



Transmitted via e-mail

September 10, 2014

Mr. Mark Cowin, Director
California Department of Water Resources
P.O. Box 942836, Room 1115-1
Sacramento, CA 94236-0001

Dear Mr. Cowin:

Final Report—San Diego County Water Authority, Propositions 84 and 50 Grant Audits

The Department of Finance, Office of State Audits and Evaluations, has completed its audits of the San Diego County Water Authority's (Authority) grants 4600009346 and 4600008209. These grants were issued by the California Department of Water Resources.

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

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

Sincerely,

Original signed by:

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

Enclosure

cc: Ms. Laura King Moon, Chief Deputy Director, California Department of Water Resources
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
Mr. Jeff Ingles, Chief Auditor, California Department of Water Resources
Ms. Tracie Billington, Chief, Financial Assistance Branch, Division of Integrated Regional Water Management, 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. Maureen Stapleton, General Manager, San Diego County Water Authority
Mr. Rodney Greek, Controller, San Diego County Water Authority
Mr. Mark Stadler, Principal Water Resource Specialist, San Diego County Water Authority
Ms. Loisa Burton, Grant Administrator, San Diego County Water Authority

San Diego County Water Authority
Proposition 50 and 84 Bond Programs
Grant Agreements 4600009346 and 4600008209



Wetlands Creation at the San Diego Wild Animal Park
Source: San Diego County Water Authority

Prepared By:
Office of State Audits and Evaluations
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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 Water Security, Clean Drinking Water, Coastal and Beach Protection Act of 2002 (Proposition 50), and the Safe Drinking Water, Water Quality and Supply, Flood Control, River and Coast Protection Bond Act of 2006 (Proposition 84) for \$3.44 billion and \$5.4 billion, respectively. The bond proceeds finance a variety of natural resource programs.

The San Diego County Water Authority (Authority) is an independent public agency serving the San Diego region as a wholesale supplier of water. Its mission is to provide a safe and reliable supply of water to its 24 member agencies. The agencies in turn provide the water to their retail customers, residents and businesses in San Diego County. The Authority also works with its member agencies to develop local supplies and promote water efficiency¹.

The Authority received the following Proposition 50 and 84 grants from the California Department of Water Resources (DWR):

- *Integrated Regional Water Management Plan (IRWMP)* (Grant 4600009346) – \$1 million to develop and complete an IRWMP. The IRWMP is a comprehensive planning document prepared on a region-wide scale that not only plans for, but ensures implementation of, priority water resource projects and programs.
- *IRWMP Implementation* (Grant 4600008209) – \$25 million to construct or implement 19 project components associated with the San Diego IRWMP. The Authority sub-granted funds to local project sponsors (local sponsors) to construct or implement the project components. Local sponsors, comprised of local government agencies and non-profit entities, are required to provide match for their individual projects. In total, \$374 million will be contributed as match to complete all projects.

SCOPE

In accordance with the Department of Finance's bond oversight responsibilities, we audited the following grants:

<u>Grant Agreement</u>	<u>Audit Period</u>
4600009346	February 22, 2011 through July 3, 2012 ²
4600008209	June 18, 2008 through June 30, 2012 ³

¹ Source: <http://www.sdcwa.org/frequently-asked-questions-and-key-facts#t7n116>.

² An interim audit was conducted since audit fieldwork was performed prior to the grant end date of October 31, 2013.

³ An interim audit was conducted since the grant term ends December 31, 2014.

The audit objectives were to determine whether the Authority'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.

The Authority'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.

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 agreements, and applicable policies and procedures.
- Reviewed five projects totaling \$5.7 million in local sponsor awards to determine if projects were within scope and cost. See Appendix A for projects reviewed.
- Selected a sample of grantee and local sponsor 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.
- Evaluated whether a sample of grant deliverables were met by reviewing supporting documentation and conducting site visits to verify project existence.

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 audits 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 complied with the grant agreement requirements. Because the grants were active at the time of our site visit, not all deliverables were completed. The Schedules of Claimed and Questioned Amounts is presented in Table 1.

