



SOUTHERN CALIFORNIA  
ASSOCIATION OF GOVERNMENTS  
900 Wilshire Blvd., Ste. 1700  
Los Angeles, CA 90017  
T: (213) 236-1800  
www.scag.ca.gov

#### REGIONAL COUNCIL OFFICERS

President  
Margaret E. Finlay, Duarte

First Vice President  
Alan D. Wapner, Ontario

Second Vice President  
Bill Jahn, Big Bear Lake

Immediate Past President  
Michele Martinez, Santa Ana

#### COMMITTEE CHAIRS

Executive/Administration  
Margaret E. Finlay, Duarte

Community, Economic &  
Human Development  
Rex Richardson, Long Beach

Energy & Environment  
Carmen Ramirez, Oxnard

Transportation  
Curt Hagman, San Bernardino County

## MEETING OF THE

# AUDIT COMMITTEE

*Tuesday, March 20, 2018*  
*2:30 p.m. – 4:00 p.m.*

#### PLEASE NOTE NEW ADDRESS

SCAG MAIN OFFICE  
900 Wilshire Blvd., Ste. 1700  
Policy Room A  
Los Angeles, CA 90017  
(213) 236-1800

#### TELECONFERENCE AND VIDEOCONFERENCE WILL BE AVAILABLE

If members of the public wish to review the attachments or have any questions on any of the agenda items, please contact Carmen Summers at (213) 236-1984 or via email at [summers@scag.ca.gov](mailto:summers@scag.ca.gov). Agendas & Minutes for the Audit Committee are also available at: [www.scag.ca.gov/committees](http://www.scag.ca.gov/committees)

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## Audit Committee Members and Other Meeting Locations

Date: Tuesday, March 20, 2018

Time: 2:30PM – 4PM

Location: SCAG Main Office

900 Wilshire, Suite 1700 – Policy Room A

Los Angeles, CA 90017

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### LIST OF MEMBERS

1. **Hon. Bill Jahn, CHAIR**  
*City of Big Bear Lake, District 11*
2. **Hon. Margaret Finlay**  
*City of Duarte, District 35*
3. **Hon. Alan Wapner**  
*City of Ontario, SBCTA*
4. **Hon. Michele Martinez**  
*City of Santa Ana, District 16*
5. **Hon. Glen Becerra**  
*City of Simi Valley, District 46*
6. **Hon. Joe Buscaino**  
*City of Los Angeles, District 62*
7. **Hon. Jeff Giba**  
*City of Moreno Valley, District 69*
8. **Hon. Ray Marquez**  
*City of Chino Hills, District 10*
9. **Hon. Greg Pettis**  
*Cathedral City, District 2*
10. **Hon. Cheryl Viegas Walker, VICE CHAIR**  
*City of El Centro, District 1*
11. **Hon. Edward H. J. Wilson**  
*City of Signal Hill, Gateway Cities COG*

### TELECONFERENCE / MEETING LOCATIONS

- SCAG Main Office**  
900 Wilshire, Suite 1700  
Los Angeles, CA 90017
- Grand Hyatt  
1000 H Street NW  
Washington, D.C. 20001
- 1212 S. Parton Street  
Santa Ana, CA 92707
- Los Angeles Metro  
One Gateway Plaza  
Los Angeles, CA 90012
- SCAG Riverside Office  
3403 10th Street, Suite 805  
Riverside, CA 92501
- Chino Hills Government Center  
14000 City Center Drive, 2nd Floor  
City Council Office  
Chino Hills, CA 91709
- City Hall  
68-700 Avenida Lalo Guerrero  
Cathedral City, CA 92234
- 290 13th Street, Apt. 3  
Brooklyn, NY 11215



**AUDIT COMMITTEE TELECONFERENCE INFORMATION**  
**Pursuant to Government Code Section §54954**

**INSTRUCTIONS REGARDING TELECONFERENCE**

**TELECONFERENCE NUMBER PROVIDED UNDER SEPARATE COVER**

**For Brown Act Requirements, please ensure that your agenda is posted at your teleconference location.**

**If you have any questions, please call:  
Carmen Summers at (213) 236-1984**

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## AUDIT COMMITTEE AGENDA

Southern California Association of Governments

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900 Wilshire Boulevard, Suite 1700  
Los Angeles, California 90017  
**Tuesday, March 20, 2018**  
**2:30 p.m. to 4:00 p.m.**

*The Audit Committee may consider and act upon any of the items listed on the agenda regardless of whether they are listed as Information or Action Items.*

### **CALL TO ORDER AND PLEDGE OF ALLEGIANCE**

*(The Honorable Bill Jahn, Chair)*

### **ROLL CALL**

### **PUBLIC COMMENT PERIOD**

Members of the public desiring to speak on items on the agenda, or items not on the agenda, but within the purview of the Committee, must fill out and present a Public Comment Card to the committee staff prior to speaking. Comments will be limited to three (3) minutes per speaker. The Chair has the discretion to reduce the time limit based upon the number of speakers and may limit the total time for all public comments to twenty (20) minutes.

