



Transmitted via e-mail

June 6, 2014

Mr. Mark Cowin, Director
California Department of Water Resources
P.O. Box 942836
Sacramento, CA 94236

Dear Mr. Cowin:

Final Report—CABY Regional Water Management Group, Proposition 84 Grant Audit

The Department of Finance, Office of State Audits and Evaluations, has completed its audit of the Cosumnes American Bear Yuba Regional Water Management Group's (CABY) grant 4600009440 issued by the California Department of Water Resources.

The enclosed report is for your information and use. CABY's response to the draft report observations and our evaluation of the response have been incorporated into this final report. The report will be placed on our website.

We appreciate the assistance and cooperation of CABY. If you have any questions regarding this report, please contact Diana Antony, Manager, or Jon Chapple, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: Ms. Katherine Kishaba, Deputy Director of Business Operations, California Department of Water Resources
Ms. Gail Chong, Deputy Assistant DWR Executive, Bond Accountability, California Department of Water Resources
Ms. Tracie Billington, Chief, Financial Assistance Branch, Division of Integrated Regional Water Management, California Department of Water Resources
Mr. Jeff Ingles, Chief Auditor, California Department of Water Resources
Mr. David Whitsell, Senior Management Auditor, California Department of Water Resources
Mr. Patrick Kemp, Assistant Secretary for Administration and Finance, California Natural Resources Agency
Ms. Julie Alvis, Deputy Assistant Secretary, California Natural Resources Agency
Mr. Bryan Cash, Deputy Assistant Secretary, California Natural Resources Agency
Ms. Elizabeth Martin, President, CABY Regional Water Management Group
Ms. Katie Burdick, Consultant, CABY Regional Water Management Group

AUDIT REPORT

CABY Regional Water Management Group
Proposition 84 Bond Program
Grant Agreement 4600009440

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

MEMBERS OF THE TEAM

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Manager

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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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BACKGROUND, SCOPE AND METHODOLOGY

BACKGROUND

California voters approved the Safe Drinking Water, Water Quality and Supply, Flood Control, River and Coastal Protection Bond Act of 2006 (Proposition 84) for \$5.4 billion. The bond proceeds finance a variety of natural resource programs.

The Integrated Regional Water Management (IRWM) grant program is a competitive grant program created under the Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002 (Proposition 50), with continuing funding provided by Proposition 84.

The program is administered by the California Department of Water Resources (DWR). DWR awards funds to local public agencies and non-profit organizations for projects and programs to improve water supply reliability and improve and protect water quality.

DWR awarded a \$647,593 Proposition 84 grant to Cosumnes American Bear Yuba Regional Water Management Group (CABY). The grant's purpose was to develop or complete a new, or update an existing IRWM plan. CABY is a non-profit organization and a collaborative planning effort comprised of more than 30 organizations, representing water supply, conservation, recreation, agriculture, and community interests, as well as federal and local governments. CABY functions as a vehicle to bring funding into the Cosumnes, American, Bear, and Yuba watershed regions, as well as bringing diverse stakeholders together.¹

SCOPE

In accordance with the Department of Finance's bond oversight responsibilities, we audited grant agreement 4600009440 for the period February 22, 2011 through April 30, 2012.²

The audit objectives were to determine whether CABY's grant expenditures claimed were in compliance with applicable laws, regulations, and grant requirements; and to determine whether the grant deliverables were completed as required. We did not assess the efficiency or effectiveness of program operations.

CABY's management is responsible for ensuring accurate financial reporting and compliance with applicable laws, regulations, and grant requirements. DWR and the California Natural Resources Agency are responsible for the state-level administration of the bond program.

¹ www.cabyregion.org.

² This was an interim audit as fieldwork was performed prior to the grant end date of September 30, 2013.

