

OFFICE OF AUDITS & ADVISORY SERVICES



COUNTY OF SAN DIEGO SANITATION DISTRICT AUDIT

FINAL REPORT

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County of San Diego

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COUNTY COMMUNICATIONS OFFICE
COUNTY COUNSEL
COUNTY TECHNOLOGY OFFICE
GRAND JURY
HUMAN RESOURCES
RETIREMENT ASSOCIATION
TREASURER-TAX COLLECTOR

January 15, 2014

TO: Richard Crompton, Director
Department of Public Works

FROM: Juan R. Perez
Chief of Audits

FINAL REPORT: COUNTY OF SAN DIEGO SANITATION DISTRICT AUDIT

Enclosed is our report on the County of San Diego Sanitation District Audit. We have reviewed your response to our recommendations and have attached them to the audit report.

The actions taken and/or planned, in general, are responsive to the recommendations in the report. As required under Board of Supervisors Policy B-44, we respectfully request that you provide quarterly status reports on the implementation progress of the recommendations. The Office of Audits & Advisory Services will contact you or your designee near the end of each quarter to request your response.

Also attached is an example of the quarterly report that is required until all actions have been implemented. To obtain an electronic copy of this template, please contact Tatiana Foster at (858) 495-5667.

If you have any questions, please contact me at (858) 495-5661.

JUAN R. PEREZ
Chief of Audits

AUD:TF:aps

Enclosure

c: Sarah E. Aghassi, Deputy Chief Administrative Officer, Land Use and Environment Group
Tracy M. Sandoval, Deputy Chief Administrative Officer/Auditor and Controller
Lisa Keller-Chiodo, Group Finance Director, Land Use and Environment Group

INTRODUCTION

Audit Objective The Office of Audits & Advisory Services (OAAS) completed an audit of the County of San Diego Sanitation District. The objective of the audit was to identify and assess internal controls for the proper use and segregation of funds.

Background Prior to FY 2011-12, the Department of Public Works (DPW) was responsible for managing five sanitation districts including Alpine, Lakeside, Spring Valley, Julian, and Pine Valley; and four sewer maintenance districts including Winter Gardens, East Otay Mesa, Harmony Grove, and Campo. All districts were established as separate entities to construct, operate, and maintain reliable and sustainable sanitary sewer systems for unincorporated areas of San Diego County.

Each district was required to maintain separate operating and capital reserve funds. Operating reserve funds were used to pay for services, operational repairs, maintenance, and emergency repairs; while capital reserve funds were used to pay for capital improvements. San Diego County Board of Supervisors Policy I-99 required operating reserve funds to be at least 50% of each district's annual operating budget and provide for all emergency repairs. The remaining collected funds were allocated to the capital reserve funds.

As of July 1, 2011, the five sanitation districts and the four sewer maintenance districts were reorganized to form one consolidated San Diego County Sanitation District¹ (the County District). As part of the consolidation process, the operating and capital reserve funds from each predecessor district were transferred into one consolidated fund for the County District. In FY 2012-13, DPW identified the remaining capital reserve funds from each predecessor district, previously transferred into the consolidated fund, and allocated them to committed accounts for each district. According to the Board of Supervisors Resolution RO10-04, the funds deposited into the committed accounts should be spent on capital improvements within the district from which the funds were collected.

Audit Scope & Limitations The scope of the audit focused on the adequacy of the controls for the proper use and segregation of operating and capital reserve funds. OAAS evaluated data from FY 2010-11 through FY 2012-13.

This audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing prescribed by the Institute of Internal Auditors as required by California Government Code, Section 1236.

¹The Board of Supervisors approved the consolidation of the districts with the intent to provide rate stability and increase flexibility for planning, funding, and implementing capital improvements.

Methodology

OAAS performed the audit using the following methods:

- Interviewed key personnel on County policies, procedures, and processes relevant to the areas being reviewed.
- Examined County policies and procedures related to the areas being reviewed.
- Evaluated DPW's controls over the use of operating and capital reserve funds before and after consolidation process.
- Recalculated committed accounts for each predecessor district to determine whether they were properly established.
- Reviewed transfer of fixed assets from each predecessor district to the consolidated district to determine whether the transfer was properly recorded.