### **REVIEW AND PRIORITIZE AGENDA ITEMS**

### **CONSENT CALENDAR**

**Time**

**Page No.**

#### **Approval Item**

- |  |  |          |
|--|--|----------|
| 1. <u>Minutes of the November 14, 2017 Meeting</u> |  | <b>1</b> |
|--|--|----------|

### **ACTION/DISCUSSION ITEM**

- |   |                |          |
|---|----------------|----------|
| 2. <u>Internal Audit Charter</u><br><i>(Joshua Margraf, Internal Auditor)</i> | <b>10 mins</b> | <b>7</b> |
|---|----------------|----------|

**Recommended Action:** Approve SCAG' updated Internal Audit Charter for the internal audit function.

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<u>INFORMATION ITEMS</u>	<u>Time</u>	<u>Page No.</u>
3. <u>Fiscal Year (FY) 2017-18 External Auditor Update</u> <i>(Joshua Margraf, Internal Auditor)</i>	35 mins.	13
4. <u>Internal Audit Status Report</u> <i>(Joshua Margraf, Internal Auditor)</i>	30 mins.	23
5. <u>Hotline Update</u> <i>(Joshua Margraf, Internal Auditor)</i>	10 mins.	29

FUTURE AGENDA ITEM/S

ANNOUNCEMENT/S

ADJOURNMENT

*The next regular meeting of the Audit Committee is scheduled for Tuesday, June 12, 2018, at the Wilshire Grand Center, 900 Wilshire Boulevard, Suite 1700, Los Angeles, CA 90017.*

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Audit Committee  
**of the**  
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**THE FOLLOWING MINUTES ARE A SUMMARY OF ACTIONS TAKEN BY THE AUDIT COMMITTEE. AN AUDIO OF THE ACTUAL MEETING IS AVAILABLE FOR LISTENING IN SCAG'S OFFICE.**

The Audit Committee held its meeting at the SCAG offices in downtown Los Angeles.

**Members Present**

Hon. Bill Jahn, Big Bear Lake, (**Chair**)  
Hon. Margaret Finlay, Duarte  
  
Hon. Glen Becerra, Simi Valley  
Hon. Michele Martinez, Santa Ana  
  
Hon. Ray Marquez, Chino Hills  
Hon. Greg Pettis, Cathedral City  
Hon. Cheryl Viegas-Walker, El Centro  
**(Vice-Chair)**  
Hon. Edward H. J. Wilson, Signal Hill

**Representing**

District 11, 2<sup>nd</sup> Vice President  
District 35, SCAG President  
(Via Teleconference)  
District 46 (Via Teleconference)  
District 16, SCAG Imm. Past President  
(Via Teleconference)  
District 10 (Via Teleconference)  
District 2 (Via Teleconference)  
District 1, SCAG (Via Teleconference)  
  
Gateway Cities COG  
(Via Teleconference)

**Members Not Present**

Hon. Alan Wapner, Ontario  
Hon. Joe Buscaino, Los Angeles  
Hon. Jeff Giba, Moreno Valley

SBCTA/SBCOG, 1<sup>st</sup> Vice-President  
District 62  
District 69

**CALL TO ORDER & PLEDGE OF ALLEGIANCE**

Hon. Bill Jahn, Chair, called the meeting to order at 2:37 p.m. and asked Councilmember and SCAG President, Margaret Finlay to lead in the Pledge of Allegiance.

**ROLL CALL**

A formal roll call was taken and it was determined that a quorum was not present.

**PUBLIC COMMENT PERIOD**

None.

**REVIEW and PRIORITIZE AGENDA ITEMS**

Due to the absence of a quorum at the start of the meeting, the FY 2016-17 Preliminary External Financial Update was presented until a quorum was reached. A quorum was established at 2:46 p.m., at which time the Audit Committee considered the remaining agenda items for action.

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In addition, as requested by the Committee, staff will poll and communicate with the Audit Committee (AC) members to determine if there is still committed interest to participate at the meetings.

**CONSENT CALENDAR**

**Approval Items**

1. Minutes of the September 12, 2017 Meeting
2. 2018 Proposed Meeting Schedule

A MOTION was made (Viegas-Walker) and SECONDED (Finlay) to approve the Consent Calendar Approval Items. The motion was passed by the following roll call vote:

AYES: Jahn, Finlay, Becerra, Marquez, Martinez, Pettis, Viegas-Walker and Wilson (8).  
NOES: None (0).  
ABSTAIN: None (0).

**ACTION ITEMS**

3. Internal Audit Charter Update

Joshua Margraf, Internal Auditor, provided a brief summary and background information on the Internal Audit Charter, which identifies the internal audit function's authority and responsibilities. He noted that his recommendation to the Committee would be to review the Internal Audit Charter and provide input before the next Audit Committee meeting. At the next AC meeting, the item can be placed on the agenda for approval.

Councilmember Viegas-Walker asked if there are other departments with stand-alone policies and procedures within SCAG's uniformed system. Darin Chidsey, COO, responded that the Internal Audit function has a specific role, whereas other departments have objectives that are adhered to. As such, other departments do not have stand-alone policies and procedures.

An Information item. No Action or Motion was taken.