Table 1: Schedules of Claimed and Questioned Amounts

Grant Agreement 460009346		
Task	Claimed¹	Questioned
Plan Update & Program Services	\$ 119,737	\$ 0
Planning Studies	30,610	0
Public Outreach	29,663	0
Proposal Administration	13,010	0
Total Grant Funds	193,020	0
Match Funds	268,663	0
Total Project Expenditures	\$ 461,683	\$ 0

Grant Agreement 460008209		
Task	Claimed²	Questioned
Proposal Administration	\$ 378,256	\$ 0
Direct Project Administration Costs	55,313	0
Land Purchase/Easement	1,925,481	0
Planning/Design/Engineering/Environmental Documentation	1,122,182	305,177
Construction/Implementation	4,344,481	0
Environmental Compliance/Mitigation/Enhancement	18,504	0
Construction Administration	413,477	0
Other Costs	52,423	0
Construction/Implementation Contingency	146,581	0
Total Grant Funds	8,456,698	305,177
Total Match	6,519,498	56,311
Total Project Expenditures	\$ 14,976,196	\$ 361,488

¹ Reflects amounts claimed through July 3, 2012.

² Reflects amounts claimed through June 30, 2012.

As noted in the Background section, grant 4600008209 was sub-granted to 19 separate local sponsors. The San Diego County Water Authority (Authority) is responsible for overall grant oversight and compliance, and is charged with ensuring the local sponsors adhere to the grant requirements. The following observations pertain to grant 4600008209 and are based on a sample of five sponsors. For further detail on each sponsor reviewed, see Appendix A.

Observation 1: Unsupported and Unallowable Expenditures Claimed

Two of five local sponsors reviewed claimed unsupported or unallowable expenditures, or did not maintain an adequate audit trail, as noted below.

Questioned Costs-San Diego Coastkeeper (Coastkeeper):

- Coastkeeper claimed unsupported personnel costs of \$305,177 for Project 15 (see Appendix A-3). In some cases, no documentation was provided to support the hours or the rates claimed. In other cases, the claimed hourly rates for staff and independent contractors were not supported. For example, Coastkeeper claimed \$85 per hour for a watershed director position; however, only \$28.26 per hour was adequately supported. Independent contractors were paid \$20 per hour, but reimbursement was claimed at \$50 per hour. Coastkeeper claimed the unsupported labor costs represented overhead or indirect costs. However, the indirect rate methodology provided was not supported, reasonable, and was not previously approved by the Department of Water Resources (DWR). Section 7a of the agreement between the Authority and Coastkeeper states administrative expenses may include appropriate pro-rata allocation of overhead and administrative expenses only when agreed to by the Authority and local sponsor and when approved by the state. No documentation was provided to indicate the indirect cost rate was approved.
- Coastkeeper claimed and was reimbursed \$38,422 in subcontractor costs for the period March through June 2012. Coastkeeper did not pay the subcontractors until April 2013, after we brought the nonpayment issue to Coastkeeper's attention, and four months after receiving payment from the Authority. We did not question this amount because it was ultimately paid.
- Coastkeeper did not provide adequate supporting documentation for \$56,311 of match expenditures. The cash match claimed could not be traced to project-related expenditures. See Appendix A-3.

Lack of Audit Trail-City of San Diego (City):

- The City did not track match funds separately for Project 6. Consequently, project expenditures could not be traced to specific funding sources (see Appendix A-2). In addition, the City also claimed match against budget line items that were not identified as match expenditures in the original grant budget for Project 2 (see Appendix A-1). We did not question the related costs because they were supported on a total basis, and sufficient match was provided in the authorized budget categories.

The Authority is responsible for ensuring local sponsors claim costs that are allowable, grant-related, incurred within the grant period, and supported by accounting records. The Authority should implement stronger fiscal controls to ensure future claims are adequately supported.

Grant Agreement, section 8, requires the grantee to assign local project sponsors to act on behalf of the grantee for the purposes of individual project management, oversight, compliance, operations and maintenance.

Grant Agreement, Exhibit D, section D.1, requires the grantee *and its local project sponsors* to maintain books, records and other documents pertinent to their work in accordance with generally accepted accounting principles and practices. Section D.19 requires accurate records of costs, disbursements, and receipts with respect to activities under the grant agreement.

Recommendations:

- A. Remit \$305,177 to DWR for unsupported personnel expenditures. DWR will determine the final disposition of the questioned grant costs and the questioned match costs, since the completion date for Project 15 is scheduled for December 2014.
- B. Ensure local sponsors maintain a clear audit trail for all claimed grant and match expenditures by project and funding source. The audit trail should facilitate the tracing of expenditures claimed on payment requests to the accounting records and source documents.
- C. Ensure indirect cost rates are well-documented and approved in accordance with agreements between the Authority and the local sponsor.
- D. Ensure all claimed expenditures have been incurred and paid prior to requesting reimbursement from the state.

Observation 2: Oversight of Grant Deliverables Needs Improvement

Two of five projects reviewed deviated from the grant's scope of work without obtaining prior written approval.

