DEPARTMENT OF FINANCE
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September 3, 2010

Ms. Susan Sims, Chief Deputy Director
California Department of Water Resources
P.O. Box 942836, Room 1115-1
Sacramento, CA 94236-0001

Dear Ms. Sims:

Final Report—Central Basin Municipal Water District, Proposition 13 Grant Audit

The Department of Finance, Office of State Audits and Evaluations (Finance), has completed its audit of Central Basin Municipal Water District's (District) Proposition 13 grant agreement 4600003114 for the period December 30, 2003 through April 15, 2009.

The enclosed report is for your information and use. The District's response to the report findings and our evaluation of the response are incorporated into this final report. The observations in our report are intended to assist management in improving the effectiveness and efficiency of its operations.

In accordance with Finance's policy of increased transparency, the final report will be placed on our website. Additionally, pursuant to Executive Order S-20-09, please post this report in its entirety to the Reporting Government Transparency website at http://www.reportingtransparency.ca.gov/ within five working days of this transmittal.

We appreciate the assistance and cooperation of the District. If you have any questions regarding this report, please contact Frances Parmelee, Manager, or Rich Hebert, Supervisor, at (916) 322-2985.

Sincerely,

David Botelho, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: On following page

cc: Mr. Art Aguilar, General Manager, Central Basin Municipal Water District
Ms. Aileen Hermoso, Chief Financial Officer, Central Basin Municipal Water District
Ms. Perla Netto-Brown, Controller, California Department of Water Resources
Mr. Jim Libonati, Deputy Director, California Department of Water Resources
Mr. Jeffrey Ingles, Chief Auditor, California Department of Water Resources
Ms. Tracie Billington, Chief, Special Projects Section, California Department of Water Resources
Ms. Gail Chong, Chief, Bond Accountability Office, California Department of Water Resources
Mr. Eric Hong, Supervising Engineer, California Department of Water Resources
Mr. Eric Koch, Chief, Flood SAFE Program Management Office, Division of Flood Management, California Department of Water Resources
Mr. Patrick Kemp, Assistant Secretary for Administration and Finance, California Natural Resources Agency
Mr. Bryan Cash, Deputy Assistant Secretary, California Natural Resources Agency
Ms. Julie Alvis, Deputy Assistant Secretary, California Natural Resources Agency

A Grant Audit

Central Basin Municipal Water District
Proposition 13 Bond Program
Grant Agreement 4600003114

Prepared By:
Office of State Audits and Evaluations
Department of Finance

103860039

August 2010

MEMBERS OF THE TEAM

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Final reports are available on our website at http://www.dof.ca.gov

You can contact our office at:

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TABLE OF CONTENTS

Background, Scope, and Methodology 1

Results 3

Response 6

Evaluation of Response 10

BACKGROUND, SCOPE, AND METHODOLOGY

BACKGROUND

In March 2000, voters approved the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Act (Proposition 13), which authorized the State of California to sell $1.97 billion in general obligation bonds. The bond proceeds provide funds for safe drinking water, water quality, food protection, and water reliability programs. Proposition 13 also provides funding for the protection, restoration, and interpretation of the diverse cultural influence and extraordinary human achievements that have contributed to the unique development of California.

The California Department of Water Resources (DWR) is one of many state departments that administer Proposition 13 programs and award funds in the form of grants. One of the programs—the Direct Zero Water Consumption Urinal Install Program—provides funding to local public agencies and incorporated mutual water companies to reduce water and sewer discharge of commercial, institutional, and industrial customers. In December 2003, DWR awarded $780,000 to the Central Basin Municipal Water District (District). Table 1 provides a summary of the project budget:

Table 1: Project Budget Components

Task	Local Cost Share	DWR Grant	Total Project Costs
#1: Purchase 2,600 urinals at $225 each	$156,000	$429,000	$585,000
#2: Pay for 2,600 installations at $75 each	0	195,000	195,000
#3: Develop participant database	0	44,000	44,000
#4: Conduct data analysis for one year	0	92,000	92,000
#5: Provide program results to DWR, MWD[1], etc.	0	20,000	20,000
Total Costs	**$156,000**	**$780,000**	**$936,000**

Source: Grant Agreement 4600003114, Exhibit C

[1] Municipal Water District of Southern California (MWD).

SCOPE

In accordance with the Department of Finance's (Finance) bond oversight responsibilities, Finance conducted an audit of grant agreement 4600003114 for the period December 30, 2003 through April 15, 2009.

The audit objective was to determine whether the District's grant expenditures were in compliance with applicable laws, regulations, and grant requirements. In order to design adequate procedures to evaluate fiscal compliance, we obtained an understanding of the relevant internal controls. We did not assess the efficiency or effectiveness of program operations.

District management is responsible for ensuring accurate financial reporting and compliance with applicable laws, regulations, and grant requirements as well as evaluating the efficiency and effectiveness of the program. DWR and the California Natural Resources Agency are responsible for state-level administration of the bond programs.

