliburton	3855 E. Jurupa	Manufacturer of soups & sauces	Commercial and Domestic industrial purchased from 2011 – 2013 \$69,043	April 2014: Fixed 186 EDU rate	\$2,490.54	Fixed industrial EDU was determined for monthly billing.
Tropicale Foods	1237 W. State St.	Manufacturer of fresh fruit & ice cream bars	Commercial connections from 2007 – 2010: \$6,177	April 2014: 2,651 HCF @ .5902 factor (August 2014: 3,984 HCF @ .0411 factor reducing bill to \$2,356.25)	\$20,950.26	Industrial assessment was conducted between April and August to reassess based on new pretreatment activities and "SOPs" regarding discharge.
American Jerky	2400 E. Francis St.	Manufacturer of chicken based pet treats.	2014: Domestic industrial and industrial: \$168,070.72	May 2014: First month billed for 91 HCF at office/ commercial factor of .0729	\$88.78 (May – 1 <sup>st</sup> month available)	New industrial not in production yet.

<sup>(a)</sup> Also pay fees for industrial waste disposed through the non-reclaimable wastewater program  
<sup>(b)</sup> Facilities in existence for extended period of time. Connection Fees not tested

IA noted that confusion and a lack of clarity about assessing Connection Fees and calculating monthly sewerage charges for Industrial entities is not limited to Ontario:



- City of Ontario staff noted that IEUA Connection Fees can be an impediment to businesses locating or relocating to their community impacting the City's goal of encouraging job growth, specifically the industrial waste permit based on Biochemical Oxygen Demand (BOD) and Total Suspended Solids (TSS), since in their experience this has resulted in fee calculations that businesses believe to be prohibitively high.
- Another Contracting Agency noted that proximity to one of the two Non-Recyclable Waste Systems (NRWS) can impact the costs to a business in terms of their desire to connect to that system rather than the regional sewerage system.
- Another Contracting Agency commented that Connection Fees paid by industrial entities based on BOD and TSS are not related to Fixture Units in the traditional sense and guidance is unclear about how these would be transferred or owned if a building is sold to a new owner or if an owner wants to transfer these to a new location or if the industrial equipment is removed.
- Another Contracting Agency commented that it is unclear what value an industrial entity receives for its previously purchased capacity as a Significant Industrial User (SIU) when it is declassified from being one or for the EDUs previously purchased when becoming an SIU.

Additionally, the number of industrial entities in the region is expected to grow in coming years, magnifying the impact on fees. According to John Husing, chief economist for the Inland Empire Economic Partnership:

**(The following is from an article in the Los Angeles Times on March 20, 2015.)**

The local logistics industry could even help boost lagging manufacturing employment. Husing said.

The production process is increasingly being broken up and scattered around the world. Husing believes that the Inland Empire distribution warehouses could do double duty as factories where various component parts are assembled into a final product and delivered to customers.

Industrial vacancy rates in the Inland Empire have fallen to 4.5% from 12.8% during the recession. As of December, 16.9 million square feet of industrial space was under construction in the region – 80% of the total for Southern California.

*IA recommends that IEUA and the Contracting Agencies compare and contrast the Connection Fees and monthly sewerage charges from being an industrial entity that is part of the regional sewer system to the fees and charges paid for contracting with either of the two NRWS lines, particularly for similar types of businesses and consider options to ensure that fees and charges are fair, equitable, determined in accordance*

*with the intent of the Regional Contract, and not a detriment to businesses considering a location in the Inland Empire.*

*IA recommends that IEUA and the City of Ontario work together to resolve their differences regarding the calculation and collection of Connection Fees and monthly sewerage charges for all commercial and public service categories, but particularly for manufacturing and industrial entities.*

*In addition to the regular meetings of the Regional Technical and Regional Policy Committees, IEUA has already begun to provide ad-hoc meetings and training as needed for things such as the updated excel Building Activity Report and the Exhibit J subcommittee. IA noted that great variability and understanding of IEUA, the Regional Contract and Exhibit J exists amongst Contracting Agencies' staff in departments such as Building, Plan Check and Utility Billing. IA recommends that IEUA take the lead to, hold workshops, meetings, plant tours and similar activities as an avenue where the Contracting Agencies' staff in departments such as Building, Plan Check and Utility Billing and/or others as well can discuss and ask questions about the application of the Regional Contract and Program. The workshops will provide a forum to discuss questions about the category types to apply, questions on definitions, other questionable items related to individual situations, as well as foster cooperation and collaboration among all. One Contracting Agency may encounter questions or situations that could apply to other Contracting Agencies. Frequent and on-going dialogue about the application of the Regional Contract would benefit all Contracting Agencies and the Regional Program to ensure consistent application of the Regional Contract and that issues are addressed on a timely basis.*

In testing recurring sewer service fees, IA also noted:

**Minimum sewer service fees based on one EDU: It would seem appropriate that a commercial customer be billed, at the minimum, the rate for 1 EDU which is used for a residential customer, even if the commercial consumption is lower than one calculated EDU.**

All residential customers are billed 1 EDU (.7 for multi residential) regardless of water consumption or actual use or waste flow. The audit noted instances where commercial customers are billed a lower amount than what a residential customer pays.

Commercial customers are billed converting water consumption into EDUs. Sometimes the calculations produce a fraction of an EDU (less than 1 EDU). The rate is applied to the calculated EDU or fraction of an EDU and the commercial customer is billed accordingly.

The monthly sewerage fee for a single EDU in the 2013/2014 fiscal year was \$13.39, yet IA noted commercial entities with billings as low as:

<b>Business</b>	<b>Monthly Billed Amount</b>
Excel Industries, Inc.	\$ 9.77

Nesco, LLC	\$ 2.01
Astrophysics, Inc	\$ 0.94
Minsly, Inc	\$ 2.01
Anjuman E. Qutbi Mosque	\$ 12.59
Jack Sweeney/Dynateck	\$ 0.94
Zurn Industries	\$ 2.68
1690 Milliken	\$ 2.01

*IA noted that Cucamonga Valley Water District and the City of Montclair both bill a minimum base amount of one EDU per month to commercial enterprises even if the amount determined through water usage would be lower under the rationale that no business should pay less than the amount charged to a single family residence.*

**Sewer service billing category inconsistencies:** There is an inconsistency between the rate charged for Connection Fees and the rate used for monthly sewerage billing.

The billing formulas are based on the memorandum “Procedures for Establishing a Regional Sewer Billing Formula” from 1997. The formulas are divided into Residential, Commercial and Industrial categories and the Commercial categories are further divided into eight Commercial categories and an additional category for schools. Category eight includes: “Restaurant – full service; Restaurant – Fast food; Market w/ grinder; and Bakery”.

*IA notes that the inclusion of both full service and fast food restaurants in the same classification for monthly sewerage contradicts the guidance provided for Connection Fees where full service restaurants are charged a significantly higher sewage factor to connect than are fast food restaurants. In general, full service restaurants would probably pay higher monthly fees from higher water consumption even though their sewer factor is the same as for fast food restaurants, however the rate classification structure does lump them together in the same category. As part of renegotiating the Regional Contract, IEUA and the Contracting Agencies should evaluate and consider the relationship between monthly Sewer Service Fees and Connection Fees and determine the need to create a correlation between the two.*

*IA notes that documentation approving and mandating the billing methodology is not available. Any revision should be presented to the IEUA Board of Directors and formally adopted, based upon the recommendation of the Regional Technical Committee.*

### **Haliburton Foods**

During the original planning for this review, the IEUA Planning and Environmental Resources Department requested IA determine the number of EDUs purchased by Haliburton Foods. IA performed a review of Building Activity Reports from December 2011 through June 2013 that found \$69,042.82 in total Connection Fees for 250 fixture units amounting to 14.2482 EDUs. In addition City of Ontario staff provided a prior permit for 3855 E. Jurupa Ave. for 18 fixture units, 0.7992 EDUs and \$3,734.66 in fees (probably paid for construction of the original shell building). In connection with these procedures, IA had the following recommendations:

*As part of renegotiating the Regional Contract, the Agency may want to consider adding provisions for the collection of additional EDUs for existing fixture units at the higher rates in situations where a change in category of usage occurs, at a minimum in situations where the building has had no prior occupants.*

*As part of renegotiating the Regional Contract, the Agency should standardize the Monthly Sewage report to require that Contracting Agencies provide sufficient information to track customer history from the time of initial connection through on-going/monthly services. The standardized monthly form should require that each non-residential business be identified with the total number of EDUs reported for the month.*

*IEUA Planning and Pre-Treatment groups should take the lead to exercise the authority provided under Regional Contract Section 26 Inspection of Facilities, and establish an on-going monitoring program to inspect random facilities or those where there is a suspected discrepancy in order to ensure the intent of the Regional Contract is applied and ensure the integrity of the Regional Program.*

As a result of conversations with City of Ontario staff, IA understands that the City of Ontario is in discussions with Haliburton about the classification and additional fees owed. Therefore, IA did not perform additional procedures as part of this review.