- County of San Diego (Project 19) was awarded funds for the removal and replacement of 14,000 square feet of existing impervious pavement with porous pavement to reduce runoff in the San Diego County Chollas Creek. During our site visit, we observed only a portion of the existing impervious pavement had been removed. Further review of the project completion report revealed that only 6,250 square feet (45 percent of 14,000) of impervious pavement was removed and replaced with porous pavement (see Appendix A-5). Scope changes require pre-approval.
- Coastkeeper project (Project 15) required data-sharing via a web-based, publicly accessible data portal. The grant funded a publicly accessible website for data-sharing; however, the website was inaccessible at the time of our site visit. Subsequent to our visit, the website was reinstated. Without continuous public access to the data collected, the full grant objectives cannot be met.

In addition to scope change approvals, project budgets should be reviewed to determine if budget modifications are warranted. No budget review was submitted to DWR for the scope changes noted above. As the grantee, the Authority is responsible for ensuring local sponsors fulfill all grant agreement requirements.

Grant Agreement, section 23, requires the grantee to ensure the commencement and continued operation of the projects, and ensure the projects are operated in an efficient and economical manner.

Grant Agreement, section 25, states that no substantial change in the scope of the projects should be undertaken until written notice of the proposed change has been provided to the state and the state has given written approval for such change.

Recommendations:

- A. For future project scope changes, obtain written approval from the grantor before making any changes to the grant's scope of work. For significant scope changes, review the project budget to determine if a budget modification is warranted.
- B. Develop and implement oversight procedures to ensure that deliverables are completed as required in the grant agreement.

Results of Local Project Sponsor Reviews

Project Number: 2

Project Sponsor: City of San Diego (City)

Project Name: Irrigation Hardware Giveaway and Cash for Plants Program

Project Description: Offer customized commercial and residential landscape surveys and state-of-the-art irrigation hardware (weather-based irrigation controllers and drip/micro spray/sprinkler heads) free-of-charge to customers with irrigation systems at landscaped sites throughout the City. Cash for Plants offers rebates to customers to convert high water use landscapes to low water use landscapes. The project is intended to conserve water and reduce pollutant-laden runoff.

Grant Amount: \$1,121,670

Total Project Cost: \$1,499,798

Project Term: February 16, 2010 through December 31, 2014

Schedule of Claimed and Questioned Amounts

Task	Claimed	Questioned
Proposal Administration	\$ 15,569	\$ 0
Direct Project Administration	3,954	0
Planning/Design/Engineering/Environmental Documentation	15,883	0
Construction/Implementation	383,157	0
Total Grant Funds	418,563	0
Match Funds	180,844	0
Total Project Expenditures	\$ 599,407	\$ 0

Compliance and Questioned Costs

Grant expenditures claimed were in compliance with grant agreement terms and were properly supported.

However, match was claimed against budget line items that were not identified as match expenditures in the original grant budget. For example, \$15,883 was claimed as match for Planning, Design, and Engineering. However, the project budget did not include match for that particular line item. We did not question this amount because sufficient match was provided in the authorized budget categories. See observation 1.

Deliverables

The project is active. Project 2 is scheduled for completion December 31, 2014.

Project Number: 6

Project Sponsor: City of San Diego (City)

Project Name: City of San Diego Recycled Water Distribution System Expansion and Parklands/Open Space Recycled Water Retrofits, and Indirect Potable Reuse/Reservoir Augmentation Demonstration Project

Project Description: Install 9,000 feet of new recycled water pipe to distribute recycled water to irrigate community open spaces, medians, slopes and the State Route 56 freeway in northern San Diego; extend the existing recycled water distribution system to serve potable water customers that have retrofitted their properties to accept recycled water; implement an indirect potable reuse and reservoir augmentation program.

Grant Amount: \$3,424,750

Total Project Cost: \$13,522,750

Grant Term: June 18, 2008 through December 31, 2014

Schedule of Claimed and Questioned Amounts

Task	Claimed	Questioned
Proposal Administration	\$ 47,537	\$ 0
Planning/Design/Engineering/Environmental Documentation	360,000	0
Construction/Implementation	2,508,000	0
Construction Administration	325,000	0
Other Costs	25,000	0
Construction/Implementation Contingency	0	0
Total Grant Funds	3,265,537	0
Match Funds	2,769,989	0
Total Project Expenditures	\$ 6,035,526	\$ 0

Compliance and Questioned Costs

Grant expenditures claimed were in compliance with grant agreement terms and were properly supported. However, the City did not track match funds separately. Project 6 was funded by multiple sources and the City tracked all expenditures at the project level and not by funding source. Consequently, project expenditures could not be traced to specific funding sources. See Observation 1.