METHODOLOGY

To determine whether grant expenditures were in compliance with applicable laws, regulations, and the grant requirements, we performed the following procedures:

- Interviewed key personnel, including the vendor, to obtain an understanding of the grant-related internal controls.
- Examined the grant files maintained by DWR, the grant agreement, and applicable policies and procedures.
- Reviewed the District's accounting records, vendor invoices, warrants, and bank statements.
- Selected a sample of expenditures to determine if costs were allowable, grant-related, incurred within the grant period, supported by accounting records, and properly recorded.
- Performed procedures to determine if other revenue sources were used to reimburse expenditures already reimbursed with grant funds.
- Conducted site visits to verify project existence.

The results of the audit are based on our review of documentation, other information made available to us, and interviews with staff directly responsible for administering bond funds. The audit was conducted from November 2009 through June 2010.

This audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our observations and recommendations based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our observations and recommendations.

Except as noted below, the Central Basin Municipal Water District's (District) expenditures were in compliance with applicable laws, regulations, and the grant requirements. The Schedule of Claimed, Audited, and Questioned Amounts is presented in Table 2.

Table 2: Schedule of Claimed, Audited, and Questioned Amounts

Grant Agreement 4600003114 For the Period December 30, 2003 through April 15, 2009			
Task	**Claimed**	**Audited**	**Questioned**
#1: Purchase 2,600 urinals at $225 each	$ 426,150	$ 312,510	$ 113,640
#2: Pay for 2,600 installations at $75 each	142,050	142,050	0
#3: Develop participant database	0	0	0
#4: Conduct data analysis for one year	0	0	0
#5: Provide program results to DWR, MWD, etc.	0	0	0
Total Expenditures	**$ 568,200**	**$ 454,560**	**$ 113,640**

Observation 1: Certain Grant Agreement Provisions were Not Completed

Most tasks the District agreed to perform were either partially or not completed. Although the District did not seek reimbursement for such tasks (specifically tasks #3 through #5), the District could have claimed up to $156,000 to perform significant data gathering and reporting tasks. The completion of such tasks would have provided the California Department of Water Resources (DWR) valuable information to measure program success. In addition, such tasks were intended to improve and facilitate adequate project monitoring, such as the development of a participant database. Without an established database, key information is not gathered, such as water savings data.

Finance inquired with the District and its vendor, Falcon Water-Free Technologies (Falcon), whether any of these tasks had been completed. Based on our discussions, it appears that some of the activities took place but went undocumented. During our site visits, we also inquired with several customers and were told they were not asked to keep data about water usage or savings.

Although the District contracted with Falcon to complete such tasks, Falcon and its subcontractors work under the direction of the District, which is ultimately responsible for grant compliance. It is imperative to clearly communicate important roles and responsibilities to ensure all the grant agreement provisions are completed.

At the time of our audit, an amendment was not in process to extend the grant agreement's term. Below is a comparison of the expected result of each task and information obtained during our audit:

Table 3: Comparison of Expected Results vs. Audit Results

Task	Expected Results	Audit Results
#1: Purchase 2,600 urinals at $225 each. #2: Pay for 2,600 installations at $75 each.	2,600 Urinals purchased, delivered, and installed to actual customers.	1,894 were installed through April 2009, and some were found to be missing/removed.
#3: Develop a participant database.	A database used to store customer information, such as number and type of urinals installed, and the expected water savings from each site.	No database was produced. Falcon claims database development containing customer data is in progress. However, Falcon has not billed the District for such task.
#4: Conduct data analysis for one year.	A one-year data analysis from actual customers measuring the amounts of water saved.	No data analysis has been conducted. However, the District did not seek reimbursement for this task.
#5: Provide program results to DWR, MWD, etc.	A report to DWR and the MWD summarizing the results of the project.	No report has been submitted. However, the District did not seek reimbursement for this task.

Recommendation:

DWR should determine whether the remaining tasks are still required and feasible, and work with the District to amend the grant agreement as needed.

Observation 2: The District was Reimbursed in Excess of the Allowed Amount

Grant Agreement, Exhibit C, states DWR will reimburse the District $165 per urinal for the purchase of up to 2,600 urinals, and $75 per urinal installation. Total maximum amount the District could claim for the two tasks is $624,000, or $240 per urinal.

According to the District's records, Falcon installed 1,894 urinals, and the District claimed and was reimbursed $300 per urinal. The District's understanding of the grant terms was that it was entitled to $225 for purchase and $75 for installation, totaling $300. Although the grant budget states the maximum amount per urinal is $225, DWR's share is limited to $165 per urinal. As a result, the District was over-reimbursed $113,640.

Recommendation:

The District should reimburse DWR $113,640 for the questioned amount. DWR will make the final determination regarding the resolution of this observation.

Observation 3: Program Accountability is Questionable

Accountability over urinal installations deteriorated throughout the life of the program. At the program's inception, the District had written policies and procedures about the invoicing process. Established controls were intended to ensure the invoices paid were supported by a work order which identified how many urinals were installed at a particular location. The work order was signed by the customer and provided reasonable assurance urinals were installed.