### **Total Sewer Service Fee Billings/Revenue**

As part of the review, IA attempted to compare the Sewer Billing Revenues recorded by IEUA for agreement to the City of Ontario's CAFR information to determine if all sewer related collections/billings by the City are paid to (or "passed-through") and reported to IEUA. The City of Ontario records all Sewer Service Revenue into one fund, which includes IEUA's treatment fee, local sewer service fees, stand-by fees, and local sewer capital replacement fees.

IA was unable to reconcile Sewer Service Revenue recorded by IEUA with the Contracting Agency's CAFR information because of the multiple types of revenue combined into one fund by the City.

Additionally, IA noted the following variances between the Contracting Agency's CAFR expenses and the revenues recognized by IEUA that are based upon Monthly Sewer Billing Reports submitted to IEUA:

IEUA Revenue compared to Ontario Expense FY 2012/13 (Jul 1, 2012 through June 30, 2013)		
Sewer Utility Revenue ending balance from IEUA SAP for City of Ontario	Sewer Utility Expense ending balance per City of Ontario's CAFR	Balance Variance over/(under) paid to IEUA
\$ 8,770,935	\$ 8,782,140	\$ (11,205)

IEUA Revenue compared to Ontario Expense FY 2013/14 (Jul 1, 2013 through June 30, 2014)		
Sewer Utility Revenue ending balance from IEUA SAP for City of Ontario	Sewer Utility Expense ending balance per City of Ontario's CAFR	Balance Variance over/(under) paid to IEUA
\$ 9,532,321	\$ 9,844,757	\$ ( 312,436)

IA did not receive information from City of Ontario staff about the reasons that utility expense recorded by the City is higher than the amount billed by and shown on the IEUA accounts.

**CAFR Reconciliation**

IA verified that the CCRA amounts reported on the City's CAFR agree to what IEUA reported on its CAFR at June 30, 2013 and June 30, 2014. The balance on both reports was \$3,337,340 at June 30, 2013.

At June 30, 2014 the City of Ontario's CAFR showed a balance of \$3,935,945 with additional accounts payable of \$1,075,788. These two amounts agree in total to the \$5,011,733 shown in IEUA's CAFR. The accounts payable amount shown by Ontario agrees to the "Capital Call" amount requested by IEUA for the third quarter of 2014.

**Extra-Territorial Fees**

The City of Ontario has no Extra-Territorial areas and does not charge Extra-Territorial (ET) fees. In recent years the City has annexed some previously unincorporated areas, but these were not considered ET areas as described in the contract.

### **Internal Audit Recommendations**

Through this evaluation, IA noted observations and recommendations to strengthen administrative, accounting, recording, and reporting controls to ensure the intent of the Regional Contract is achieved. The recommendations can be applied to all Contracting Agencies going-forward, as part of an amendment and/or as part of the Regional Contract review and renegotiation process; in order to ensure all Regional Contracting Agencies apply and administer the Regional Contract in a similar and consistent manner. IA's recommendations are for IEUA's Executive Management to consider.

#### ***Recommendations relating to Connection Fees:***

***As part of the review and renegotiation of the Regional Contract, IEUA and the Contracting Agencies should:***

- 1. In addition to the regular meetings of the Regional Technical and Regional Policy Committees, IEUA has already begun to provide ad-hoc meetings and training as needed for things such as the updated excel Building Activity Report and the Exhibit J subcommittee. IA noted that great variability and understanding of IEUA, the Regional Contract and Exhibit J exists amongst Contracting Agencies' staff in departments such as Building, Plan Check and Utility Billing. In order to develop greater consistency and uniformity throughout the region, IEUA should consider taking the lead in holding quarterly or more regular workshops, meetings, plant tours and similar activities as an avenue where Contracting Agencies' staff in departments such as Building, Plan Check and Utility Billing and/or others as well can discuss and ask questions about the application of the Regional Contract and Program. The workshops would provide a forum to discuss questions about category types to apply, definitions, other questionable items and individual situations, and foster cooperation and collaboration among all. One Contracting Agency may encounter certain questions or situations that could apply to other Contracting Agencies. Frequent and on-going dialogue about the application of the Regional Contract would benefit all Contracting Agencies and the Regional Program to ensure consistent application of the Regional Contract and that issues are addressed on a timely basis.***
- 2. Add language in the Regional Contract regarding recourse for non-collection, in addition to over/under collection of Initial Connection Fees.***
- 3. Develop a standardized calculation worksheet to create uniformity among the Contracting Agencies with fixture unit counts and the connection fee calculations. Currently, each Contracting Agency utilizes its own calculation worksheet and it is not always consistent with Regional Contract Exhibit J. The standardized calculation worksheet should mirror the fixture unit types in Exhibit J and provide additional clarification and uniformity to the fixture count process. The worksheet should be flexible enough to allow for multiple components of a business to be calculated at***

***different Commercial categories when there is more than one type of business at the same location (for example, a gas station/minimart with a car wash). The standardized calculation worksheet will facilitate computing the Connection Fees in a consistent and uniform manner.***

- 4. Require the inclusion of the connection calculation worksheets for all nonresidential entities with monthly Building Activity Reports as additional support for the connections reported and the Connection Fees collected. This would provide IEUA staff greater visibility and documented support for the application of the category types and the fixture counts. This process would also allow IEUA staff to contact the Contracting Agency if any questions or discrepancies are noted at the time that connections are reported rather than identifying these later on.***
- 5. Exhibit J was recently updated and now provides detailed definitions for many business types, yet there is still room for varying interpretation and application. Businesses continue to evolve and new types of businesses emerge. Exhibit J should be updated regularly to provide additional language, definitions and guidance to ensure all types of commercial businesses are classified consistently. This would reduce the risk of misclassification of businesses and the potential under-collection of IEUA fees. Examples include private community centers, swimming facilities and recreation centers in residential communities. Ontario's practice has been to classify these as category III which includes descriptions such as "health spa with pool" whereas the City of Chino included these in category I along with fast food restaurants, stores and offices.***
- 6. Provide additional clarification and descriptive information for the various types of appliances, appurtenances and/or fixtures in the descriptions included in Exhibit J. Examples include; defining the nature of an emergency drain (The City of Ontario charges two Fixture Units for all floor drains under the general "Floor Drain" category whereas in the City of Upland all California State Plumbing Code required drains such as in bathrooms are considered "Emergency" and are charged zero Fixture Units.), clarifying differences between lavatories, wash fountains, receptors, sinks and mop basins and defining whether a drinking fountain that includes a separate basin for handicapped access consists of one or two fountains. The review revealed differences in interpretation.***
- 7. Consider a two-step process of determining Connection Fees as part of Exhibit J that distinguishes between common features that are part of any commercial facility such as restroom toilets & sinks (i.e. a toilet is always the same cost regardless of type of business whether a restaurant, office or gym) vs. those features that are unique to a specific site, such as a butcher shop drain or a restaurant dishwasher or washing sink, etc. This***

**would create consistency in the treatment of same-type and same-use fixture units.**

- 8. Develop significant expertise within IEUA in fixture count techniques and providing regular and ongoing training at the building departments of the individual Contracting Agencies to develop consistency in the IEUA fixture count process across the region.**
- 9. Consider, as part of the permitting and plan check process, a requirement that an IEUA representative provide final sign-off and approval prior to the Contracting Agency issuing a permit to a nonresidential entity and allowing a connection to the regional system. This added approval step will ensure IEUA agrees with the interpretation of the contract and the appropriate category type and sewage factor have been applied so correct connection fees are assessed and collected.**
- 10. Have IEUA Planning and Pretreatment groups take the lead to exercise the authority provided under Regional Contract Section 26 Inspection of Facilities, and establish an on-going monitoring program to inspect random facilities or those where there is a suspected discrepancy in order to ensure the intent of the Regional Contract is applied and ensure the integrity of the Regional Program.**
- 11. Compare and contrast the Connection Fees and monthly sewerage charges associated with being an industrial entity that is part of the regional sewer system to the fees and charges paid for contracting with either of the two NRWS lines (including transportation costs and distance), particularly for similar types of businesses and consider options to ensure that fees and charges are fair, equitable, determined in accordance with the intent of the Regional Contract and not a detriment to businesses considering a location in the Inland Empire. Additionally, clarifying the relationship between EDUs and “paying for capacity” would assist the Contracting Agencies and businesses considering locating in the region to understand their costs at the outset.**

Although the City of Ontario collected Connection Fees for other types of Public Service Facilities, the City did not collect Connection Fees for new construction at the public schools selected for testing.