Deliverables

Project is active. Project 6 is scheduled for completion December 31, 2014.

Project Number: 15

Project Sponsor: San Diego Coastkeeper (Coastkeeper)

Project Name: San Diego Regional Pollution Prevention

Project Description: Engage the community to remove inland and coastal trash. Teach community members how to monitor water quality, access publicly available water quality data, and analyze and interpret these data to identify water quality impacts for the purpose of addressing pollution and improving water quality. All information and data generated will be shared regionally through education, outreach and community involvement.

Grant Amount: \$721,000

Total Project Cost: \$866,518

Project Term: June 18, 2008 through December 31, 2014

Schedule of Claimed and Questioned Amounts

Task	Claimed	Questioned
Proposal Administration	\$ 21,000	\$ 0
Direct Project Administration	14,475	0
Planning/Design/Engineering/Environmental Documentation	523,547	305,177
Construction/Implementation	122,650	0
Environmental Compliance/Mitigation/Enhancement	9,043	0
Other Costs	11,533	
Total Grant Funds	702,248	305,177
Match Funds	140,588	56,311
Total Project Expenditures	\$ 842,836	\$ 361,488

Compliance and Questioned Costs

As noted in Observation 1, grant expenditures and match were not in compliance with grant agreement terms nor were they properly supported, as follows:

Grant Funds

- Questioned Costs \$305,177 – Hourly rates claimed for Coastkeeper staff and independent contractors were not supported. For example, Coastkeeper claimed \$85 per hour for the Executive Director's time spent on the project. However, only \$28.26 per hour was supported. Independent contractors were paid \$20 per hour, but reimbursement was claimed at \$50 per hour.
- Coastkeeper stated the unsupported labor costs represented overhead or indirect costs. However, the methodology provided to support the allocation of the indirect costs was not reasonable. For example, overhead costs were

allocated based on total labor costs charged to the grant as a percentage of all labor costs. However, the labor costs charged to the grant included the unsupported overhead costs, and therefore could not be used in a formula to determine the overhead costs.

- Subcontractor Expenditures – Coastkeeper claimed and was reimbursed for \$38,422 in subcontractor expenditures incurred from March through June 2012. Coastkeeper did not pay the subcontractors until April 2013, after we brought the nonpayment issue to Coastkeeper’s attention, and four months after receiving payment from the Authority. We did not question this amount because it was ultimately paid.

Match Funds

- Coastkeeper did not provide adequate supporting documentation for \$56,311 of match expenditures. Coastkeeper’s match included in-kind labor provided by volunteers and other cash funds. While in-kind labor was supported, the cash match could not be traced to project-related expenditures.

Deliverables

The project was not completed in accordance with the grant agreement requirements.

- The grant agreement required data-sharing via a web-based, publicly accessible data portal. While the grant funded a publicly accessible website for data-sharing, it was inaccessible at the time of initial fieldwork. Subsequent to our visit, the website was reinstated.

Project is active. Project 15 is scheduled for completion December 31, 2014.

Project Number: 16

Project Sponsor: San Diego Zoo Safari Park (Park)

Project Name: Biofiltration Wetland Creation and Education Program

Project Description: Develop wetlands in the Park to act as biological filters to improve water quality within the Park, enhance habitat, and reduce water consumption. Incorporate wetlands demonstration into tours as community outreach and education.

Grant Amount: \$721,100

Total Project Cost: \$862,100

Project Term: February 2, 2010 through December 31, 2014

Schedule of Claimed and Questioned Amounts

Task	Claimed	Questioned
Proposal Administration	\$ 21,000	\$ 0
Direct Project Administration	10,700	0
Construction/Implementation	520,300	0
Construction Administration	60,000	0
Other Costs	9,000	0
Construction/Implementation Contingency	100,000	0
Total Grant Funds	721,000	0
Match Funds	141,100	0
Total Project Expenditures	\$ 862,100	\$ 0

Compliance and Questioned Costs

Grant expenditures and match claimed were in compliance with grant agreement terms and properly supported.

Deliverables

Project is complete.

Project Number: 19

Project Sponsor: County of San Diego, Department of General Services

Project Name: County of San Diego Chollas Creek Runoff Reduction and Ground Water Recharge

Project Description: Demonstrate implementation of a range of low impact development practices to reduce runoff from two county facilities in the Chollas Creek sub-watershed of the Pueblo San Diego hydrological unit.