4. Ethics Policy Update

Joshua Margraf, Internal Auditor, discussed briefly the process for updating the Ethics Policy. He turned the discussion over to Darin Chidsey, COO, to provide highlights of the report.

Mr. Chidsey commented that the Ethics Policy has been updated to reflect current practices and procedures as recommended by the Committee. He noted that the procedures outline specific



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steps, with the intent to offer separation between fraud, waste, and abuse complaints from harassment-related and non-fraudulent complaints. Also, SCAG is developing a more comprehensive set of procedures for defined roles and responsibilities throughout the receipt of complaints via the Ethics Hotline report through close out.

Mr. Chidsey thanked staff for their vital input in implementing the updated policies and procedures set forth in the Ethics Policy in order for the Committee to adopt and forward them to the Regional Council for approval.

Staff responded on the comments and questions expressed by the Committee members, including that clarification be made and updated on how ethical complaints and investigations are handled if filed against Legal, Internal Audit or Human Resources, and, the reporting procedures for investigations that may involve the Executive Director, as highlighted in the Ethics Policy, section 12 (C).

Darin Chidsey, COO, responded that the reporting procedures for the Executive Director are consistent with the Bylaws, being that the President and Officers would be notified before an investigation started, but that verification would be done by procedures in the Ethics Policy, and/or applicable changes made, if needed, to the Ethics Policy.

Mr. Chidsey stated that staff is currently reviewing all of SCAG's policies and procedures, with the next review being the Regional Council Policy Manual.

Hasan Ikhata, Executive Director, reiterated that because the Ethics Hotline allows for the submission of personnel complaints and/or personnel issues, the updated Ethics Policy incorporates specific steps to separate those issues from fraud, waste and abuse-related issues.

In conclusion, staff commented that the Ethics Hotline was created in 2009 as an effective best practice for the agency. The cost to subscribe to have the Ethics Hotline managed by an independent third-party is fairly low. Staff requested that the Committee review SCAG's updated Ethics Policy for adoption prior to forwarding to the Regional Council for approval.

A MOTION was made (Finlay) and SECONDED (Becerra) to approve staff's recommendation, and allow for any additional necessary modifications to the updated Ethics Policy to ensure better alignment with SCAG policies and procedures. The motion was passed by the following roll call vote:

AYES: Jahn, Finlay, Becerra, Marquez, Martinez, Pettis, Viegas-Walker and Wilson (8).  
NOES: None (0).  
ABSTAIN: None (0).

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**INFORMATION ITEMS**

5. FY 2016-17 Preliminary External Financial Update

Joshua Margraf, Internal Auditor, introduced Roger Alfaro, Partner, Varinek, Trine, Day and Company, LLP (VTD), SCAG's outside independent auditors who presented the FY 2016-17 preliminary audit report. The audit scope, key areas of emphasis and responsibility, the summary of audit results, the planning and risk assessment performed, financial statement highlights, internal control structure, and the year-end fieldwork and testing were presented in detail.

Mr. Alfaro reported that SCAG would receive a report on the Internal Controls and an Unmodified Opinion for its FY 2016-17 financial statements (CAFR), Single Audit and Compliance Report later in the month of December, 2018.

The Committee thanked the audit team for a thorough audit presentation.

6. Service Review of Extended Warranties and Software Agreements

Joshua Margraf, Internal Auditor, provided a brief summary of his review of SCAG's extended warranties and software agreements. He noted that SCAG lacks clear guidance on how to manage extended warranties and software agreements; and as SCAG moves forward with updating its policies and procedures, it should consider ways to address documentation of costs associated with extended warranties and software agreements, so as to allow for identification of overall costs, as well as inclusion of a written process that provides clarity regarding roles and responsibilities for tracking costs.

Discussion ensued, Hon. Viegas-Walker requested staff to ensure that the agency implement standards whereby there is better integration and training between the project management group and the contract department.

Debbie Dillon, Deputy Executive Director, commented that management's highest priority is focused on improving and updating the policies and procedures across the agency, including addressing its project management and procurement policies. She noted that staff will report to the Committee as to progress made on reports highlighted by internal audit.

7. Internal Audit Status Report

Joshua Margraf, Internal Auditor, provided a brief overview of the Internal Audit Status Report which also included updates of the agenda items presented on the agenda today. He asked the Committee to identify any additional risks that Internal Audit might review.

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Audit Committee  
**of the**  
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**FUTURE AGENDA ITEMS**

There were no future agenda items requested.

**ANNOUNCEMENTS**

There were no announcements given.

**ADJOURNMENT**

*Hon. Bill Jahn, Chair, adjourned the meeting at 3:41 p.m. The next meeting of the Audit Committee will be held on Tuesday, March 20, 2018 at 2:30 p.m.*

**Minutes Approved by:**  
Joshua Margraf, Internal Auditor

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Southern California Association of Governments  
900 Wilshire Blvd., Suite 1700, Los Angeles, CA 90017

**Agenda Item No. 2**  
**March 20, 2018**

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**To:** Audit Committee (AC)

**From:** Josh Margraf, Internal Auditor, (213) 236-1890,  
margraf@scag.ca.gov

**Subject:** Internal Audit Charter Update

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**RECOMMENDED ACTION:**

Approve SCAG' updated Internal Audit Charter for the internal audit function.