AUDIT RESULTS**Summary**

Within the scope of the audit, there is reasonable assurance that adequate controls exist for the proper use of funds. However, we determined that the capital reserve funds from each predecessor district were not accurately segregated. Despite this, we found that the total operating and capital reserve funds for all predecessor districts were properly transferred into the consolidated County District. Additionally, we identified improvement opportunities in the payment approval process.

Finding I:**Predecessor Districts' Committed Accounts Need to be Adjusted**

Audit work determined that some funds allocated to the predecessor districts' committed capital reserve accounts in FY 2012-13 need to be adjusted. More specifically, OAAS identified the variances summarized in Table 1.

Table 1. Committed Accounts for FY 2012-13

Predecessor District	Committed Account Established by DPW	Committed Account Per OAAS' Calculation	FY 2012-13 Variance
Spring Valley	\$0	\$2,503,861	\$2,503,861
Lakeside	\$6,239,249	\$10,084,835	\$3,845,586
Winter Gardens	\$5,113,427	\$6,317,583	\$1,204,156
Julian	\$113,222	\$123,029	\$9,807
Pine Valley	\$0	\$65,359	\$65,359
Total	\$11,465,898	\$19,094,667	\$7,628,769

The variance found during the audit is the result of DPW utilizing data from the FY 2012-13 proposed budget instead of the FY 2012-13

adopted budget² to calculate remaining capital funds from each predecessor district. These variances were carried over to the committed accounts balances in FY 2013-14. According to DPW management, adopted budget was not available when committed accounts were established.

Adjustments to the committed accounts are necessary to eliminate the risk of not using capital reserve funds collected prior to the consolidation process for the benefit of the district from which the funds were collected. According to DPW management, capital projects for each of the predecessor districts have been budgeted by the County District for FY 2013-14 and FY 2014-15. The cost related to these projects will be funded by the committed accounts and operating reserve fund. As a result, in FY 2014-15 variances noted during the audit will be reduced to \$2,955,261.

The Board of Supervisors Resolution RO10-04 states that the successor district should maintain separate accounts for each predecessor district that has capital reserve balances as of the consolidation effective date. Upon the effective date, funds from these reserve accounts should only be spent on capital projects that benefit the customers of the predecessor districts from which the reserves were collected.

Recommendation: Due to strict budget process' deadlines, DPW is unable to amend committed accounts balances established for FY 2013-14. However, DPW should utilize adopted budget's data to identify the correct balances to be allocated into the predecessors' district committed accounts for FY 2014-15.

Finding II: **Controls Over Payment Approval Process Need Improvement**
OAAS reviewed a sample of 25 payments made from the predecessor districts operating reserve funds; 11 of which were payments for internal DPW labor services and 14 were payments for contracted goods and services. Audit work found that invoices were not consistently reviewed and approved by management prior to payment. Further, there was no evidence that labor adjustments were approved before they were processed in Oracle, as detailed below.

- **Approval of Billing Invoices.** Of the 14 payments for contracted goods and services selected for review, 8 invoices totaling \$51,840 were not properly approved. More specifically, five invoices were approved by unauthorized approver prior to payment, and three invoices had no evidence of approval. OAAS also found that one of these invoices totaling \$2,468 was paid by the Spring Valley Sanitation District while the expenditure was incurred by the Probation Department.

² The proposed budget is the initial budget provided to the Board of Supervisors for approval. The adopted budget is the budget approved by the Board of Supervisors which includes adjustments made to the proposed budget through the hearing process. Therefore, the adopted budget provides the most reliable projection of future cost.

- **Approval of Labor Adjustments.** Of the 11 payments for internal DPW labor services selected, 1 payment was the result of a labor adjustment which did not have evidence of approval by the authorized manager prior to recording in Oracle.

According to DPW management, invoices and labor adjustments are verbally approved prior to payment or recording in Oracle. However, approvers do not always initial invoices or labor adjustments as indication of approval.

Insufficient payment approval process increases the risk of inaccurate or unauthorized payments made from the districts funds. Proper approval of invoices or labor adjustments is an indication of a strong system of internal controls.

Recommendation:

To strengthen controls over the approval process of invoices and labor adjustments, DPW should:

1. Develop and implement an enhanced process to ensure that all disbursements are approved prior to payment. Also, ensure that evidence of approval is maintained.
2. Develop a training plan to properly communicate the approval process to responsible staff.