Grant Amount: \$618,000

Total Project Cost: \$728,000

Grant Term: April 26, 2010 through December 31, 2014

Schedule of Claimed and Questioned Amounts

Task	Claimed	Questioned
Proposal Administration	\$ 18,000	\$ 0
Planning/Design/Engineering/Environmental Documentation	178,000	0
Construction/Implementation	371,700	0
Construction Administration	0	0
Other Costs	0	0
Construction/Implementation Contingency	50,300	0
Total Grant Funds	618,000	0
Match Funds	75,805	0
Total Project Expenditures	\$ 693,805	\$ 0

Compliance and Questioned Costs

Grant expenditures claimed were in compliance with grant agreement terms and were properly supported.

Deliverables

The project is closed. However, not all grant agreement deliverables were completed.

The grant agreement required the removal and replacement of 14,000 square feet of existing impervious pavement with porous pavement at the Central Regional Public Health Facility. However, only 6,250 square feet of existing impervious pavement was removed and replaced. See Observation 2.



San Diego County Water Authority

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June 30, 2014

VIA EMAIL TO: OSAEReports@dof.ca.gov

MEMBER AGENCIES

- Carlsbad Municipal Water District
- City of Del Mar
- City of Escondido
- City of National City
- City of Oceanside
- City of Poway
- City of San Diego
- Fallbrook Public Utility District
- Helix Water District
- Lakeside Water District
- Olivenhain Municipal Water District
- Otay Water District
- Padre Dam Municipal Water District
- Camp Pendleton Marine Corps Base
- Rainbow Municipal Water District
- Ramona Municipal Water District
- Rincon del Diablo Municipal Water District
- San Dieguito Water District
- Santa Fe Irrigation District
- South Bay Irrigation District
- Vallejitos Water District
- Valley Center Municipal Water District
- Vista Irrigation District
- Yuima Municipal Water District
- OTHER REPRESENTATIVE**
- County of San Diego

State of California Department of Finance
Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations
915 L Street, 6th Floor
Sacramento, CA 95814-3706

Re: San Diego County Water Authority Response to Draft Audit Report dated June 6, 2014 on San Diego County Water Authority Proposition 50 and 84 Bond Programs Grant Agreements 4600009346 and 4600008209

Dear Mr. Sierra:

This letter constitutes the San Diego County Water Authority's response to the observations and recommendations contained in the draft report by the Department of Finance (DOF) concerning its compliance audit of the Water Authority's subject grant agreements with the State of California Department of Water Resources. DOF transmitted the draft report via email to Maureen Stapleton, the Water Authority's General Manager on June 6, 2014. As requested in your letter accompanying the draft report, the Water Authority has prepared a written response to each observation and associated recommendations. The written response states the Water Authority's agreement or disagreement with each observation and recommendation along with relevant narrative to support the Water Authority's position.

DOF Observation and Recommendations	Water Authority Response
<p>Observation 1: Unsupported and Unallowable Expenditures Claimed. Two of five local sponsors reviewed claimed unsupported or unallowable expenditures, or did not maintain an adequate audit trail, as noted below.</p>	<p>The Water Authority partially disagrees with this observation.</p> <p>While the Water Authority agrees that Coastkeeper did have some unsupported labor expenditures, the Water Authority disagrees with the DOF calculation of the disallowed amount. In addition, Coastkeeper has documentation to support 100% of the match requirement with volunteer labor hours and a cash grant. See Addendum A.</p>

DOF Observation and Recommendations	Water Authority Response
	<p>The Water Authority agrees that all local project sponsors need to maintain adequate audit trails to support not only required expenditures but also match funding as reflected in the grant agreement.</p>
<p>Recommendations: A. Remit \$305,177 to DWR for unsupported personnel expenditures. DWR will determine the final disposition of the questioned grant costs and the questioned match costs, since the completion date for Project 15 is scheduled for April 1, 2016 (per grant amendment No. 7, executed February 18, 2014).</p>	<p>A. The Water Authority disagrees with this recommendation. Based on corrected information provided by Coastkeeper and submitted as an addendum to this response, the unsupported personnel expenditures claimed is \$37,185.84 rather than the \$305,177 based on a recalculation of the disallowed overhead.</p> <p>DOF auditors communicated that they are disallowing all overhead charges for two main reasons:</p> <ol style="list-style-type: none"> 1) The overhead calculation methodology was not preapproved by DWR as required in the contract. 2) The overhead calculation used by Coastkeeper included errors in the methodology. <p>As to the first reason, when the Water Authority asked DWR whether preapproval of an overhead methodology was necessary for a project in agreement 4600008209, DWR responded that as long as the methodology used is reasonable and auditable, DWR will not object to it. This response is contained in an email correspondence on February 7, 2011 from DWR Research Program Specialist Anna Aljabiry with the subject header "Allowable Overhead." In the email, Ms. Aljabiry wrote, "As long as you can prove that the local agency (city) has a standing practice of x amount for overhead rate, we will accept it. But keep in mind, it has to make sense and you have to be able to prove where your figure came from."</p>