**EXECUTIVE SUMMARY:**

***The Internal Audit Charter has been updated as per audit standards to reflect current work of the internal audit function.***

**STRATEGIC PLAN:**

This item supports SCAG's Strategic Plan Goal 7B: Maximize Efficiency and Effectiveness in Resource Allocation to Maintain Adequate Working Capital, Appropriate Reserves, and Investments, and Utilize Resources in a Timely and Responsible Fashion.

**BACKGROUND:**

Internal Audit has reviewed and updated the *Internal Audit Charter* (attachment 1) in November 2017. The charter is to identify the internal audit function's authority and responsibilities.

The *Internal Audit Charter* establishes the internal audit function's position within SCAG, to include reporting relationships with the Audit Committee and management. In addition, the *Internal Audit Charter* authorizes access to records, personnel, and properties relevant to the performance of audit engagements. Internal auditing standards state that the internal audit charter should be reviewed periodically.<sup>1</sup> This helps ensure the charter reflects the current purpose and responsibilities of the internal audit function, and that they are suitable documented. The updates reflect both the current version of U.S. Generally Accepted Government Auditing Standards (GAGAS) as well as current internal auditing standards.<sup>2</sup> SCAG last updated the *Internal Audit Charter* in 2002.

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<sup>1</sup>Institute of Internal Auditors (IIA), *International Standards for the Professional Practice of Internal Auditing (Standards)* (Jan. 2017), and ISACA, *Information Systems (IS) Audit and Assurance Standards* (Nov. 2013).

<sup>2</sup>GAO, *Government Auditing Standards 2011 Revision*, GAO-12-331G, (Dec. 2011), and (IIA) *International Standards for the Professional Practice of Internal Auditing (Standards)* (Jan. 2017). Updates to GAGAS are currently being reviewed by the U.S. Government Accountability Office (GAO) and have not been finalized. As the updates are finalized, Internal Audit will review them to determine the extent to which they affect SCAG's *Internal Audit Charter*.

**CONCLUSION:**

The *Internal Audit Charter* has not been updated in approximately 16 years. It should be reviewed, updated, and approved as necessary.

**RECOMMENDATION:**

The Audit Committee should approve the *Internal Audit Charter*.

**FISCAL IMPACT:**

None

**ATTACHMENT:**

Internal Audit Charter

## SCAG INTERNAL AUDIT CHARTER

### INTRODUCTION

Internal auditing is an independent and objective assurance and consulting activity that is guided by a philosophy of adding value to improve operations. It assists in accomplishing an organization's objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of the organization's governance, risk management, internal control.

### POLICY

The Southern California Association of Governments (SCAG) will provide and support an internal audit function to perform independent assessments of SCAG operations, including evaluations of the effectiveness and efficiency of various departments and functions and evaluating governance, risk management, and essential internal controls.

### OBJECTIVE

The internal audit function will assist all members of management in efficient and effective discharge of responsibilities by providing independent analyses, appraisals, findings, and recommendations.

### PROFESSIONALISM

The internal audit function will adhere to U.S. Generally Accepted Government Auditing Standards (GAGAS) as issued by the Government Accountability Office as well as consult other professional internal audit standards as promulgated by Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*. In cases where requirements from one set of standards are more restrictive, the internal audit function will conform to those that are more restrictive. If complete conformance with GAGAS is not feasible, the internal audit function will document such as part of its audit work.

### AUTHORITY

The internal audit function derives its authority from the Regional Council, Executive Director and Chief Operating Officer (COO), and is authorized to conduct engagements of any department system or function as necessary to accomplish its objectives. The internal audit function, with strict accountability for confidentiality and safeguarding records and information, is authorized full, free, and unrestricted access to any and all of SCAG records, physical properties, and personnel pertinent to carrying out any engagement.

The internal audit function is charged with the responsibility to perform independent assessments of fiscal, operational, and administrative systems. However, services of the internal audit function are a staff function; the position has neither authority over, nor responsibility for, any activities audited or reviewed.

### ORGANIZATION

The internal audit function will report functionally to the Regional Council and administratively (i.e. day to day operations) to the COO.

The Regional Council provides oversight of the internal audit function through its Audit Committee. As part of its responsibilities, the Audit Committee will:

- Review the charter, plans, activities, staffing, and organizational structure of the internal audit function.
- Review and approve the internal audit function's annual workplan, including the nature and scope of the audits scheduled for the fiscal year.
- Receive and review draft internal audit reports.
- Ensure no unjustified restrictions or limitations, and review and concur in the appointment, replacement, or dismissal of the internal auditor.
- Meet separately with the internal audit function on an as-needed basis to discuss any matters that the Audit Committee or internal audit believes should be discussed privately.

### **INDEPENDENCE AND OBJECTIVITY**

The internal audit function will remain free from interference by any element in the organization, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of a necessary independent and objective mental attitude.