**Recommendations relating to Public Service Facilities:**

**As part of the review and renegotiation of the Regional Contract IEUA and the Contracting Agencies should consider:**

- 12. The legal and financial impacts of excluding Public Service Facilities from the charge for Connection Fees and monthly sewerage charges. As documented under the audit report “Comparison of the Regional Sewage**



***Service Contract and Program with similar contracts and programs”, IA found that some Agencies (for example, the Los Angeles County Sanitation Districts) exclude local governmental agencies such as public schools (Kindergarten through 12<sup>th</sup> grade and community college) and City governments from both Connection Fees and monthly sewerage charges.***

- 13. Adding language to the Regional Contract regarding IEUA’s inspection and verification rights for Public Service Facilities as to Connection Fees and monthly sewer fees and the recourse IEUA has when IEUA believes a Contracting Agency has under-collected and/or under-reported such fees.***

IEUA sewerage revenue from the seven Regional Contracting Agencies totaled almost \$43 million for the 2013/14 fiscal year, yet IEUA relies entirely on a one-page self-reported monthly EDU count from the Contracting Agencies to generate invoices for these revenues with no significant oversight or reconciliation. Once these self-reported EDU totals are provided to IEUA (generally approximately 15 days after the end of the month), IEUA generates invoices that are mailed to each of the Contracting Agencies. The Contracting Agencies then have 45 days to remit their payments. The following recommendations are intended to improve and make this process more efficient:

***Recommendations relating to sewer service fees:***

***As part of the review and renegotiation of the Regional Contract IEUA and the Contracting Agencies should consider:***

- 14. Establishing the collection of monthly sewer service fees for the entire region directly through the County’s Property Tax Roll. Collection of sewer service fees through the property tax roll could result in a more efficient process and reduce the administrative resources used by Contracting Agencies in billing and collecting for these fees. Residential properties could be transferred initially until consideration is given to ways in which and whether to transition fees from commercial, industrial and other entities.***
- 15. Evaluating the methodology used for billing monthly sewerage fees and possible alternatives; either by water consumption or EDUs purchased. Since the adoption of the existing billing methodology in a 1997 memorandum there have been greater efficiencies achieved in water usage, which may have an impact on the type and amount of sewerage discharged and the types of services provided to the region as a whole. The billing methodology should be aligned with the services provided. The billing methodology should be presented to the IEUA Board of Directors and formally adopted, since the Regional Contract specifies that the role of the Regional Technical Committee is to make recommendations.***
- 16. Updating the 1997 memorandum to consider new business types and provide more detailed definitions and descriptions. Since the adoption of***

***the 1997 memorandum, businesses have continued to evolve and new types of businesses emerge. The 1997 memorandum should be updated regularly to provide additional language, definitions, and guidance to ensure all types of commercial businesses are classified consistently. IEUA should consider documenting additional definitions and descriptions to the classification of businesses in the 1997 memorandum.***

- 17. How and which customers are billed for sewerage services. As an example the Los Angeles County Sanitation Districts do not bill local governments and schools for monthly sewerage services. As another example Paso Robles and the City of Mill Valley are measuring residential water flows during winter months to develop a differentiated rate structure for residential customers as opposed to the uniform 1 EDU per residence no matter what size utilized by IEUA. Conversely, the City of Fontana bills all customers, residential and commercial, a fixed billing amount based upon the number of EDUs purchased.***
- 18. Evaluating the relationship between monthly sewer service fees and Connection Fees. For example fast-food restaurants and full-service restaurants are both included in Category 8 for monthly sewerage billing purposes and pay at the same rate. However, for purposes of Connection Fees fast-food restaurants are grouped with office, retail and similar uses (which are Category 1 for monthly sewerage billing). Therefore, fast-food restaurants incur lower Connection Fees, but pay monthly sewer service fees at the higher rates charged to full-service restaurants. Such inconsistencies between Connection Fees and monthly sewerage charges could lead them to be challenged.***
- 19. Evaluating the need to provide additional guidance for locations serviced by a master meter. In these, generally mall-like locations, multiple types of businesses are all serviced by a single connection. Consideration should be given to providing billing guidance in these instances, possibly through a blended volumetric rate or utilizing the highest volumetric rate applicable to the businesses at that location or considering some other methodology.***
- 20. Adding language to the Regional Contract regarding IEUA's inspection and verification rights as to the monthly sewerage fees and the recourse IEUA has when IEUA believes a Contracting Agency has under-collected and/or under/reported such fees.***
- 21. Determining the most appropriate methodology for billing commercial businesses that do not consume or discharge a minimum of one EDU. Currently, two member agencies bill a minimum base of one EDU determined by water consumption under the rationale that no business should pay less than the amount charged to a single family residence; while all others bill based on actual consumption. Provide contracting***

**agencies' clear guidance, in the Regional Contract, as to the most appropriate methodology to ensure all contracting agencies' bill commercial customers in a consistent and uniform method.**

- 22. Standardizing and providing automated and itemized listing of non-residential monthly sewerage charges to provide information that could be reviewed and researched for anomalies and reconciled on a regular basis.**
- 23. Evaluating the current process used for invoicing each Contracting Agency for monthly sewer fees collected. By establishing a contract for monthly payment instead of relying on the invoice process, each Contracting Agency could provide the EDU information and remit the funds collected to IEUA directly within a reasonable period of time; instead of waiting for an invoice that delays payment for up to 45 days. By reengineering the process, IEUA would receive the monthly sewer fees collected by the Contracting Agencies in a more efficient and timely manner.**

Although this is not a financial audit, and IA makes no recommendations to the City of Ontario, the following are suggested recommendations for the City of Ontario's consideration.

**Recommendations for consideration by the City of Ontario:  
The City of Ontario should:**

- 24. Work to resolve issues regarding the calculation and collection of Connection Fees and monthly sewerage charges for manufacturing and industrial entities.**
- 25. Work together with the local School Districts to determine and collect any additional Connection Fees that are due to IEUA as required by the Regional Contract.**
- 26. Examine and restructure the Connection Fee calculation and collection process to ensure that the fixture unit counts are correctly tallied, the categorization of businesses is appropriate and that connection fees are not under-collected. The current procedure omits the step of verifying that the Connection Fee calculation conforms to the building/plumbing plans.**
- 27. Ensuring all current customers receiving sewer services are reported on the Monthly Volumetric report and the appropriate rates are paid to IEUA, according to the Regional Contract. Work together with IEUA to resolve the accounts identified in this review, where there is no indication that monthly sewer fees are paid to IEUA.**
- 28. Consider the City of Upland's cross-departmental approach to the Development Review Process. This team approach to the Development**

***Review Process (or, alternatively a liaison relationship with the Fire Department which seems to play a role even with Public Service Facilities) facilitates obtaining information about new Public Service Facilities construction to ensure fee collection.***

### **Acknowledgements**

We would like to extend our appreciation to the City of Ontario and the IEUA Planning and Environmental Resources Department for their cooperation and assistance during this review.