DOF Observation and Recommendations	Water Authority Response
	<p>As to the second reason, the Water Authority agrees that flaws in the overhead methodology ought to be corrected to identify the accurate and reasonable overhead that may be applied to the labor charged to the project. However, the Water Authority disagrees that all overhead should be excluded simply due to errors in the initial calculation. It is patently inequitable to take the position that if an overhead methodology is not accepted as 100% correct, then the appropriate remedy is to allow 0% of the overhead. This “gotcha” reasoning is especially inappropriate with respect to a multi-year project performed reliably and cost-effectively by a small and highly valued non-profit organization such as Coastkeeper. While Coastkeeper’s overhead allocation methodology is complex, it is reasonable.</p> <p>After carefully reviewing the draft audit report and speaking with the DOF auditor, the Water Authority asked Coastkeeper to correct its methodology and report the revised calculation that supports reasonable and allowable overhead costs for the project. Coastkeeper representatives documented actual labor and fringe costs paid to employees and fully documented the associated overhead relative to the paid positions. The fact that Coastkeeper was able to perform and document this recalculation is evidence that Coastkeeper does maintain records that are auditable and traceable.</p> <p>Further background helps to explain this finding and the reason it should be addressed in this manner. Throughout the project term, Coastkeeper operated under the assumption that it was required to bill for labor at the rates identified in Grant Agreement 4600008209, an</p>

DOF Observation and Recommendations	Water Authority Response						
	<p>assumption that was reinforced by the fact that 12 invoices were paid by DWR over the course of three years based on those billing rates. When it was called to Coastkeeper's attention after project completion that expenses should be recalculated for each invoice, according to pay records and a supported overhead rate, Coastkeeper provided data to support not only the overhead calculations, but also actual costs for salary and fringe. The difference between the invoiced labor (billable rate in the agreement) and actual labor, fringe and overhead is as follows:</p> <table data-bbox="803 976 1404 1081"> <tr> <td>Invoiced Labor</td> <td style="text-align: right;">\$499,110.00</td> </tr> <tr> <td>Actual Salary/Fringe/Overhead</td> <td style="text-align: right;"><u>\$461,924.16</u></td> </tr> <tr> <td>Amount overbilled</td> <td style="text-align: right;"><u>\$ 37,185.84</u></td> </tr> </table> <p>Coastkeeper submitted documentation to support the above calculation. See Addendum B</p> <p>Coastkeeper used this same methodology with its IRWM Proposition 84, Round 1 project. The Water Authority shared the methodology with Eduardo Pech, DWR Regional Service Representative for the Proposition 84, Round 1 grant agreement. Mr. Pech, in an email on September 3, 2013, acknowledged that this methodology was reasonable and acceptable for billing, and DWR-authorized payments have been made under Proposition 84 on that basis.</p> <p>The labor calculation encompassed the questioned amount related to the independent contractor line item. The independent contractor provided services to Coastkeeper's entire organization, including hours directly billed to the project. Coastkeeper billed and reported these services in conjunction with the calculation of actual labor rates described above.</p>	Invoiced Labor	\$499,110.00	Actual Salary/Fringe/Overhead	<u>\$461,924.16</u>	Amount overbilled	<u>\$ 37,185.84</u>
Invoiced Labor	\$499,110.00						
Actual Salary/Fringe/Overhead	<u>\$461,924.16</u>						
Amount overbilled	<u>\$ 37,185.84</u>						