The internal audit function will have no direct operational responsibility or authority over any of the activities audited. Accordingly, they will not implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that may impair internal auditor's judgment. In cases where the internal audit function is requested to assist in any activities or processes that could impact independence and objectivity, in appearance or in actuality, the audit function will indicate such.

The internal audit function will exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. The internal audit function will make a balanced assessment of all relevant circumstances and not be unduly influenced by own interests or by others in forming judgments.

The internal audit function will confirm to the Audit Committee, at least annually, its organizational independence.

### **INTERNAL AUDIT PLAN**

The internal audit function will develop and internal audit plan based on a prioritization of the audit universe using a risk-based methodology, including input of senior management and the Audit Committee.

### **RESPONSIBILITY**

The scope of internal auditing encompasses, but is not limited to, the examination and evaluation of the adequacy and effectiveness of SCAG's governance, risk management, and internal controls as well as the quality of performance in carrying out assigned responsibilities to achieve the SCAG's stated goals and objectives.



- Develop a flexible annual audit plan, including any risks or control concerns identified by management or the Audit Committee.
- Determine compliance with SCAG fiscal policies and regulations regarding revenue, expenses, budgets, contracts, lease compliance, subregions, projects and programs.
- Evaluate the efficiency, effectiveness and economy of SCAG operations, including the safeguard of SCAG assets.
- Provide the Audit Committee with timely reports of audit findings, analyses, and recommendations designed to strengthen and improve internal control and performance results.
- Perform special assignments as directed by the Regional Council, Executive Director, or Chief Operating Officer.
- Direct, manage, plan and perform internal audits including operational, compliance, and financial audits of all SCAG activities.
- Prepare audit plans for internal audits; conduct appropriate follow-up research, prepare analysis and work papers to document audit work product and write audit reports.
- Participate in the development and implementation of new or revised SCAG audit programs, systems, procedures and methods of operation.
- Report all cases of actual or suspected loss, theft, misappropriation or misuse of Association monies or property immediately to the Chief Counsel and Chief Operating Officer.
- Review and coordinate any requests by outside agencies to conduct audits, which includes, but not necessarily limited to, federal, state, county, or others with a contractual right to audit.

END OF CHARTER

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Southern California Association of Governments  
900 Wilshire Blvd., Suite 1700, Los Angeles, CA 90017

**Agenda Item No. 3**  
**March 20, 2018**

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**To:** Audit Committee (AC)

**From:** Josh Margraf, Internal Auditor, (213) 236-1890,  
margraf@scag.ca.gov

**Subject:** Fiscal Year (FY) 2017-18 External Financial Audit

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**RECOMMENDED ACTION:**

For Information Only - No Action

**EXECUTIVE SUMMARY:**

*SCAG's external financial auditor will present its proposed FY 2017-18 audit plan and receive the Audit Committee's input.*

**STRATEGIC PLAN:**

This item supports SCAG's Strategic Plan Goal 7B: Maximize Efficiency and Effectiveness in Resource Allocation to Maintain Adequate Working Capital, Appropriate Reserves, and Investments, and Utilize Resources in a Timely and Responsible Fashion.

**BACKGROUND:**

SCAG's external independent financial auditors, Vavrinek, Trine, Day, and Company, LLP (VTD), will commence their preliminary work soon for the audit of SCAG's FY 2017-18 financial statements. They will present and discuss their proposed audit plan and receive input as well as answer questions from the Committee.

**FISCAL IMPACT:**

None

**ATTACHMENT:**

VTD Audit Presentation



# Southern California Association of Governments

AUDIT COMMUNICATIONS

# Audit Scope and Timing

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Perform the audit of the:

- Comprehensive Annual Financial Report (CAFR)
- OMB Uniform Grant Guidance – Single Audit

Timeline:

- Planning and Interim Fieldwork – April
- Final Fieldwork – September/October
- Report Delivery – November/December

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## Our Responsibility

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U.S. Generally Accepted Auditing Standards and *Government Auditing Standards*

Express opinions about whether the financial statements that have been prepared by management are presented fairly, in all material respects, in conformity with generally accepted accounting principles

- Reasonable, not absolute assurance
- Audit does not relieve the management of its responsibilities

For Single Audit, express an opinion on compliance applicable to major federal programs

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## Our Responsibility

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Our audit will include obtaining an understanding of the entity and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing and extent of further audit procedures –

- Material misstatements may result from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or regulations that are attributable to the entity or to acts by management or employees acting on behalf of the entity
- No opinion on internal control will be expressed

# Our Responsibility

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Communicate other matters:

- Qualitative aspects of accounting policies, accounting estimates and note disclosures
- Difficulties encountered
- Uncorrected misstatements
- Material corrected misstatements
- Disagreements with management
- Management representations
- Consultations with other accountants



# Our Approach

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## Planning and Risk Assessment:

- Meet with Management
- Obtain an understanding of the entity, its environment and risks
- Identify audit risk areas
- Inspect financial and other information
- Consider/inquire regarding fraud risks
- Understand the design and implementation of internal control
- Prepare risk assessment and audit plan
- Test key business cycles – revenue, disbursements, payroll, investments, capital assets, financial reporting, IT and budget