METHODOLOGY

To determine whether grant expenditures were in compliance with applicable laws, regulations, and the grant requirements; and if the grant deliverables were completed as required, we performed the following procedures:

- Interviewed key personnel to obtain an understanding of the grant-related internal controls.
- Examined the grant files, the grant agreement, and applicable policies and procedures.
- Reviewed CABY's accounting records, contracts, vendor invoices and payment requests.
- Reviewed the contractor accounting records, vendor invoices and timesheets.
- 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.
- Evaluated whether a sample of grant deliverables were met by reviewing supporting documentation.

We conducted this audit in accordance with generally accepted government performance auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our observations and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our observations and conclusions based on our audit objectives.

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 grant funds.

Except as noted below, the grant expenditures claimed were in compliance with the requirements of the grant agreement. Because the project was active at the time of our site visit, not all deliverables were completed; however, the Cosumnes American Bear Yuba Regional Water Management Group (CABY) has completed interim deliverables in accordance with the grant agreement. The Schedule of Claimed and Questioned Amounts is presented in Table 1.

Table 1: Schedule of Claimed and Questioned Amounts

Grant Agreement 460009440		
Task	Claimed	Questioned
Grant Funds		
1. Administration and Program Mgmt.	\$ 49,813	
2. Stakeholder Involvement	85,320	\$ 25,376
3. Disadvantaged Community	41,779	10,694
4. Update Region Description	16,406	
5. Resource Mgmt. Strategies	5,073	
6. Land Use Coordination	7,064	2,569
7. Local Water Planning	3,715	
8. Objectives	11,311	1,320
9. Climate Change	12,721	2,497
10. Project Development	37,549	3,960
11. Plan and Project Performance	1,303	
12. Data Management	18,273	
13. Finance	3,981	
14. Impacts and Benefits	165	
15. Technical Analysis	525	
16. Regional Coordination	12,381	
17. IRWMP Preparation	8,216	3,300
Total Grant Funds	315,595	49,716
Match Funds	323,649	
Total Project Funds	\$ 639,244	\$ 49,716

Our audit found significant control deficiencies which impair CABY's grant fiscal oversight. Further, the grant was subcontracted to a primary contractor who also acts as the CABY executive director and manages several key fiscal duties of the grant.

Specifically, on February 22, 2011, California Department of Water Resources (DWR) awarded the Proposition 84 grant to CABY, a non-profit organization. On February 23, 2011, the entire grant was sub-contracted to a sole-proprietor (contractor). The contractor also acts as the executive director of CABY. This lack of operational independence creates a conflict of interest between CABY and its contractor. This conflict, in combination with the weak fiscal controls noted below, exposes the grant funds to loss or misuse.

Observation 1: Significant Lack of Fiscal Controls

As noted in the text box, one individual acting as both the executive director and the primary contractor for CABY performed several conflicting duties that compromise the internal control structure.

Although CABY established written policies and procedures, they were not implemented as intended. Specifically, according to CABY's Accounting Policies and Procedures Manual (2011), the CABY treasurer should receive bank statements and review bank reconciliations. Additionally, the CABY fiscal manager should reconcile bank accounts and only CABY board members should have check signing authority over CABY bank accounts.

When brought to the attention of CABY's board members,¹ they acknowledged the conflicts and stated they would be implementing the established policies and procedures and/or developing new procedures to ensure proper segregation of duties.

Proper segregation of duties is a key element of an entity's internal control, and is essential to reducing the risk of erroneous or inappropriate actions. Typically, no one person should initiate, approve, record, and reconcile a transaction, and have custody of funds.

Grant Agreement, Exhibit D, section D.1.b, requires, at a minimum, that the grantee's fiscal controls and accounting procedures be sufficient to permit tracing of grant funds to a level of expenditure adequate to establish that such funds have not been used in violation of state law or the grant agreement.

Recommendation:

Develop and implement policies and procedures to ensure proper segregation of fiscal duties. CABY should consider whether it is appropriate to contract with an entity that may create a conflict.