DOF Observation and Recommendations	Water Authority Response
	<p>As appropriate, no benefits were provided by the organization to the independent contractor, so no benefit expense is included in this rate. Overhead was allocated since this work was performed in the context of the fully functioning organization. While the organization did not control the time or manner in which the contractor performed his work, the project required that Coastkeeper provide lab and office space, equipment and materials to perform the full scope of assignments and utilities. Note that the cost of this individual is not included in the “contractor” line on the allocable overhead calculation, which includes only expenses of management consultants.</p> <p>The project completion report for this project was submitted to DWR on December 12, 2012 and all deliverables have been met.</p>
<p>B. Ensure local sponsors maintain a clear audit trail for all claimed grant and match expenditures by project and funding source. The audit trail should facilitate the tracing of expenditures claimed on payment requests to the accounting records and source documents.</p>	<p>B. The Water Authority agrees with this recommendation and will conduct random audits to ensure compliance by the local project sponsors with the costs provision described in the grant agreement.</p>
<p>C. Ensure indirect cost rates are well documented and approved in accordance with agreements between the Authority and the local sponsor.</p>	<p>C. The Water Authority agrees with this recommendation and will work with DWR to ensure the Water Authority complies with contractual requirements related to indirect cost allocations as applicable.</p>
<p>D. Ensure all claimed expenditures have been incurred and paid prior to requesting reimbursement from the state.</p>	<p>D. The Water Authority disagrees with this recommendation. To ensure with certainty that all claimed expenditures are incurred and paid prior to requests for reimbursement, the Water Authority would necessarily have to audit each</p>

DOF Observation and Recommendations	Water Authority Response
	<p>invoice from a local project sponsor. This would place an unreasonably heavy administrative burden on the Water Authority and delay timely payment of expenses that had been incurred.</p> <p>The Water Authority will ensure each local project sponsor has adequate internal controls and accounting practices to minimize the risk of a local project sponsor requesting reimbursement for expenses that have not been incurred and paid. However, the Water Authority cannot eliminate all risk of false reporting. To limit the risk, the Water Authority must rely on each local project sponsor's professionalism, internal controls, and billing certification that costs submitted are incurred for the project every time reimbursement requests are submitted. The Water Authority will conduct random audits to identify potential discrepancies in proper reporting.</p>
<p>Observation 2: Oversight of Grant Deliverables Needs Improvement Two of five projects reviewed deviated from the grant's scope of work without obtaining prior written approval.</p>	<p>The Water Authority partially disagrees with this observation.</p> <p>Although the County of San Diego reported to DWR on numerous occasions, via progress reports and PAEP reports, about the deviations in its deliverables for Project 19, a written approval for the change was not obtained. The County of San Diego's project has since been completed and the project's Completion Report has been submitted to and accepted by the Department of Water Resources. This completion report includes the final scope of the project consistent with DOF observation.</p> <p>Coastkeeper's Project 15 website was offline during the audit visit to San Diego in February 2013, at a time when Coastkeeper had completed all project deliverables and the</p>

DOF Observation and Recommendations	Water Authority Response
	<p>project completion report had been submitted. The website was subsequently placed back online in support of a related Coastkeeper project funded by a Prop 84 Round 1 grant. The website may be viewed at http://www.sdcoastkeeper.org/quick-links/water-monitoring.html.</p>
<p>Recommendations: A. For future project scope changes, obtain written approval from the grantor before making any changes to the grant's scope of work. For significant scope changes, review the project budget to determine if a budget modification is warranted.</p>	<p>A. The Water Authority agrees with this recommendation. The following response describes the process the Water Authority has used since December 2010 to process all requested scope changes from a local project sponsor.</p> <p>All requested changes to the project are administered through an agreement amendment process that requires written approval from DWR.</p> <p>A local project sponsor must notify the Water Authority of any proposed changes to its agreement with the Water Authority. The local project sponsor is required to submit an agreement amendment form to the Water Authority detailing the recommended change, justification for the modification and any ways in which the change may affect the project's Project Assessment Evaluation Plan (PAEP).</p> <p>Once notified by the local project sponsor, the Water Authority carefully reviews the requested change and coordinates with the local project sponsor regarding any potential issues that may result from the proposed revision and to determine if the change is justified. When a significant scope change is proposed, the Water Authority and the local project sponsor review the project budget to determine if any budget revisions are necessary.</p>

DOF Observation and Recommendations	Water Authority Response
	<p>The Water Authority notifies DWR of amendment requests in writing. There are two types of amendment procedures: informal and formal. The informal process, for minor changes to the contract, is handled by an exchange of emails between the Water Authority and the DWR Regional Service Representative (RSR), with DWR approval coming via an email.</p> <p>The formal process is for major changes usually related to the scope, budget category changes or schedule revisions that will affect the completion of the grant agreement term. Formal amendments are handled via a written request from the Water Authority to the RSR to amend the grant contract. The letter includes the project details, justification and any impacts to the PAEP. Once the amendment is approved by DWR, the RSR processes a formal agreement amendment document that is signed and executed by both DWR and the Water Authority. Once the grant agreement amendment is executed, the local project sponsor and the Water Authority execute an amendment to the local project sponsor agreement.</p>
<p>B. Develop and implement oversight procedures to ensure that deliverables are completed as required in the grant agreement.</p>	<p>B. The Water Authority agrees with this recommendation. The following response describes the processes the Water Authority uses to ensure all deliverables are completed as required in the grant agreement.</p> <p>Since the Water Authority began administering its IRWM Prop 84 Round 1 Implementation grant in 2012, the Water Authority has followed procedures to ensure required project deliverables are completed and submitted in accordance with its grant agreement with DWR. The Water Authority developed a Deliverables</p>

