



August 19, 2014

REPORT #: 2015-01

Roubik Golanian, Director
Public Works Department

Dear Roubik,

Enclosed is the final audit report for the Los Angeles-Glendale Water Reclamation Plant operational audit. Internal Audit would like to thank you and your staff for the support and assistance provided to us during the audit.

Should you have any questions, please feel free to contact Natalie Minami-Valdivia or myself.

Thank you,

A handwritten signature in cursive script that reads "Michele Flynn".

Michele Flynn,

City Auditor

Enclosure

cc: Yasmin Beers, Assistant City Manager
Robert Elliot, Director of Finance
Scott Ochoa, City Manager
Maurice Oillataguerre, Environmental Program Administrator
City Council
Audit Committee

Los Angeles-Glendale Water Reclamation Plant Operational Audit

August 19, 2014

Background

In accordance with Internal Audit's fiscal year 2013-2014 audit plan and at the request of the City of Glendale (Glendale) Public Works Department (PW), Internal Audit performed an audit of the expenses charged to Glendale through the Los Angeles-Glendale Water Reclamation Plant (LAGWRP) agreement.

The water reclamation plant was constructed in the 1970's through a joint powers agreement between the City of Los Angeles (Los Angeles) and Glendale and began operations in 1976. The plant is located at 4600 Colorado Boulevard in Los Angeles and serves the Eastern San Fernando Valley.

LAGWRP currently has the capacity to process 20-million gallons per day (mgd) of sewage flow. Los Angeles and Glendale each have an allocated average flow of 10 mgd (50% of the plant's capacity) with approximately 20 mgd of wastewater processed daily.

The LAGWRP joint agreement provides that Los Angeles and Glendale share the water reclamation plant operations and maintenance costs (O&M). Annually, the two cities meet between October and December to discuss the O & M budget for the current year with Glendale's portion of actual costs calculated based on an agreed upon formula.

Per the contract terms, the O&M costs are to be invoiced by February 1st of each year. The invoice will include a true-up of the actual O&M costs incurred to the estimated O&M costs for the current fiscal year. Per the contract terms, Glendale pays Los Angeles estimated O&M costs for the

current fiscal year equal to the prior fiscal year's actual costs. Estimated O&M costs for the current year are due by March 1st of each year and the final invoice for the prior fiscal year is due 30 days after the receipt of the invoice.

Currently, the contract terms are silent regarding the invoicing terms for capital costs. However, the contract does specify that capital costs are mutually agreed upon and shared equally by each party. Los Angeles and Glendale meet annually to discuss the planned capital projects for the upcoming year. The Director of Public Works or his designee has the authority to approve the listing of planned capital projects.

For fiscal year 2011-12, Glendale was invoiced approximated \$1.9 million in LAGWRP related costs (\$1.6 million in O&M costs and \$273k in capital costs). As of July 10, 2014, the FY 2012-13 O&M and/or capital invoices had not yet been received.

In order to assist in Glendale's project management of LAGWRP, Glendale has also procured a professional services agreement with Kennedy/Jenks Consultants. Services available through the agreement include:

- Assisting in reviewing wastewater bills submitted by Los Angeles
- Assisting in negotiations with Los Angeles regarding the maintenance and operations of the LAGWRP
- Providing continuing miscellaneous engineering, technical and financial support services to evaluate,

review and research Glendale’s existing and future wastewater treatment issues and alternatives and other issues related to Glendale’s local wastewater collection and treatment systems

- Conducting winter water usage and other financial studies as requested by Glendale.

Although this professional services agreement exists, PW makes a conscious effort to minimize its expenses by minimizing its use of the contractor.

This particular audit primarily focused on the O&M costs, overhead calculations, and capital expenditures.

Objectives

The objectives of the audit were to perform the following:

- Obtain an understanding of key contract management functions within PW pertaining to the LAGWRP operations.
- Determine the accuracy and completeness of the O&M and capital expenses included within the LAGWRP invoices submitted by Los Angeles to Glendale.

Scope and Procedures

The scope of this audit included Los Angeles’ invoicing processes for O&M and capital invoices, Glendale’s LAGWRP contract administration and invoice review and

payment process. The detailed invoice testwork included the last five O&M invoices (July 1, 2007-June 30, 2012) and the last five capital expenditure invoices (July 1, 2009-June 30, 2012) paid as of our testwork date.

In order to accomplish the audit objectives noted above, Internal Audit performed the following:

- Obtained and reviewed the Joint Powers Authority agreement between Los Angeles and Glendale.
- Performed a walk-through of the LAGWRP.
- Conducted interviews and performed detailed testwork on selected maintenance and operations and capital invoices.