Executive Director/Contractor Conflicting Fiscal Duties

- ✓ Prepares DWR (state) reimbursement claims
- ✓ Receives DWR (state) reimbursement checks
- ✓ Makes deposits to the CABY bank account
- ✓ Has signature authority over CABY bank account
- ✓ Prepares CABY checks made payable to herself
- ✓ Receives CABY bank statements
- ✓ Oversees CABY bank reconciliations
- ✓ Receives CABY mail

¹ Board members specifically included CABY's current and past president and treasurer.

Observation 2: Weak Contract Management Resulted in Questioned Costs

The lack of contract management oversight resulted in the following questioned costs and fiscal deficiencies.

- CABY submitted reimbursement claims for \$18,480 and \$31,236 in contractor and subcontractor costs, respectively, that had not been paid. Specifically, reimbursement claims submitted to the DWR for the period November 2011 through April 2012 included costs which had not been paid to the contractor and subcontractors as of April 30, 2012. The questioned costs noted above are based on a sample of claimed expenditures.
- Time-keeping records need improvement. The contractor did not maintain timesheets to account for all hours worked during each payroll period. This prevented a determination of whether the contractor adequately allocated her total time between projects.
- The primary contractor did not have a written contract or agreement with three of its subcontractors. Additionally, other subcontractors were paid in excess of their contracted rate, and subcontractor invoices did not contain a description of the work performed or sufficient detail to determine what project-related tasks were completed. Without valid contracts and invoices that clearly describe the work performed and final deliverables, there is an increased risk of deliverables not being completed as required.

Grant Agreement, Exhibit D, section D.1.a, requires the grantee to maintain audit and accounting procedures in accordance with generally accepted accounting principles and practices, and is required to keep complete and accurate records of all grant receipts and disbursements. Further, this section also requires the grantee to ensure its contractors or subcontractors maintain books, records, and other documents pertinent to their work.

Grant Agreement, section 7, requires invoices (reimbursement claims) to be submitted with receipts and supporting documentation certifying costs were incurred.

Grant Agreement, Exhibit A, section 1.3, requires the grantee to identify required consultants and sub-consultants, negotiate contracts with those entities and supervise completion of contracts and deliverables. Further, per the State Contracting Manual, a contract must contain a performance term or contract completion dates, the maximum amount to be paid, a clear scope of work, and a performance schedule.

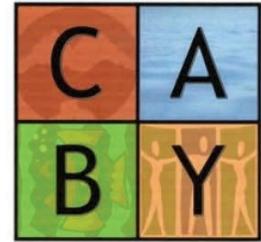
Recommendations:

- A. Remit \$49,716 in questioned costs to DWR. DWR will determine the final disposition of the questioned costs.
- B. Ensure all claimed expenditures have been incurred and paid prior to requesting reimbursement from the state.
- C. Maintain timesheets accounting for 100 percent of contractor time.
- D. Execute complete valid contracts with all subcontractors and consultants performing state-funded services and ensure the work performed complies with the grant agreements.

April 8, 2014

VIA E-MAIL : OSAEReports@dof.ca.gov

Mr. Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations
California Department of Finance



Cosumnes, American, Bear & Yuba River
Integrated Regional Water Management

Re: Written Response to Draft Report—CABY Regional Water Management Group,
Proposition 84 Grant Audit, Dated: March 25, 2014

Dear Mr. Sierra:

On behalf of the CABY Regional Water Management Group (hereinafter referred to as “CABY RWMG”), I am writing in response to the above-referenced Draft Report of March 25, 2014 (hereinafter referred to as the “Draft Report”).

Before addressing the specific observations and recommendations of the Draft Report, I want to personally recognize the extraordinary effort of DOF Supervisor Jon Chapple in conducting this audit. He is truly an asset to your department and deserves recognition for his dedication and professionalism. This has been an extremely valuable learning experience for the leadership of the CABY RWMG, which has and will continue to implement the guidance afforded through this process. Many of the recommendations of the Draft Report, which CABY had already begun to implement following early discussions with John, have and will continue to be implemented to strengthen the long-term viability and success of the CABY RWMG. We wish to thank you and your staff for assisting us to improve as an organization and fulfill a critical function for the IRWM region we serve.