### **Discussions with City of Ontario and Planning & Environmental Resources**

We provided the results of this audit to Mr. Michael Sigsbee, Utilities Admin Services Manager, Mr. Kevin Shear, Building Official and Ms. Delilah Patterson, Revenue Services Director for their review and comments prior to finalizing the report. We also discussed the report with Chris Berch, Executive Manager of Engineering/Assistant General Manager, Sylvie Lee, Manager of Planning and Environmental Resources, Craig Proctor, Pretreatment and Source Control Supervisor, Pietro Cambiaso, Senior Engineer and Kenneth Tam, Environmental Compliance Officer of the IEUA Planning and Environmental Resources Department prior to finalizing this report, for their review and comments.

### **Action Items**

IA will submit a separate report for each of the seven Contracting Agencies as each review is completed. At the conclusion of the audit of all seven Contracting Agencies, IA will provide a comprehensive report summarizing all the identified observations and recommendations and any additional observations and recommendations identified throughout this process. IA anticipates finalizing the seven audit reports by June 2015 and the final report thereafter; in the meantime the recommendations provided in this report should be evaluated and considered at this time.

**Attachment 1**

**REGIONAL CONTRACT REVIEW:  
 CITY OF ONTARIO  
 REVISED CALCULATION WORKSHEET**


Regional Contract Review			
Site	Facet	Unit	Value
Site #	Facet #	Unit #	Value
<b>Regional Contract Review - Worksheet: Fixtures - Plumbing (1 of 1)</b>			
Fixture	Quantity	Category	Value
Automatic Clothes Washer Qty	1	1	1
Bathub Showers Qty	1	2	2
Drainage Unit Qty	1	3	3
Dishwasher Qty	1	4	4
Breakup Footfall Qty	1	5	5
Floor Drains Qty	1	6	6
Floor Sinks Qty	1	7	7
Laundry Sinks Qty	1	8	8
Lavatory Qty	1	9	9
BB Park Trap-Over Trailer Qty	1	10	10
Shower Qty	1	11	11
Sink Service Hot Qty	1	12	12
Sink Food Waste Qty	1	13	13
Urinal Qty	1	14	14
Wash Sink Circular Qty	1	15	15
Water Closet-Home Metal Qty	1	16	16
Water Closet-Commercial Qty	1	17	17
<b>Fixture Units Total</b>			<b>40.0</b>

**INFORMATION  
ITEM  
2B**

Date: September 16, 2015

To: The Honorable Board of Directors

Through: Audit Committee (9/9/15)

From:   
Teresa V. Velarde  
Manager of Internal Audit

Subject: Follow-up Audit Report of Outstanding Recommendations Intercompany Receivables

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### **RECOMMENDATION**

This is an informational item for the Board of Directors.

### **BACKGROUND**

Internal Audit (IA) has completed the follow-up evaluation of the outstanding recommendations for intercompany receivables according to the fiscal year (FY) 2014/15 Annual Audit Plan. The IA Department Charter requires that IA perform follow-up evaluations to determine the progress made to implement the recommendations provided in previous audits. The follow-up audit evaluated the outstanding recommendations related to the following reports:

- Chino Desalter Authority (CDA), dated February 24, 2011
- Inland Empire Regional Composting Authority (RCA), dated March 30, 2011
- Chino Basin Watermaster (Watermaster), dated August 30, 2011

In 2011, a total of 14 recommendations were provided in the three intercompany receivable reports. Since the original audit reports were completed, the Finance and Accounting Department (FAD) implemented four recommendations and ten remained outstanding. This follow-up report provides the status of nine recommendations as follows:

- CDA – two recommendations remain outstanding
- RCA – two recommendations remain outstanding
- Watermaster – five recommendations remain outstanding

Of the nine recommendations that were outstanding, Finance and Accounting (FAD) implemented seven and two recommendations are considered no longer applicable and closed.

The attached report provides details of the observations and recommendations. Below is a brief summary of the changes identified.

- FAD documented Standard Operating Procedures (SOP) to document procedures for accounts receivable intercompany processes for ensuring payment of bills and to comply with the Agreement requirements for CDA and RCA.
- FAD implemented procedures to ensure that reconciliations are performed in a timely manner and reviewed by a supervisor/manager for accuracy.
- FAD re-evaluated its budget assumptions and lowered the budgeted interest rate that is utilized to calculate the budgeted interest expense to align with current market trends. The rates applied for budgetary purposes decreased to be more conservative than in prior years and therefore, reducing the need to apply a large credit.

Refer to the attached report for additional details of the findings and recommendations.

### **PRIOR BOARD ACTION**

On September 17, 2014, the Board of Directors approved the Annual Audit Plan for Fiscal Year 2014/15.

On December 18, 2013, the Board of Directors reconfirmed the Internal Audit Department Charter.

### **IMPACT ON BUDGET**


None.





**Inland Empire Utilities Agency**  
A MUNICIPAL WATER DISTRICT

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DATE: August 31, 2015  
TO: Joe Grindstaff  
General Manager  
FROM:   
Teresa V. Velarde  
Manager of Internal Audit

**SUBJECT: Intercompany Receivables Follow-Up Review**

**Audit Authority**

The Internal Audit (IA) Department's Charter and the Annual Audit Plan require that IA follow-up on the status of audit recommendations to determine if corrective actions have been taken. The audit 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 outstanding recommendations related to the following audit reports:

- Chino Desalter Authority (CDA), dated February 24, 2011
- Inland Empire Regional Composting Authority (RCA), dated March 30, 2011
- Chino Basin Watermaster (Watermaster), dated August 30, 2011

**Audit Objective and Scope**

The purpose of the follow-up review was to evaluate the corrective actions implemented for each of the outstanding recommendations. The reports originally issued identified opportunities for improvement and provided recommendations to tighten controls and improve billing and receivable functions.

A total of 14 recommendations were provided in the original audit reports in 2011. Since the original audits were completed, the Finance and Accounting Department (FAD) implemented four recommendations and 10 remained outstanding. This report provides the status of 9 recommendations as follows:

- CDA – 2 recommendations remain outstanding
- RCA - 2 recommendations remain outstanding
- Watermaster – 5 recommendations remain outstanding

**Audit Techniques**

Audit techniques included:

- Discussions with Finance and Accounting staff
- Review of the related agreements
- Review of policies and procedures
- Review of supporting documents and schedules

*Water Smart – Thinking in Terms of Tomorrow*

**Audit Results – Executive Summary**

As a result of this follow-up evaluation, of the 9 outstanding recommendations, FAD implemented seven (7) recommendations and two (2) recommendations are considered no longer applicable and closed. The attached report provides details of the findings and recommendations.

**Acknowledgements**

We would like to extend our appreciation to Finance and Accounting Department staff for their cooperation during this follow-up review.

**Discussions with Management**

We provided the results of this follow-up review to Christina Valencia, Assistant General Manager/Chief Financial Officer, Javier Chagoyen-Lazaro, Manager of FAD, and Mr. Suresh Malkani, Principal Accountant on August 26, 2015, prior to finalizing this report for their review and comments.

**Written Response to Internal Audit**

Nine outstanding recommendations have been cleared. There is one recommendation that is outstanding and will be evaluated separately. No new recommendations were provided in this report. No response is required.

### **Background**

Three separate reviews and audit reports were completed related to Intercompany accounts receivables. The purpose of the original audits was to determine whether IEUA accounts receivable functions are performed timely and effectively and according to the requirements of the agreements and whether each entity (CDA, RCA and Watermaster) paid IEUA for all costs incurred on its behalf. Overall, the audits found that FMD provides effective support in performing the required functions, additionally, IA identified opportunities for improvements and a total of 14 recommendations were provided in the original reports. This follow up review, only reports on nine of the outstanding recommendations.

Internal Audit refers readers to each of the respective Intercompany Receivables audit reports, which were received and filed by the Board of Directors at the time of issuing the original audit reports, these can also be accessed through AIM, or can be requested from the Manager of Internal Audit.

At the time of the original audit reports, the department responsible for the accounts receivable functions was called Fiscal Management Department (FMD). The Department has been renamed Finance and Accounting Department (FAD) and is now combined with the budget staff, previously the Financial Planning Department. The report makes reference to "FMD" and/or "FAD".