Summary of Results

As a result of the audit procedures performed, eight improvement opportunities were identified related to general and administrative, O&M invoices, and capital expense invoices. The recommendations included, but were not limited to future contract language additions related to an audit clause and capital expense invoice payment terms, ensuring regular O&M and capital expense planning and update meetings, and obtaining and reviewing O&M and capital expense supporting documentation.

Item	Observation/Risk	Recommendation	Management Response
General & Administrative			
1.	<p>Status update meetings are not consistently scheduled to provide Glendale with an update on LAGWRP operations, maintenance, & capital expenditures.</p> <p style="text-align: center;">* * *</p> <p>Lack of a consistently scheduled update meeting increases the risk that Glendale is not informed of LAGWRP operations, maintenance, and capital expenditures in a timely manner.</p>	<p>It is recommended that PW management work with Los Angeles to ensure that update meetings are scheduled on a regular basis.</p>	<p>Management agrees with the recommendation and will work with Los Angeles to ensure that the annual maintenance and operations meetings and annual capital projects meetings are conducted in a consistent and timely manner. The anticipated completion date is June 30, 2015.</p>
2.	<p>The LAGWRP agreement does not contain a 'right to audit' clause.</p> <p style="text-align: center;">* * *</p> <p>The lack of a 'right to audit' clause within the agreement could potentially result in Glendale's inability to efficiently review/audit annual O&M and/or capital invoice supporting documentation.</p>	<p>It is recommended that the PW management include the 'right to audit' clause within the next contract amendment.</p>	<p>Management agrees with the recommendation and will consider the 'right to audit' clause within the next contract amendment negotiations.</p>

Item	Observation/Risk	Recommendation	Management Response
O&M Invoices			
3.	<p>Based upon detailed testwork performed on the five annual O&M invoices received from the City of Los Angeles, we noted the following:</p> <p>-5 (100%) were not date-stamped upon receipt.</p> <p>-5 (100%) were not provided by Los Angeles to Glendale by February 1st in accordance with the contract terms.</p> <p>-3 (60%) were not paid within 30 days of receipt in accordance with the contract terms.</p>	<p>Internal Audit recommends the following:</p> <p>-Contract be amended to make the O&M preliminary invoice for the next fiscal year due 30 days after receipt which is consistent with the previous year's final invoice payment period.</p> <p>-All LAGWRP invoices received be date-stamped upon receipt and paid within 30 days of receipt in accordance with the contract terms.</p>	<p>Management agrees with the recommendation and will work with Los Angeles to amend the contract's O&M payment terms when the contract is next amended, immediately begin date stamping all invoices upon receipt, and ensure invoice payments are processed within 30 days of receipt or document the issues and discussions with Los Angeles related to any delayed payments.</p>
* * *			
<p>Improper tracking of invoice receipt dates, and delinquent payments increases Glendale's risk of non-compliance with contract payment terms and decreases Glendale personnel's accountability for timely invoice processing and increases the risk that Glendale may not be able to provide proper evidence of the actual date that the invoice was received.</p>			

Item	Observation/Risk	Recommendation	Management Response
4.	<p>Based upon review of an invoice supporting schedule provided by Los Angeles, we noted that \$17,125 was deducted from the LAGWRP non-labor charges in error resulting in an understatement of approximately \$6,000 in Glendale’s portion of the fiscal year 2011-12 O&M expenses.</p> <p style="text-align: center;">* * *</p> <p>Lack of a review process for the O&M expense calculation increases the risk of errors in the O&M invoice submitted by Los Angeles to Glendale and/or inaccurate payments.</p>	<p>It is recommended that the PW management work with Los Angeles to obtain an understanding of the invoice calculation, establish a review process including the supporting schedules, and recalculate the revised fiscal year 2011-12 O&M expenses to determine if there are any amounts due to/from Glendale.</p>	<p>Management agrees with the recommendation and will work with the City of Los Angeles to obtain an understanding of the invoice calculation, establish a review process, and revise the fiscal year 2011-12 O&M invoice as necessary.</p> <p>The anticipated completion date is September 30, 2015.</p>

Item	Observation/Risk	Recommendation	Management Response
5.	<p>Based upon ten O&M expenses included within the Los Angeles' annual invoice to Glendale selected for detailed testwork, we noted the following:</p> <ul style="list-style-type: none"> - 4 of 10 (40%) expenses had discrepancies between the vendor name listed in the related detailed expense listing as compared to the purchase order, invoice, and/or remittance advice. - 1 of 10 (10%) expenses agreed to the invoiced amount, but exceeded the amount paid by Los Angeles per the remittance advice in which a discount had been applied. This discount was not passed onto Glendale. <p style="text-align: center;">* * *</p> <p>Failure to obtain and review O&M related expenses increases the risk that expenses billed are inaccurate.</p>	<p>It is recommended that Glendale work with Los Angeles to obtain a listing of expenses incurred with the appropriate supporting documentation attached (i.e. copy of check/remittance advice and Los Angeles approved invoice) on a periodic basis.</p>	<p>Management agrees with the recommendation and will work with Los Angeles to obtain a listing of O&M related expenses and the supporting invoice and payment documentation to be reviewed for reasonableness on a periodic basis to be agreed upon by both parties. The anticipated completion date is September 30, 2015.</p>