# Our Approach

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## Final:

- Address key audit areas
- Perform tests, on a sample basis, on account balances and classes of transactions
- Prepare draft CAFR
- Test journal entries
- Assess accounting principles used and significant estimates
- Confirm contingencies with legal counsel
- Consider subsequent events

## Exit:

- Propose / discuss audit adjustments
- Present findings and recommendations
- Provide required communications to those charged with governance

# Questions

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Contact information  
Roger Alfaro, Partner  
[ralfaro@vtdcpa.com](mailto:ralfaro@vtdcpa.com)  
909-466-4410

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Southern California Association of Governments  
 900 Wilshire Blvd., Suite 1700, Los Angeles, CA 90017

**Agenda Item No. 4**  
**March 20, 2018**

**To:** Audit Committee (AC)

**From:** Josh Margraf, Internal Auditor, (213) 236-1890,  
[margraf@scag.ca.gov](mailto:margraf@scag.ca.gov)

**Subject:** Internal Audit Status Report

**RECOMMENDED ACTION:**

For Information Only – No Action Required

**EXECUTIVE SUMMARY:**

*The Internal Auditor will describe work performed since the last Audit Committee meeting.*

**STRATEGIC PLAN:**

This item supports SCAG’s Strategic Plan Goal 7B: Maximize Efficiency and Effectiveness in Resource Allocation to Maintain Adequate Working Capital, Appropriate Reserves, and Investments, and Utilize Resources in a Timely and Responsible Fashion.

**BACKGROUND:**

Since the last Audit Committee meeting in November 2017, Internal Audit has assisted the Contracts Department with preaward reviews, monitored the Ethics Hotline, followed-up on prior recommendations, and started gathering information for a risk assessment.

*A. Preaward Reviews*

Internal Audit performed the following preaward reviews.

<u>Consultant (Contract Number)</u>	<u>Proposal Amount</u>	<u>Questioned Costs</u>	<u>Questioned Costs Sustained</u>
AECOM (18-001-B02)	\$253,691	\$12,507	\$12,507
The Arroyo Group (18-001-B08)	\$192,999	\$17,113	\$17,113
KTUA (18-001-B54)	\$99,861	-0-	-0-
Civilian, Inc. (18-004-C01) <sup>a</sup>	\$1,439,478	\$14,538	-0-
Global Green (18-006-C01)	\$800,495	\$3,704	\$3,704
<b>Totals</b>	<b>\$2,786,524</b>	<b>\$47,862</b>	<b>\$33,324</b>

<sup>a</sup>The consultant’s proposal was under-stated due to addition errors. Questioned costs are the result of corrections to proposed labor amounts (payroll support showed actual labor rates to be less than the proposal rates). When correcting for the calculation errors, and applying the questioned costs to the correct amount, the proposal amount was still significantly under-stated.

Internal Audit also provided assistance to the Contracts department by reviewing consultant information for various proposals.<sup>1</sup> This included procedures for verifying direct labor rates as well as indirect rates and other direct costs.

*B. Preaward Update*

While performing preaward reviews, Internal Audit has noticed potential areas that may help improve the proposal review and selection process.<sup>2</sup> For instance, the line item budgets that support proposals' overall cost estimates have contained noticeable calculation errors as well as information that has not corresponded to the overall proposal narrative. In addition, support for subconsultant costs has occasionally been inconsistent with the line item budgets. Below is additional information on these areas.

- Line Item Budget Calculation Errors

In some winning proposals, the line item budgets contained recognizable calculation errors that under-stated overall proposal amounts. In one instance, the consultant did not correctly multiply proposed labor rates (for staff listed in the line item budget) by proposed labor hours. On other occasions, the consultant incorrectly applied indirect rates (e.g. overhead and fringe rates) to overall direct labor amounts. For example, by not correctly applying indirect rates, one consultant understated its proposal by approximately \$25,600. The consultant indicated that it could still perform the work for the original proposal amount, but reduced total hours by approximately 21 percent. It is unclear how the same scope of work would be performed with substantially less hours.

- Line Item Budgets Not Always Corresponding to Proposal

In some winning proposals, the line budget included staff with no corresponding labor hours. For example, one consultant included multiple positions with no associated hours and different hourly rates. There was no discussion about whether and how these individuals would perform on the scope of work. This can call into question how solid a consultant's requirements are with regard to performing planned work at the time of proposal selection (e.g. who will ultimately perform work described in the proposal, and/or how the overall cost will be impacted given that rates associated with "no hours" staff differ from those positions described in the proposal and have hours listed).

- Line Item Budget Inconsistent with Subconsultant Support

In some winning proposals, support provided by subconsultants does not correspond to the line item budget. In a few instances, subconsultants could not clearly show how they developed costs (e.g. direct labor and indirect rates). For example, one subconsultant could not provide any support for indirect rates because its staff were actually contractors. Since the labor consisted of contractors, the subconsultant did not have a relevant way to develop indirect rates. The subconsultant indicated that it planned to convert the contractors to full time employees if the proposal won. Without clear documentation showing how cost estimates had

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<sup>1</sup>These included RFP 18-001-B14, RFP 18-001-B22, and RFP 18-001-B28.