### **Chino Desalter Authority (CDA) Follow-up review to the Audit Report dated February 24, 2011**

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IEUA's Finance and Accounting Department (FAD) was responsible for performing all finance and accounting functions on behalf of the CDA. The follow up audit found that of the five recommendations provided in the original audit report, four have been implemented and one is no longer applicable. The report that follows provides details of the follow-up review.

#### **Work Order Errors**

**Recommendation #2 – IEUA FMD work with ESS to resolve the work order issue to ensure that these do not create a discrepancy/reconciling item at the end of each billing cycle, and provide any necessary training.**

#### **Status: No Longer Applicable**

In the original audit report, IA noted there were discrepancies/reconciling items at the end of each billing cycle related to costs recorded through work orders. A work order is a request to perform maintenance work and all the associated costs (labor, parts or materials) utilized in carrying out the service are summarized and charged to the individual work order. The purpose of reviewing discrepancies/reconciling items is to

ensure the items identified are researched and resolved appropriately and billed correctly. Although the original audit noted that the amounts appeared to be low and immaterial, nonetheless, IA recommended these be resolved.

In 2012, IEUA implemented the timekeeping module in the Agency's ERP system. The SAP NetWeaver Business Client Employee Self-Service (SAP ESS) or timekeeping module is the Agency's employee time recordkeeping system and allows for integration with other SAP business modules. Each employee must record their labor hours to a specific "project"; therefore, all employee time is captured under a specific project code.

FAD indicated that after the final payroll of each month and at year-end, FAD staff will review and reconcile all work orders in SAP to ensure any costs associated with a work orders are directed to the correct project and/or cost center if necessary. Any exceptions identified during the month-end processes are resolved prior to closing the month-end ledgers, according to FAD. Once this process is complete, FAD closes the timekeeping module in SAP for the month and no changes are allowed. All labor hours recorded to a Work/Internal Order number are transferred from the SAP ESS timekeeping module and posted to the designated general ledger account in the Agency's SAP system. Finally, labor reports from the Agency's SAP accounting system are utilized to prepare the intercompany receivable billings.

FAD believes that the current process is adequate and ensures labor hours and costs are posted and settled into the appropriate expense account in the Agency's SAP accounting system, eliminating any discrepancies or reconciling items that previously existed at the end of the billing cycle.

IA also discussed the recommendation with the Business Information Services Department (BIS) and they believe that the work order issue identified through the 2011 audit no longer applies because of the timekeeping system now in place. However, BIS was not able test to ensure this.

IA has determined the recommendation is no longer applicable due to the implementation of ESS. IA defers the detailed review labor processes and expenses to a future Payroll Audit. The Payroll Audit would be scheduled through the Annual Audit Plan approved by the Board. The Payroll Audit is included in IA's list of possible future audits.

#### **Standard Operating Procedures**

**Recommendation #5 – FMD should develop an SOP to document procedures for accounts receivable intercompany processes for ensuring payment of bills and to comply with the Agreement requirements.**

**Status: Implemented**

During the 2011 audit, IA found that FAD did not have Standard Operating Procedures (SOPs) documenting the process for ensuring payment of bills and to comply with the Agreement requirements. The purpose of SOPs is to ensure there are documented processes during staff absences, staffing changes, and cross-training. Having written procedures serves as an added control and reference guide to ensure functions are performed consistently and uniformly.

During this follow-up evaluation, IA noted that FAD has documented the process in the SOP titled: SOP on Intercompany billings in SAP. The SOP provides detailed procedures for the preparation of invoices to bill for the reimbursement of Operations & Maintenance costs and Labor expenses paid by IEUA on behalf of the CDA and RCA.

IA reviewed the SOP, which was approved and signed by the Manager of Finance and Accounting Department in August 2015.

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**Inland Empire Regional Composting Authority (IERCA)**  
**Follow-up review to the Audit Report dated March 30, 2011**

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IEUA is responsible for managing IERCF's operations, as well as the finance and accounting functions, and are compensated for services rendered. The follow up audit found that of the three recommendations provided in the original audit report, two have been implemented and one is no longer applicable. The report that follows provides details of the follow-up review.

**Work Order Errors**

**Recommendation #2 – Fiscal Management Department work with Enterprise System Services Department to resolve the root cause of the order issue to ensure that these do not create a discrepancy/reconciling item at the end of each billing cycle for intercompany receivables.**

**Status: No Longer Applicable**

As indicated under Recommendation #2 for CDA, according to FAD and BIS, the implementation of the SAP ESS timekeeping module appears to have resolved the root cause of the discrepancies/reconciling items on work orders, as identified through the original audit. FAD has noted that this issue is no longer a concern.

See more details under CDA Recommendation #2 above for further discussion. IA has determined the recommendation is no longer applicable due to the implementation of ESS. IA defers the detailed review labor processes and expenses to a future Payroll Audit. The Payroll Audit would be scheduled through the Annual Audit Plan approved by the Board. The Payroll Audit is included in IA's list of possible future audits.

**Standard Operating Procedures**

**Recommendation #3 – Fiscal Management Department should update all SOPs to reflect business process changes resulting from the implementation of the Agency’s ERP system, specifically those for process inter-company receivables. FMD should make all SOPs available on the departments share drive and, provide training to staff, where necessary.**

**Status: Implemented**

As noted above, under Recommendation #5 for CDA, FAD has documented the SOP; a final draft was signed by the Manager of Finance and Accounting Department in August 2015. IA reviewed the SOP and it contains the processes recommended.

**Chino Basin Watermaster (Watermaster)**  
**Follow-up review to the Audit Report dated August 30, 2011**

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IEUA has two recurring receivables with Watermaster, one for Operations and Maintenance(O&M) and the other is for Debt Service.

The Chino Basin Recharge Master Plan Agreement outlines the conditions for reimbursement of O&M costs to IEUA. The O&M agreement requires Watermaster to pay IEUA, quarterly, in advance, the estimated amount of the total budget that is expected to be expended during quarter. Therefore, IEUA will receive four quarterly payments during the fiscal year from Watermaster for the reimbursable O&M costs.

For the Debt Service receivable, IEUA and Watermaster have each agreed to pay one half of the debt service on the bonds issued by the Chino Basin Regional Financing Authority in accordance with a May 2002 agreement between Chino Basin Regional Financing Authority and Chino Basin Watermaster called the Recharge Facilities Financing Agreement. The purpose of the payment is to fund the Local Share of the recharge facilities improvements described in the Recharge Master plan. As part of the agreement, Watermaster is required to pay an operating fee that will be sufficient to pay one-half of the debt service. The debt service payments represent the portion of the capital costs not paid for by Proposition 13 grant funding, and to be financed by the Authority through the issuance of bonds. Therefore, IEUA will receive one payment annually from Watermaster with payment to be received by the required due date.

**Quarterly Billing: Operation & Maintenance Expenses**

**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.**

FAD and IA continue to work on the final implementation status of this recommendation. The status of this recommendation will be discussed in a separate report.

**Debt Service: Prior Year's Reconciliations**

**Recommendation #2 – Fiscal Management Department should review the annual debt service reconciliations for FYs 2006, 2007, and 2010 and identify any monies owed to Watermaster, then take steps to resolve any overpayment.**

**Status: Implemented**

In the original audit report, IA found errors in the reconciliation performed for the annual fixed project costs (debt service) for FY 2005/06, 2006/07, and 2009/10, totaling \$85,030. FAD investigated and agreed with IA's findings, which resulted in the issuance of two Credit Memos (Invoice Number: 90008217 and 90008218, dated August 24, 2011) to Watermaster for the overpayments totaling \$85,031. According to FAD, the annual debt service reconciliation is now thoroughly reviewed by a manager before issuing an invoice or credit memo.

**Debt Service: Annual Reconciliation**

**Recommendation #3 – Fiscal Management Department should establish procedures to ensure that reconciliations are performed in a timely manner. The procedures should specify the time frame when the reconciliation should be performed, the person(s) or department responsible for the reconciliation, and the procedure to ensure that the paper reconciliation is thoroughly reviewed by a supervisor/manager for accuracy.**

**Status: Implemented**

In the original audit report dated August 2011, IA noted the annual debt service reconciliation was not performed in a timely manner. Originally, the reconciliations were performed 2 to 7 months after the Agency's CAFR was finalized and approved by the IEUA's Board of Directors. IEUA's CAFR is approved by the Board of Directors in December for the preceding fiscal year with the reconciliation anticipated to be completed in January. Additionally, there were no procedures in place to ensure a specific individual was assigned the responsibility to complete the reconciliation timely and supervisory review and approval of the reconciliation.