Response to Observation 1:

Separation of duties: As of December 31, 2011, the contract engaging the “primary contractor” of CABY RWMG (Burdick & Co. and its principal Katie Burdick) as Executive Director expired. Thus, while performing the work of grant agreement #4600009440 (hereinafter referred to as the “Grant Agreement”) Ms. Burdick no longer served as Executive Director to the CABY RWMG. From 2007 – 2011, Ms. Burdick performed the functions of Executive Director of the CABY Integrated Regional Water Management (IRWM) effort, including CABY RWMG, as an independent contractor under a written professional services agreement with Nevada Irrigation District (NID), the fiscal agent for the CABY IRWM effort at that time. That agreement was entered into after a competitive process open to the public.

The agreement expired 12/31/11 and has not been renewed. Nor has any other written or oral contract been entered into with Ms. Burdick to perform such Executive Director services for the CABY RWMG or any other facet of the overall CABY IRWM effort. Since 12/31/11, Ms. Burdick's sole duty for CABY RWMG has been to perform the work of the Grant Agreement. In fact, the role of Executive Director has remained vacant since December of 2011 with volunteer Board members providing day-to-day administrative services for CABY RWMG. The CABY RWMG never had any employees or staff.

Implementation of Policies and Procedures to Ensure Segregation of Fiscal Duties:

Upon notification of the inconsistent implementation of existing written policies and procedures of CABY RWMG early in the audit process, the CABY RWMG Board of Directors took immediate action to revise the fiscal management process to ensure greater fiscal control. Specifically, the process now proceeds as follows:

1. Each invoice (including supporting documentation) under the Grant Agreement is prepared by CABY RWMG's consultant who then delivers it directly to the President of the Board of Directors of CABY RWMG for his or her review.
2. After his or her review and approval, the Board President delivers the invoice directly to DWR.
3. Upon receipt of payment to CABY RWMG by DWR, the Treasurer of the Board of Directors of CABY RWMG reconciles the payment from DWR with the record of invoicing by CABY RWMG and then deposits the check from DWR in the CABY RWMG bank account and receives a copy of the proof of deposit from the bank for the records of CABY RWMG.
4. Thereafter, the Board Treasurer prepares, signs, issues and records a check to the consultant of CABY RWMG for payment of services performed.

Currently, only the President and Treasurer of the Board of Directors are authorized signatories on the bank account for CABY RWMG. CABY RWMG has requested in writing to DWR that all future correspondence from DWR to CABY RWMG, including any and all payments under the Grant Agreement, be sent to a new address that is accessible only to the officers of the Board of CABY RWMG.

Response to Observation 2:

Questioned costs: The Draft Report indicates that CABY RWMG failed to follow its contractual requirements with DWR under the Grant Agreement by submitting invoices for contractor and subcontractor costs that were incurred but not paid by CABY RWMG prior to invoicing DWR. The Draft Report recommends CABY RWMG "ensure all claimed expenditures have been incurred and paid prior to requesting reimbursement from the state." Moreover, the Draft Report recommends remittance to DWR of \$49,716 in "questioned costs" that were

invoiced to DWR before CABY RWMG paid its contractor and subcontractor. Additionally, the Draft Report states that invoices submitted to DWR included costs that had not been paid by CABY RWMG to its contractor and subcontractors “as of April 30, 2012.” Candidly, these observations and recommendations came as a complete surprise to CABY RWMG.