<sup>2</sup>Internal Audit has not performed a review on the current proposal review and selection process. Typically preaward reviews are performed on consultant proposals that SCAG has selected based on a review of those submitted in response to a request for proposal. Contracts staff can request a preaward review prior to awarding a contract based on the winning proposal.

been developed, it is difficult to determine whether they are fair and reasonable and based on actual costs.

The areas mentioned above demonstrate the importance of preaward reviews, but also show the need for scrutiny of proposals during the proposal review and selection process as many contracts do not undergo a preaward review. It is unclear the extent to which line item budgets are reviewed as part of the current process (to include a basic review of calculations and how hours and staff are allocated across tasks as well as correspond to the narrative). Providing guidance on what to look for when reviewing and selecting proposals, particularly with regard to the line item budget, may help mitigate some risks that proposals are awarded with incorrect or incomplete information, and thus alleviate the need for potential contract amendments.<sup>3</sup>

SCAG is currently in the process of developing and updating policies and procedures for project management, which may provide an opportunity to provide guidance for the proposal review and selection process.

### C. Recommendation Follow-up

Audit standards require follow-up on past recommendations.<sup>4</sup> The following information provides updates to recommendations that Internal Audit has made in the past.

- Shared Drives

In a report on SCAG's use of shared drives provided to the Audit Committee on June 15, 2016, Internal Audit recommended that SCAG should finalize policies and procedures for maintaining information, and should include the use of shared drives and handling of sensitive information when inventorying agency-wide data and updating records management policies and procedures. SCAG issued a Records Management Handbook in July 2017.<sup>5</sup> The handbook discusses sensitive information as well as the use of shared network drives. For instance, the handbook provides guidelines for how unclassified sensitive information should be protected. In addition, the handbook notes that SCAG is in the process of moving towards an electronic content management system that will store all final records. Shared network drives are to be eventually eliminated.

- Separated Employee Access to SCAG Systems

In a report on the potential for separated employees to access SCAG IT systems provided to the Audit Committee on June 15, 2016, Internal Audit recommended that SCAG should strengthen procedures for terminating access to accounts for separated employees by: (1) developing policies and procedures regarding separating employees that include specific time frames for disabling and/or deleting accounts; and (2) verifying that separated employees' accounts have been disabled within the prescribed time frames. Human Resources has been working with the IT Division in conjunction with Allied Digital Services, LLC (ADSL) to finalize procedures related to

<sup>3</sup>Contracts and Accounting staff indicated that SCAG requires subconsultants to follow the same procedures as a prime consultant, which includes submitting documentation, such as payroll and receipts, to show that invoice costs are based on actual expenses. However, this usually occurs after the contract has been executed.

<sup>4</sup>Performance Standard 2500, Institute of Internal Auditors (IIA), *International Standards for the Professional Practice of Internal Auditing (Standards)* (Jan. 2017).

<sup>5</sup>SCAG, *Records Management Handbook*, (July 2017).

deactivating separated employees' accounts, including set time frames and confirmation of time frames.<sup>6</sup>

- Contract Closeout

In a report on SCAG's contract close-out practices provided to the Audit Committee on September 12, 2017, Internal Audit recommended that as SCAG updates its policies and procedures, it should consider ways to address limitations associated with current practices, including how contract deliverables are to be managed and tracked. SCAG is currently updating its contract close-out process to include tracking contract deliverables as they are received as well as evaluating consultant performance and assigning overall responsibility for ensuring the contract was satisfactorily completed, among other things. This is being done in conjunction with a current effort to develop agency-wide guidance for project management, including mapping out the overall processes and actions involved with carrying out project (e.g. managing staff effort as well as consultant effort). New close-out practices will be finalized as project management guidance is formalized.

Internal Audit will provide more updates regarding these actions as well as any others related to past recommendations at future Audit Committee meetings.

*D. Risk Assessment Update*

Internal Audit has started soliciting information from management staff for an annual risk assessment.<sup>7</sup> The results of the risk assessment are to provide input into Internal Audit's upcoming workplan for fiscal year (FY) 2019. In addition to inquiring about potential areas of risk, Internal Audit also sought information on how SCAG could optimize and/or generate efficiencies in its operations. The most frequent comments included a desire for a framework and/or guidance regarding how SCAG should carry out its operations, to include a clear description of various staff responsibilities and defined roles for each department (e.g. Budget and Grants, Contracts, and Planning, etc.).<sup>8</sup>

With regard to SCAG operations, comments were split between managing staff effort (to include budgeting staff hours and ensuring staff have necessary project management skills, among other things) and contracting. This seems, in part, due to SCAG relying on both staff and consultant efforts to complete projects listed in the agency's overall work program (OWP).<sup>9</sup> On more than one occasion, it was noted that SCAG planners are hired for their planning skills. As such, some may have little experience with project management. Without standardized guidance that staff can access, staff tend to learn how to manage SCAG projects from senior staff or managers. However, such senior staff or managers do not always follow the same processes or procedures, leading to inconsistencies in how projects are managed, and can cause a risk that SCAG is not following its own policies as well as requirements of grantors. In addition to updated and standardized guidance, it

<sup>6</sup>SCAG has contracted with ADSL for daily IT support. See <https://www.allieddigital.net/us/> for information on ADSL.