For the follow up audit, IA reviewed when FAD performed the annual reconciliation for the debt service and the table below is a summary of prior fiscal years:

**Groundwater Recharge Program (RW Fund)  
Debt Service – Annual Reconciliation**

<b>Fiscal Year</b>	<b>Reconciliation Completed</b>	<b>Number of Months Late</b>
2011/12	April 2013	3 months
2012/13	April 2014	3 months
2013/14	October 2014	Immediately
2014/15	October 2015 <sup>(1)</sup>	To be completed

According to FAD, beginning with FY 2013/14, a reconciliation is performed annually during the **second quarter** following the close of the fiscal year to compare the estimated and actual fixed project costs for the prior fiscal year. In addition, FAD noted a specific person has been assigned the responsibility of performing the annual reconciliation, which is thoroughly reviewed and approved by a manager

Based on IA's review, the FAD has implemented procedures to ensure the annual reconciliation is performed timely and a designated staff member has been tasked with this responsibility. No further action is required and IA considers this recommendation to be implemented.

**Debt Service: Annual Payment**

**Recommendations:**

**#4 – Fiscal Management Department should submit invoices to Watermaster to allow sufficient time to receive payment from Watermaster by July 15<sup>th</sup>, AND**

**#5 – Fiscal Management Department should consider implementing procedures and controls to enforce the Financing Agreement requirement that payment be made by Watermaster to IEUA by the July 15<sup>th</sup> deadline.**

**Status for Recommendations # 4 and # 5: Implemented**

During the prior audit, IA noted the annual payments from Watermaster for the Fixed Project Costs (i.e., debt service) were received after the required due date, July 15<sup>th</sup>. Originally, the annual payments were received 15 to 90 days after the due date and occurred because IEUA does not invoice Watermaster in a sufficient amount of time for payment to be received by July 15<sup>th</sup>.

According to the 2002 Recharge Facilities Financing Agreement, IEUA and Watermaster agreed to each pay one-half (50%) of the debt service for the bonds issued by the Authority. Additionally, Watermaster is required to make the annual debt payment to the Authority **on or before July 15<sup>th</sup>** of each fiscal year, or unless no longer required. IA reviewed when FAD invoiced Watermaster for the debt services costs for the prior years:



**Groundwater Recharge Program (RW Fund)  
 Debt Service – Invoice and Payment Date**

<b>Fiscal Year</b>	<b>Net Amount Invoiced</b>	<b>Invoice Date</b>	<b>Required due date</b>	<b>Date Payment Received</b>	<b>No. of Days Late</b>
2011/12	\$ 556,431	July 28 <sup>th</sup>	July 15 <sup>th</sup>	August 16 <sup>th</sup>	32
2012/13	\$ 504,688	July 22 <sup>nd</sup>	July 15 <sup>th</sup>	July 30 <sup>th</sup>	15
2013/14	\$ 406,126 <sup>(1)</sup>	<b>July 2<sup>nd</sup></b>	July 15 <sup>th</sup>	<b>July 16<sup>th</sup></b>	<b>1</b>
2014/15	\$ 505,740	<b>July 2<sup>nd</sup></b>	July 15 <sup>th</sup>	<b>July 14<sup>th</sup></b>	<b>(1)</b>
2015/16	\$ 460,201	<b>July 1<sup>st</sup></b>	July 15 <sup>th</sup>	<b>July 13<sup>th</sup></b>	<b>(2)</b>

(1) = Net amount invoiced includes an additional credit due for the FY 2011/12 Debt service Reconciliation (\$423,075.50 - \$16,949.00).

IA observed that FAD is invoicing Watermaster on the first or second day of the fiscal year as seen for FY 2014 through 2016, which is an improvement from prior fiscal years. This change has allowed for payment to be received within a day of the due date, July 15<sup>th</sup>. IA noted the suggested processes and recommendations from the original audit have been implemented by FAD to ensure Watermaster is invoiced in enough time to allow for payment to be received by the required date (July 15<sup>th</sup>) and compliance with the agreement provisions.

IA considers this recommendation to be implemented.

**Bonds – Interest Expense**

**Recommendation #6 – Financial Planning should re-evaluate its budgeting methods for interest expense on the variable bonds so that budgeted amounts are more reflective of anticipated expense.**

**Status: Implemented**

During the 2011 audit, IA noted the budgeted portion of the debt service expense that represented interest expense significantly exceeded the actual interest expense. The interest expense is related to the 2008B Variable Rate Demand Revenue Refunding bonds.

As part of the 2015 follow-up evaluation, IA compared the budgeted interest rate to actual interest rate for the 2008 bonds and the following table below shows a summary for previous fiscal years:

**Chino Basin Watermaster  
 Groundwater Recharge Program (RW Fund)  
 Debt Service - Interest 2008B Bonds (SAP Account # 555010)**

<b>Results</b>	<b>Fiscal Year</b>	<b>Credit issued to Watermaster</b>	<b>Budgeted Interest Rate</b>	<b>Actual/Average Interest Rate</b>
Original Audit	2009/10	(\$270,408)	4%	0.28%
	2010/11	(\$296,265)	4%	0.23%
Follow-up Audit	2011/12 <sup>(1)</sup>	(\$188,937)	4%	0.14%
	2012/13	(\$94,882)	3%	0.14%
	2013/14	(\$89,762)	1%	0.06%
	2014/15	Unavailable	2%	0.05%
	2015/16	Non-Applicable	1%	-
	2016/17	Non-Applicable	2%	-

(1) = Additional credit of \$16,949 was applied based on the FY 2011/12 Debt Service Reconciliation. Credit Memo was not issued Watermaster, instead the additional adjustment was applied to FY 2013/14 Annual Debt Service Payment.

The original audit suggested that interest amount billed to Watermaster be more reflective of the anticipated expense. At the time, the rate applied was considered a “conservative approach,” and budgeted at a 4% interest rate as seen in the table above for FY 2010 through FY 2012.

In more recent years, it appears, FAD has re-evaluated its budget assumptions and lowered the budgeted interest rate that is utilized to calculate the budgeted interest expense. As the analysis above shows, the rates as of 2013/14 decreased to a 1% or 2%, being more conservative than in prior years. The credit issued to Watermaster has therefore, significantly reduced. This recommendation is considered implemented.

**Attachment 2 – Intercompany Receivables Recommendations – CDA, February 24, 2011**

Rec #	Recommendation	Implemented	In Progress	No Longer Applicable
1	IEUA FMD staff ensure that supporting documentation is reviewed, verified and correctly reflect SAP report information and approved/authorized charges before processing invoices. (Implemented prior to the 2015 follow-up review)	X		
2	IEUA FMD work with ESS to resolve the work order issue to ensure that these do not create a discrepancy/reconciling item at the end of each billing cycle, and provide any necessary training.			X
3	IEUA Management work with CDA and the necessary parties to amend/update the current Agreement to document the labor factor and/or actual costs of labor that should be passed on to the CDA for reimbursement. Documenting the agreed upon labor factor will confirm the actual rate and prevent any uncertainty in the application of the factor and prevent potential differences among the parties to the agreement. (Implemented prior to the 2015 follow-up review)	X		
4	IEUA management should work with the CDA to reevaluate the labor factor and determine if 1.7 is the most appropriate factor to apply. The agreed-upon labor factor should be properly documented in the agreement (as recommended under Recommendation 3). (Implemented prior to the 2015 follow-up review)	X		
5	FMD should develop an SOP to document procedures for accounts receivable intercompany processes for ensuring payment of bills and to comply with the Agreement requirements.	X		
<b>Totals</b>		<b>4</b>	<b>0</b>	<b>1</b>