Item	Observation/Risk	Recommendation	Management Response
6.	<p>Based upon detailed testwork performed on sample of Los Angeles O&M related payroll, we noted the following:</p> <p>-12 of 46 (26%) time entries were entered by someone other than the employee and payroll source documentation were not consistently available for our review.</p> <p>-10 of 46 (22%) time entries were not reviewed by an individual independent of the input function.</p> <p>-Payroll for employees performing work at a non-LAGWRP site and non-LAGWRP work orders were included within the LAGWRP payroll billing.</p> <p>-Payroll for employees scheduled to work at the LAGWRP facility whose payroll defaults to a non-LAGWRP facility were excluded from the LAGWRP payroll billing. * * *</p> <p>Lack of a procedure to review payroll documentation increases the risk of inappropriate invoicing and payment.</p>	<p>It is recommended that Glendale work with Los Angeles to periodically obtain and review a LAGWRP organization chart and LAGWRP labor expenses on a periodic basis (i.e. quarterly) for reasonableness. Additionally, it is recommended that Glendale work with Los Angeles to resolve the payroll related billing errors.</p>	<p>Management agrees with the recommendation and will request that all LAGWRP related payroll expenses and supporting work schedules be provided to Glendale on a quarterly basis, or some other agreed upon interval, for review. Additionally, Glendale will work with Los Angeles to review and resolve the payroll billing errors. The anticipated completion date is September 30, 2015.</p>

Item	Observation/Risk	Recommendation	Management Response
Capital Expense Invoices			
7.	<p>Based upon a review and inquiry of five capital invoices submitted to Glendale by Los Angeles and selected for detailed testwork, we noted the following:</p> <ul style="list-style-type: none"> -5 (100%) were not date-stamped by PW upon receipt. -Copies of capital expense related documentation (vendor invoices) are not provided to Glendale for review. -The contract does not contain language regarding the capital expense payment terms. <p style="text-align: center;">* * *</p> <p>The exclusion of clear payment terms within the contract and/or the submission of proper supporting expense documentation increases the risk of inaccurate and/or untimely payments.</p>	<p>It is recommended that PW perform the following:</p> <ul style="list-style-type: none"> -date-stamp all invoices upon receipt. -work with Los Angeles to obtain a monthly capital expenditures report with the appropriate supporting documentation for review purposes. -include capital cost payment terms and required supporting documentation within the next contract amendment. 	<p>Management agrees with the recommendation and will perform the following:</p> <ul style="list-style-type: none"> -date-stamp all invoices upon receipt. -request and obtain a monthly capital expenditures report and supporting documentation. -include capital expenditure invoicing and payment terms within the next contract amendment. <p>The anticipated completion date is June 30, 2015.</p>

Item	Observation/Risk	Recommendation	Management Response
8.	<p>Based upon best practices, a review of the capital invoices, annual capital meeting agendas/meeting information provided, and discussions with Glendale staff, we noted the following:</p> <ul style="list-style-type: none"> -Los Angeles does not provide a complete annual budget for capital expenditures. Currently, capital budgets are only provided for new capital project proposals. -Los Angeles does not provide Glendale with a budget to actual analysis for the approved and/or invoiced capital projects. -Los Angeles does not notify Glendale of emergency capital expenses. <p style="text-align: center;">* * *</p> <p>Failure to obtain and review the annual capital budget, capital expense documentation, budget to actual expenditures and/or percentage of project completion increases the risk that Glendale may not appropriately budget for the upcoming year's expenses, commit to a project without a full understanding of the expected costs, and/or not be made aware of increased project cost projections and/or delayed completion dates.</p>	<p>It is recommended that PW management coordinate with Los Angeles' Bureau of Sanitation to periodically obtain the full annual capital project budget by an agreed upon date to enable the estimate to be included within Glendale's budget process, periodic capital project status updates, and notification of emergency capital expenses. The periodic update should include the current year-to-date budget to actuals and explanations for any variances in excess of a pre-determined percentage (i.e. 10%).</p>	<p>Management agrees with the recommendation and will work with Los Angeles' Bureau of Sanitation to obtain the full annual capital project budget by February of each year, obtain a periodic capital project status update, including year-to-date budget to actuals and explanations for any variances on an annual basis, and notification of emergency capital expenses. The anticipated completion date is September 30, 2015.</p>