To correct inaccurate payment of the invoice, DPW should:

3. Make the necessary adjustments to transfer \$2,468 from the Probation Department to the County District.

Office of Audits & Advisory Services

Compliance

Reliability

Effectiveness

Accountability

Transparency

Efficiency

VALUE

DEPARTMENT'S RESPONSE



County of San Diego

DEPARTMENT OF PUBLIC WORKS

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January 7, 2014

RECEIVED

JAN 10 2014

TO: Juan R. Perez, Chief of Audits
Auditor and Controller (O-305)

FROM: Richard E. Crompton, Director
Department of Public Works (O-332)

OFFICE OF AUDITS &
ADVISORY SERVICES

DEPARTMENT RESPONSE TO AUDIT RECOMMENDATIONS: SAN DIEGO COUNTY SANITATION DISTRICT AUDIT

Finding I: Predecessor Districts' Committed Accounts Need to be Adjusted

OAAS Recommendation: Due to strict budget process' deadlines, DPW is unable to amend committed accounts balances established for FY 2013-14. However, DPW should utilize adopted budget's data to identify the correct balances to be allocated into the predecessors' district committed accounts for FY 2014-15.

Action Plan: DPW notes that OAAS found the methodology used by DPW to determine the amounts to allocate to the predecessor districts' committed accounts was appropriate and accurate. The audit found a variance between the available budget data used to calculate the allocations and the budget data subsequently adopted by the Board of Directors. DPW notes that the adopted budget data was unavailable for use in determining the allocations; however, DPW agrees with the OAAS recommendation to adjust the committed account balances and will update the information as part of the Second Quarter Budget Status Report Board Letter for FY 2013-14.

DPW will include adjustments to the committed accounts as part of the Second Quarter Budget Status Report Board Letter for FY 2013-14 and make any final adjustments as part of the FY 2014-15 Sanitation District budget. The adjustments will be based on FY 2013-14 capital improvement budgets to account for current capital expenditures in the predecessor districts service areas. Based on the FY 2013-14 adopted budgets, the committed account variance to be adjusted for is \$5,024,902.

Planned Completion Date: The budget adjustments will be recommended to the District Board of Directors as part of the Second Quarter Budget Status Report Board Letter for Fiscal Year 2013-14, and any additional updates will be made as part of the adoption of the FY 2014-15 Sanitation District Budget by the District Board of Directors.

Mr. Perez
January 7, 2014
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Contact Information for Implementation: Daniel Brogadir, LUEG Program Manager, (858) 694-2714.

Finding II: Controls Over Payment Approval Process Need Improvement

OAAS Recommendation: To strengthen controls over the approval process of invoices and labor adjustments, DPW should:

1. Develop and implement an enhanced process to ensure that all disbursements are approved prior to payment. Also, ensure that evidence of approval is maintained.
2. Develop a training plan to properly communicate the approval process to responsible staff.

To correct inaccurate payment of the invoice, DPW should:

3. Make the necessary adjustments to transfer \$2,468 from the Probation Department to the County District.

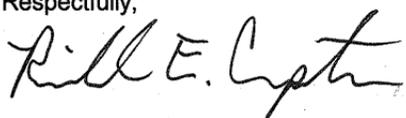
Action Plan: DPW agrees with the finding and has completed the recommended actions to strengthen controls over the approval process (recommendations 1 and 2). These actions included the revision of written procedures for the approval of Sanitation District invoices and labor adjustments to include identification of designated approvers and areas of responsibility, specific documentation requirements for approving managers and review and filing requirements for analysts. The section's Administrative Analyst III is responsible for maintaining, updating and recording any policy changes, including training new staff. Staff training on the approval process has been completed and annual refresher training will be programmed.

Planned Completion Date: Recommendations 1 and 2 have been completed and implemented. Recommendation 3 will be completed in the 3rd Quarter FY 2013-14 and annually thereafter.

Contact Information for Implementation: Daniel Brogadir, LUEG Program Manager, (858) 694-2714.

If you have any questions, please contact me or Mohamad Fakhreddine, Deputy Director, at (858) 694-8948.

Respectfully,



RICHARD E. CROMPTON, Director
Department of Public Works