Due to staff turnover, the District subsequently paid invoices without such work orders. Coupled with the fact that the District did not perform on-site inspections or the monitoring tasks discussed in Observation 1, the risk of improper, unsupported, or duplicate payments increases.

The District contracted with Falcon to perform tasks such as project planning, program administration, and data collection; however, many of these tasks remained incomplete or the District could not demonstrate that the tasks had been completed. Neither the District nor Falcon maintained adequate accountability.

In November and December 2009, we conducted site visits to verify installations and determined some urinals were either missing or had been removed. Missing urinals were those installed per Falcon's invoices, but the original urinals were still in place. Removed urinals were those originally installed but were subsequently removed by the customers for various reasons. Reasons for removal were generally customer dissatisfaction, such as the high cost of replacement cartridges, emission of unpleasant odors, and unknown water savings. Discussions with the District indicated they were unaware of the missing/removed urinals.

The results of our inspections are as follows:

Table 4: Inspection Results

Sites Visited	63
Urinals Inspected	542
Urinals identified missing	41
Urinals identified removed	24
% of Urinals missing	7.56%
% of Urinals removed	4.43%

Recommendation:

For future grants, the District should develop monitoring practices and grant management techniques to ensure adequate accountability over bond-funded programs.

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August 24, 2010

Mr. David Botelho, Chief, Office of State Audits and Evaluations
Department of Finance
Office of State Audits and Evaluations
300 Capitol Mall, Suite 801
Sacramento, CA 95814

Dear Mr. Botelho:

Response – Department of Finance Office of State Audits and Evaluations Proposition 13 Grant Audit

Central Basin Municipal Water District has enclosed its response to the draft report for the audit of grant agreement 4600003114 for the period December 30, 2003 through April 15, 2009.

If you have any questions regarding this response or need further assistance, please contact me at (323) 201-5522.

Sincerely,

Aileen Hermoso
Chief Financial Officer

Enclosure

Printed on Recycled Paper

CBMWD Response to Audit Recommendations

Performed by the Department of Finance, Office of State Audits and Evaluations

Proposition 13 Grant Program (#4600003114)

Recommendation #1

DWR should determine whether the remaining tasks are still required and feasible, and work with the District to amend the grant agreement as needed.

CBMWD Response

CBMWD has started working on the remaining tasks, and will work with DWR to amend the grant agreement as needed. The District will request that the amendment authorizes the District to issue a Request for Proposals (RFP) from qualified contractors who will meet the program management standards set forth by the District and DWR to complete the tasks.

Recommendation #2

The District should reimburse DWR $113,640 for the questioned amount. DWR will make the final determination regarding the resolution of this observation.

CBMWD Response

In 2004, CBMWD contracted with Falcon to administer tasks #1-5 of this program. The District's billing to DWR followed Falcon's invoicing format and system. Falcon has been unable to provide sufficient evidence to prove that any tasks other than Task #1 and #2, the purchase and installation of urinals, were completed.

CBMWD intends to continue working with DWR to resolve this issue with Falcon.

Recommendation #3

For future grants, the District should develop monitoring practices and grant management techniques to ensure adequate accountability over bond-funded programs.

CBMWD Response

Aspects of mismanagement identified in this grant program are not indicative of the District's current grant management practices. Since 2006, when West Basin MWD dissolved its joint operation with Central Basin MWD, the District has employed new grant monitoring practices and management techniques for all state and federal grant programs. Furthermore, the original staff assigned to manage this grant from 2003-2006, during which 92% of all installations occurred, is no longer employed at the District. Finally, the District is looking at options to improve the cross training of staff, which will help maintain a consistent level of accountability for all grant programs, particularly in the event that the District undergoes another significant organizational restructuring as it did in 2006.

Table 4: Inspection Results

	Audit Results	CBMWD Results
Sites Visited	63	14
Urinals Inspected	542	194
Urinals identified missing	41	13*
Urinals identified removed	24	17
% of Urinals missing	7.56%	
% of Urinals removed	4.43%	

**CBMWD conducted inspections of the 41 urinals identified as missing by the auditors. CBMWD confirmed only 13 of the urinals were in fact missing. In May 2010 CBMWD received authorization from DWR to install 10 of the 13 urinals found missing at Garfield Elementary School in the City of Montebello. This has now been completed.*

EVALUATION OF RESPONSE

The Department of Finance (Finance) reviewed the Central Basin Municipal Water District's (District) response, dated August 24, 2010, to our draft audit report. We acknowledge the District's willingness to implement the recommendations and take corrective action. For Observation 3, we provide the following comments:

Observation 3: Program Accountability is Questionable

Our inspections were performed in November and December 2009. Because the dates of the District's inspections are unknown, a comparison of our results and the District's results depicted in Table 4 may be misleading. Finance did not perform an analysis of the District's inspection results; therefore, our observation remains as reported.