DOF Observation and Recommendations	Water Authority Response
	<p>Master List containing required submittals or deliverables for each project. A section for deliverables is incorporated into the local project sponsor's quarterly progress report template to ensure submitted deliverables are reported. The Water Authority cross-references items listed in this section against the Deliverables Master List to ensure submittals are tracked and documented. Together with the Completion Report checklist, this list is used to ensure all required deliverables are completed and submitted to DWR.</p> <p>The Water Authority will use the same procedures with all of its Prop 84 grant awards and will apply these procedures to its Prop 50 grant. With the Prop 50 grant, the Water Authority has in place a completion checklist that is used when reviewing required project deliverables from a local project sponsor before closing out a project.</p> <p>In addition, to ensure that work is progressing and project goals are being met, the local project sponsor must report on budget or task categories in its quarterly progress reports for all grants. Local project sponsors must report periodically on progress made in each of the categories to explain activity status, including project issues, delays and concerns. This internal reporting control assists in tracking of progress made on each project and ensures project goals and deliverables are progressing, as scheduled.</p> <p>The Water Authority holds meetings with local project sponsors at least once per year to communicate about various project and administrative issues. These meetings also serve as an open platform during which local project sponsors may discuss potential project issues.</p>

DOF Observation and Recommendations	Water Authority Response
	Separate meetings are held for local project sponsors in each grant.

The Water Authority coordinated closely with Coastkeeper to prepare this response. Where applicable to Coastkeeper, this response reflects the joint comments of both parties. Representatives from both the Water Authority and Coastkeeper are prepared to meet with you and your staff to further discuss the report and these responses. We appreciate the assistance and cooperation that your staff has provided during this grant compliance audit. If you require further information from the Water Authority or would like to schedule a meeting, please contact Mark Stadler at mstadler@sdewa.org or Rod Greek at rgreek@sdewa.org.

Sincerely,

original signed by

Mark Stadler
Principal Water Resource Specialist
San Diego IRWM Program Manager

original signed by

Rodney J. Greek
Controller
San Diego County Water Authority

Enclosure: Addendum A – Prop 50 Audit Findings Match
Addendum B – San Diego Coast Keeper, (2) Explanation of calculations

cc: Maureen A. Stapleton, General Manager
Dan Hentschke, General Counsel
Sandra Kerl, Deputy General Manager
Lisa Marie Harris, Director of Finance/Treasurer
Ken Weinberg, Director of Water Resources
Dana Frieauf, Principal Water Resource Specialist

EVALUATION OF RESPONSE

The San Diego County Water Authority's (Authority) June 30, 2014 response to the draft audit report has been reviewed and incorporated into the final report. The Authority partially disagreed with Observations 1 and 2. The Authority provided additional information including a revised indirect cost allocation methodology, a list of volunteer names and hours for in-kind match, and documentation for cash match (not previously claimed). The additional information is omitted herein for brevity. We acknowledge the Authority's willingness to implement several corrective actions.

We reviewed the information submitted and provide the following comments:

Observation 1: Unsupported and Unallowable Expenditures Claimed

The Authority is requesting questioned personnel costs be reduced to \$37,186 based on a revised indirect cost (overhead) allocation methodology. Since February 2013 (original audit field visit), the Authority has been unable to provide adequate documentation. The Authority was provided a second opportunity to present documentation during a subsequent audit field visit in July 2013; however, our review found several errors in the methodology provided. The Authority has submitted a revised version in response to the draft audit report; however, the information provided did not include the source documents required to substantiate the revised methodology. Moreover, cost allocation plans should be developed prior to accepting a grant award and should not be developed after-the-fact.

The Authority also submitted documentation for questioned in-kind match and claimed new cash match funding; however, the documentation was insufficient to support the match funding claimed. The observation and recommendations remain unchanged.

Observation 2: Oversight of Grant Deliverables Needs Improvement

The Authority partially disagrees with this observation, noting that grant scope changes were reported in progress and other reports. However, the Authority agreed with the recommendation to obtain formal written approval from the California Department of Water Resources before making any changes to the grant's scope of work. We appreciate the Authority's willingness to implement the recommendation. The observation and recommendations remain unchanged.