**Attachment 3 – Intercompany Receivables Recommendations – RCA, March 30, 2011**

Rec #	Recommendation	Implemented	In Progress	No Longer Applicable
1	The Fiscal Management Department should implement controls that prevent, or at minimum, limit staff's ability to "back-post" transactions; if possible, controls should be configured into IEUA's accounting system. (Implemented prior to the 2015 follow-up review)	X		
2	Fiscal Management Department work with the Enterprise Systems Services Department to resolve the root cause of the work order issue to ensure that these do not create a discrepancy/reconciling item at the end of each billing cycle for intercompany receivables.			X
3	Fiscal Management Department should update all SOPs to reflect business process changes resulting from the implementation of the Agency's ERP system, specifically those for processing inter-company receivables. FMD should make all SOPs available on the departments share drive and, provide training to staff, where necessary.	X		
<b>Totals</b>		<b>2</b>	<b>0</b>	<b>1</b>

**Attachment 4 – Intercompany Receivables Recommendations – Watermaster, August 30, 2011**

Rec #	Recommendation	Implemented	In Progress	No Longer Applicable
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.		X	
2	Fiscal Management Department should review the annual debt service reconciliations for FYs 2006, 2007, and 2010 and identify any monies owed to Watermaster, then take steps to resolve any overpayment.	X		
3	Fiscal Management Department should establish procedures to ensure that reconciliations are performed in a timely manner. The procedures should specify the time frame when the reconciliation should be performed, the person(s) or department responsible for the reconciliation, and the procedure to ensure that the paper reconciliation is thoroughly reviewed by a supervisor/manager for accuracy.	X		
4	Fiscal Management Department should submit invoices to Watermaster to allow sufficient time to receive payment from Watermaster by July 15th.	X		
5	Fiscal Management Department should consider implementing procedures and controls to enforce the Financing Agreement requirement that payment be made by Watermaster to IEUA by the July 15th deadline.	X		
6	Financial Planning should re-evaluate its budgeting methods for interest expense on the variable bonds so that budgeted amounts are more reflective of anticipated expense.	X		
<b>Totals</b>		<b>5</b>	<b>1</b>	<b>0</b>


**INFORMATION  
ITEM  
2C**

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Date: September 16, 2015

To: The Honorable Board of Directors

Through: Audit Committee (9/9/15)

From:   
Teresa V. Velarde  
Manager of Internal Audit

Subject: External Financial and Single Audit Services Request for Proposal Process  
and Audit Committee Financial Advisor Contract Extension

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### **RECOMMENDATION**

This is an information item for the Board of Directors.

### **BACKGROUND**

This is to provide the Board of Directors with a status of the External Financial Audit Services contract and the Audit Committee Financial Advisor's contract.

#### **External Financial Audit Services**

State law and the Agency's Ordinance No. 77 require an annual audit be performed by an independent auditor to ensure the accountability of the annual financial statements to assess the efficiency and effectiveness of the internal controls and to determine the compliance with governmental laws and regulations. The audit is to be performed in accordance with:

- Generally Accepted Auditing Standards (GAAS)
- The General Accounting Office's (GAO) Government Auditing Standards (2007 edition, with all subsequent amendments) issued by the Comptroller General of the United States
- The provisions of the federal Single Audit Act of 1984 (as amended in 1996) and U.S Office of Management and Budget (OMB) Circular A-133, Audits of State and Local Governments and Non-Profit Organizations, including additional requirements under the American Recovery Reinvestment Act (ARRA).

In 2011, the Agency entered into a contract with White Nelson Diehl Evans, LLP (WNDE) certified public accountants (formerly Diehl Evans, LLP). The contract was for three years with two single year options to extend, for a total of five years. The current contract expires in December of 2015 with the completion of the FY 2014/15 Financial and Single Audits.

Sound business practices provide that it is in the best interest of the Agency to request proposals from capable certified public accounting firms for the External Financial Audit. The Internal Audit

Department will work closely with the Contracts and Procurement Department as well as the Finance and Accounting Department to ensure an RFP is issued to qualified firms. IA will coordinate the RFP process, including ensuring there is a knowledgeable evaluation panel. The new audit firm should be established by June 2016 to ensure preliminary audit work begins shortly after that. A recommendation to the Audit Committee and then the Board of Directors is planned by March 2016. The timetable for this process is expected to be:

<u>Process</u>	<u>Timeline</u>
IA prepares RFP documents	November 2015
Final RFP and solicitation for bids	December 2015
Review of bids and interview panel	February 2016
Recommendation of selected firm	March 2016
Begin preliminary audit work	June 2016

#### Audit Committee Financial Advisor

The Audit Committee Charter, states that: “The Audit Committee shall also have access to at least one financial expert, an outside party, with no voting rights, who will provide advisory and consulting duties and shall be compensated as agreed upon, in writing with the audit committee, the Board, management and its designees.” Additionally, the Audit Committee Charter requires the financial expert to possess expertise and experience in understanding generally accepted accounting principles and financial statements; auditing comparable entities; internal controls; and an understanding of audit committee functions.

Since 2008, the Audit Committee has relied on the advisory services of Travis C. Hickey, CPA consultant with Rogers, Anderson, Malody & Scott. Mr. Hickey has provided accounting and auditing services to governmental agencies since 1997, including experience with water/wastewater activities. Mr. Hickey attends the Agency's Audit Committee Meetings and provides consulting and advisory services to both the Audit Committee and the Internal Audit Department to ensure the responsibilities of the Audit Committee and Internal Audit Department, as outlined in the Board approved Charters, are fulfilled. Mr. Hickey is a Certified Public Accountant in the State of California and in good standing. He is a member of the American Institute of Certified Public Accountants and California Society of Municipal Financial Officers.

Over the past seven years, Mr. Hickey has established himself as a valuable resource to the Audit Committee and the Internal Audit Department by providing professional auditing advice and information. Mr. Hickey has gained extensive knowledge of the Agency's operations, has established professional working relationships with the Audit Committee, and the Agency has been satisfied with his services.

The current contract with Mr. Travis Hickey expires in December of 2015 and has two single year options to extend. Staff recommends the contract for the single year option is extended through December 2016. This extension of Mr. Hickey's services will extend Audit Committee Advisory Services for one year through Calendar Year 2016.

The External Financial Audit Services Request for Proposal (RFP) process and the extension of the Audit Committee Financial Advisor Services is consistent with the Agency's Business Goals of Fiscal Responsibility, Workplace Environment and Business Practices by following recommended practices for the procurement of such services to provide independent evaluations and oversight of Agency financial statements and the operational effectiveness of the Audit Committee.

#### **PRIOR BOARD ACTION**

On June 10, 2014, the Agency approved Amendment Number 46000000883-005 with White Nelson Diehl Evans LLP to extend contract services for an additional year through June 30, 2015.

On March 24, 2011, the Agency approved Contract Number 46000000886 with Rogers, Anderson, Malody & Scott, LLP, for advisory audit services. The contract superseded Contract Number 46000000093 to establish the necessary name change in firms.

#### **IMPACT ON BUDGET**

There is no significant impact on the Agency's Fiscal Year 2015/2016 Budget as a result of these items, since the external financial audit and audit committee advisory services are already budgeted in the Administrative Services (GG) Fund as part of the Agency's two-year budget.

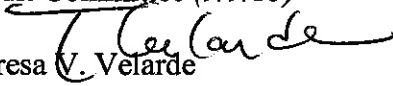


**INFORMATION  
ITEM  
2D**

Date: September 16, 2015

To: The Honorable Board of Directors

Through: Audit Committee (9/9/15)

From:   
Teresa V. Velarde  
Manager of Internal Audit

Subject: Internal Audit (IA) Department Status Report for September 2015

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### **RECOMMENDATION**

This is an information item for the Board of Directors.

### **BACKGROUND**

The Audit Committee Charter requires that a written status report be prepared and submitted each quarter. The IA Department Status Report includes a summary of significant internal and external audit activities for the reporting period. Attached is the Status Report for September 2015.

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 of Agency financial and operational activities and suggesting recommendations for improvements.

### **PRIOR BOARD ACTION**

On September 17, 2014 the Board of Directors approved the Annual Audit Plan for Fiscal Year 2014/15.

On December 18, 2013, the Board of Directors reconfirmed the approved Audit Committee Charter.