CABY RWMG has diligently followed the stated procedures for invoicing and payment in the Grant Agreement and the direction provided by DWR staff throughout the project. The Grant Agreement states that invoices are to be submitted to DWR for “costs incurred” by the grantee in performance of the project. There is no requirement anywhere in the Grant Agreement for CABY RWMG to pay its contractor or subcontractors before submitting an invoice to DWR. Moreover, DWR staff received and approved each invoice without ever communicating anything to anyone at CABY RWMG to even suggest this was required. There have been no requests for proof of payment or even any mention of the subject by anyone at DWR. Likewise, other IRWM groups across the state who have received similar grant funds under Proposition 84 have followed the exact same invoice and payment process as CABY RWMG. The approach recommended by the Department of Finance has never applied to this project.

Per the requirements of the contract and consistent with direction from DWR staff, CABY RWMG submitted each invoice to DWR after incurring costs for services performed by CABY RWMG’s contractor and subcontractors on the project. Immediately upon receipt of each payment from DWR, CABY RWMG, has disbursed those funds in their entirety to its contractor. As the attached documentation shows, all amounts invoiced by CABY RWMG to DWR to date have been paid in full to CABY RWMG’s contractor without delay, including all of the funds in question (\$49,716). The documentation shows that all amounts invoiced to DWR as of the close of the audit period (April 30, 2014) have been paid in full to the contractor. Since no other funds are at issue, there is no basis to remit any monies to DWR.

With regard to the recommendation to maintain timesheets for 100 percent of contractor time, CABY RWMG will reevaluate its contract requirements for the future with regards to the level of detail and format of timesheet information from its contractors. Notwithstanding the absence of this requirement under existing contractual arrangements, CABY RWMG’s existing contractor, Burdick & Co., has offered to provide additional timesheet information for all of its clients during the audit period, which will substantiate all hours billed to the CABY project.

As for the recommendation that the contractor execute valid contracts with all of its subcontractors, the contractor on this project has already executed written agreements with all of its subcontractors. Those agreements can be made available for review.

In closing, we appreciate your efforts to protect the public's investment in our state's water resources. We share your commitment and will use the lessons learned from this process to improve our effectiveness in accomplishing this important work.

Sincerely,

Original signed by:

Elizabeth J. Martin
President, CABY RWMG

EVALUATION OF RESPONSE

We reviewed the Cosumnes American Bear Yuba Regional Water Management Group's (CABY) April 8, 2014 response to the draft audit report. While CABY generally agreed with the audit observations and recommendations, CABY provided additional comments for both observations. CABY also provided additional documentation in response to Observation 2. The Attachment to the response was removed for brevity and consisted of accounting records supporting CABY reimbursement claims. In evaluating CABY's response, we provide the following:

Observation 1: Significant Lack of Fiscal Controls

CABY generally agreed with the observation and states it has implemented policies and procedures to ensure adequate segregation of fiscal duties. With regard to the same individual acting as both the executive director and primary contractor, CABY claims this person served as executive director until December 31, 2011. However, we were informed on numerous occasions by CABY board members that during the time of our audit, this person was acting as both the executive director and primary contractor. Furthermore, we note the grant term start date was February 22, 2011. We acknowledge CABY's implementation of policies and procedures to improve its fiscal controls and continue to recommend it reconsider whether to contract with an entity that may create a conflict. The observation and recommendation remain unchanged.

Observation 2: Weak Contract Management Resulted in Questioned Costs

CABY claims there is no requirement to pay its contractors or subcontractors prior to submitting a reimbursement claim to the California Department of Water Resources (DWR). However, this grant was awarded on a reimbursement basis and the grant agreement specifically prohibits advanced funds.

CABY provided documentation in its response relating to the questioned costs of \$49,716. Although we did not audit this subsequent information, we noted payments were made to the contractor and subcontractor after April 30, 2012 (the reimbursement claims submitted to DWR claimed project expenditures during the period November 2011 through April 2012). Because this documentation shows the vendors were not actually paid prior to submitting the reimbursement claims to DWR, our recommendation that DWR should determine the final disposition of the questioned costs remains unchanged.