### **IMPACT ON BUDGET**

None.



## Internal Audit Department Status Report for September 2015

<u>City of Chino Hills</u>	COMPLETED	June 2015
<u>Cucamonga Valley Water District</u>	COMPLETED	March 2015
<u>City of Chino</u>	COMPLETED	December 2014
<u>City of Fontana</u>	COMPLETED	December 2014
<u>City of Montclair</u>	COMPLETED	September 2014
<u>City of Upland</u>	COMPLETED	September 2014

Refer to the final reports under separate cover for details on all observations and recommendations

### IA also submitted the following audit reports related to the Regional Contract Review:

- The report titled "Regional Contract Review – Review of the Ten Year Forecast" was completed in June 2014. The scope of the Ten Year Capacity Demand Forecast (TYCDF) review was to evaluate the TYCDF prepared by each of the seven Contracting Agencies and how that information is subsequently compiled and utilized by IEUA to prepare the IEUA Ten Year Capital Improvement Plan (TYCIP). The review considered the requirements of the Regional Contract and how those requirements are met through the TYCDFs prepared by the Contracting Agencies and the TYCIP prepared by IEUA.
- The report titled "Regional Contract Review – Survey of Comparable Agencies" was completed in June 2014. The report compared IEUA's Regional Contract and program with four similar agencies/programs in California. The review evaluated the structure used to bill and collect Connection Fees and sewer service fees from residential, commercial, industrial and public service users. The review considered whether greater efficiencies could be gained from adopting different applications and methodologies in administering the contract and collecting fees as applied at other agencies.
- The "Survey of Comparative Information" was completed in September 2014. This report provided a comprehensive side-by-side comparison of the preliminary responses received from each Contracting Agency about how the Regional Contract provisions are applied.
- The first "Internal Audit Recommendations" report was completed in September 2014. This report provided a comprehensive list of recommendations and the related relevant Contracting Agency. This report was limited to the two Contracting Agencies that had been completed: Upland and Montclair.
- A new "Internal Audit Recommendations" report has now been completed. This report has been updated to include all seven Contracting Agencies. This report is complete and is presented under separate cover for this agenda. There are three sections of recommendations:
  - Connection Fees Recommendations
  - Public Service Facilities Recommendations
  - Monthly Sewerage Billing Recommendations

## Internal Audit Department Status Report for September 2015

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- Audit:**     **Follow up of Outstanding Recommendations: Intercompany Receivables**
- **Chino Desalter Authority(CDA),**
  - **Inland Empire Regional Composting Authority (RCA), and**
  - **Chino Basin Watermaster (Watermaster)**

**Scope:**

Follow-up evaluation of the 10 outstanding recommendations provided in the Intercompany Receivables audit reports dated February 24, 2011, March 30, 2011 and August 30, 2011.

**Status:**     **COMPLETED**

Of the 10 outstanding recommendations, six recommendations have been implemented, two recommendations are consider non-resolvable and two recommendations are in progress. IA has followed up on all the original recommendations issued in the Intercompany Receivables reports and the final status of the recommendation has been determined. No additional findings or recommendations were noted.

See the report under the separate item in the Audit Committee Agenda

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**Project:**    **Annual Audit Plan**

**Scope:**

The IAD and the Audit Committee Charters require that annually, IA submit a flexible plan of proposed audit projects for the following fiscal year.

**Status:**     **IN PROGRESS**

The Manager of IA has inquired of all Agency key individuals of any recommendations, referrals, or key areas for audit, such as a process, contract, activity or business unit. Inquiries have been made of the External Auditors, the Audit Committee Advisor, Executive Management, the Board, as well as consider audit trends and best practices. If information is provided, a risk assessment will be completed prior to finalizing the Annual Audit Plan for Board approval.

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**Audit:**     **Follow up of Outstanding Recommendations: Information Technology Equipment**

**Scope:**

IA is in the progress of performing a follow-up evaluation to determine the status of the 18 outstanding recommendations provided in the Information Technology (IT) Equipment audit reports dated August 21, 2012 and November 14, 2012.

**Status:**     **IN PROGRESS**

There are 18 recommendations that require follow-up evaluation. IA is currently in the planning phase of this project. IA met with Integrated Systems Services to discuss the outstanding recommendations with the assigned representatives. All 18 recommendations require audit follow-up procedures be performed to verify if corrective actions have been implemented.

IA will report on the status of each outstanding recommendation and the anticipated date for completion is December 2015.

## Internal Audit Department Status Report for September 2015

### On-going Projects

**Project: Review of Internal Audit Department SOP's**

**Scope:** As required by the Internal Audit Department Charter and the IIA Standards, the Manager of IA is responsible for documenting procedures and review/update procedures periodically to ensure these are aligned with current department practices/procedures, leading practices or new requirements.

**Status: IN PROGRESS and ON-GOING**

IA has formally documented seven SOPs. SOPs serve various objectives: provide consistency in the audit methods applied, are a useful training/reference tool, establish ground rules of professional conduct and responsibilities, and provide continuity during staff changes.

**Project: Management Requests**

**Scope:**

Assist Agency Management with requests for analysis, evaluations and verification of information, assist with the interpretation of policies and procedures, or providing 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 IAD determines it has the necessary staff, skills and resources to provide 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/assistance and the Manager of IA and when deemed appropriate by Executive Management.

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

- Requested to serve on the Agency's Steering Committee for Managing Records and Information. Additionally, IA assisted the Records Management group during the 18 Enterprise Content Management (ECM) sessions where various Agency steps and stages of selected activities and processes were discussed to determine the types of documents and the course and/or method of submitting/issuing/saving/processing the needed documents.
- Requested to review and provided recommendations to the Agency's Fiscal Ordinance #102 related to internal controls, preferred business practice and sound controls.
- Assisted with a recent request for information from an outside audit firm.
- Provided a brief workshop to Executive Management on options for moving forward with the Regional Contract recommendations.
- Provided a presentation to the Regional Technical Committee related to the Regional Contract Review Findings.

### Planned/Future/Additional Projects

**Audit: Master and Rotating Contracts Audit**

**Scope:** To evaluate the Agency's Master and Rotating Contracts to ensure these follow the required Agency policies and procedures and ensure controls exist that enforce proper contracting and procurement for transactions are in place.

**Status:** Projected start date: September 2015

IA will coordinate an audit kick-off meeting in mid-September with responsible managers/supervisors. IA will perform preliminary surveys, planning, interviewing and inquiries of Agency personal in relation to the

## Internal Audit Department Status Report for September 2015

areas of the audit. It is anticipated fieldwork will begin thereafter. A status report of the progress of the Master and Rotating Contracts Audit will be provided at the December Audit Committee Meeting.

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**Project: Request for Proposal for External Financial Audit Services**

**Scope:**

To secure a professional firm to perform the annual financial audit and single audit of IEUA to ensure compliance with all regulatory requirements and the Agency's Financial Ordinance.

**Status:**

The current contract for External Financial Audit Services is set to expire on December 31, 2015. Per preferred practices and good internal controls, it is in the best interest of the Agency to request proposals from capable certified public accounting firms for the external financial audit services contract. The current financial auditors White Nelson Diehl Evans have been the Agency's external auditors since 2011. The Internal Audit Department will work closely with the Contracts and Procurement Department to ensure the RFP is issued to qualified firms and coordinate the RFP process ensuring there is a knowledgeable evaluation panel. The new audit firm should be established by June 2015 to ensure preliminary audit work begins shortly after that.

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### ***Internal Audit Department***

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**Internal Audit Department Staffing:**

The Internal Audit Department is staffed as follows:

- 1 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*, 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 review of industry periodicals. Three IA members are working hard in preparation for the third exam of the 3-part Certified Internal Auditor (CIA) certification examination. 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. One Senior Auditor is a Certified Public Accountant (CPA). One Senior Auditor is a Certified Government Audit Professional (CGAP). One Senior Auditor recently attended training alongside the Engineering and Construction Management group related to Primavera, the project management tool, this training provides some foundation knowledge will be good information for future audits related to this field. Additional professional development education will be scheduled in October 2015.

**Future Audit Committee Meetings:**

- Wednesday, December 9, 2015 – Regularly Scheduled Audit Committee Meeting