<sup>7</sup>Staff consulted included managers and directors. Much of the information discussed is the result of discussions and input from SCAG planning managers.

<sup>8</sup>Other issues discussed included length of contracts and when they should be re-bid; increased advertising of requests for proposals (RFP) so as to help gain a wider range of bids; and guidance on funding requirements, among other things.

<sup>9</sup>The OWP is basically SCAG's official statement of proposed work and estimated costs that tie transportation planning activities to specific available funding sources.



was mentioned that regular (e.g. annual) training would be helpful. Below are summaries of issues raised with regard to managing staff as well as contracts.

- Managing Staff Effort

With regard to managing staff effort, there is a desire for clear direction on how staff are to budget their hours as well as charge their time. Others have noted that there should be some guidance on how to charge to the OWP. For instance, some comments noted that staff spend time on work not directly related to a specific project, but they do not have an indirect or general code to charge for such type of work. Also, there needs to be training and guidance on how to develop a scope of work for projects (this includes OWP projects as well as for contracts).

- Managing Contracts

With regard to managing contracts, there is a desire for basic training on how contracts are to be administered at SCAG. Some comments included a desire for a centralized way to review, approve, or deny invoices since project managers do not necessarily know how to access invoices by themselves.<sup>10</sup> Also, there is no framework for how to monitor contracts, to include tracking and maintaining contract deliverables; there is a need for an easily accessible inventory of existing contracts. Another issue mentioned is that guidance is needed for contracts involving cities. For such contracts, SCAG provides funding and performs invoicing, but the cities tend to act as the lead project managers, thereby resulting in consultants having two bosses (SCAG and the cities). Further, city officials can have their own priorities.

As noted in prior reports, SCAG is currently in the process of developing and updating policies and procedures for project management. This provides an opportunity to address some of the issues discussed above. The Planning Division has taken the lead in these efforts, and Internal Audit plans to provide the division with a summary of risk assessment results so as to help inform any new project management guidance. Also, SCAG is in the process of adopting an electronic content management system that will store all final records, which could enhance transparency with regard to project files, to include invoices and contract deliverables.

**FISCAL IMPACT:**

None

**ATTACHMENT:**

None

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<sup>10</sup>Accounting receives and maintains invoices.

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Southern California Association of Governments  
900 Wilshire Blvd., Suite 1700, Los Angeles, CA 90017

**Agenda Item No. 5**  
**March 20, 2018**

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**To:** Audit Committee (AC)

**From:** Josh Margraf, Internal Auditor, (213) 236-1890,  
margraf@scag.ca.gov

**Subject:** Ethics Hotline Update

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**RECOMMENDED ACTION:**

For Information Only – No Action Required

**EXECUTIVE SUMMARY:**

*This report provides a summary of the new SCAG Ethics and Compliance Hotline which was implemented last year.*

**STRATEGIC PLAN:**

This item supports SCAG's Strategic Plan Goal 5: Recruit, Support, and Develop, a World-class Workforce and Be the Workplace of Choice.

**BACKGROUND:**

As previously reported to the Audit Committee, SCAG implemented a new Ethics and Compliance Hotline system (Hotline) on February 1, 2017. In an effort to ensure no perceived barriers exist for reporting violations, and to set up a formal case recording and management system, SCAG selected Lighthouse Services, an independent third party consultant, to operate the Hotline. The new Hotline replaced the former internal fraud/ethics hotline established by SCAG in 2009 as a separate phone number that was monitored by the Internal Auditor.

SCAG has received 33 reports since the new Hotline has been in operation. Since the Audit Committee's last meeting, there have been nine reports. By comparison, SCAG received only one report through the prior hotline. Although the prior hotline allowed individuals to leave anonymous messages, there may have been concern about anonymity given that it was an internal SCAG phone number; this may have accounted for only one report submitted.

SCAG reviews the information for each report made through the Hotline. When SCAG receives a report through the Hotline, the report is identified with a case number as part of the Hotline's case management system. The 33 reports were all submitted anonymously. SCAG has the ability to ask follow-up questions or request additional information from the reporter, even with anonymous reports. If the reporter does not respond to the follow-up questions, SCAG will usually close the case. In instances, where detailed information has been provided, SCAG performs a preliminary fact-finding review. Of the 33 reports, SCAG staff engaged in preliminary fact-finding for six cases. There was also one report which required a full investigation that led to a separate issue that may

not have been reported if the investigation did not happen. The new Hotline system has provided a mechanism for reporting matters that may not have otherwise been raised, as well as allowed the agency to address serious situations such as inappropriate conduct in the workplace.

SCAG continues to develop a method for how to best manage report intake and responses. In late 2017, SCAG updated the Ethics Policy and developed written procedures to reflect the current process for reviewing reports submitted through the new Hotline. Of the 33 cases in the case management system, SCAG has closed 31. Internal Audit will continue to monitor the Hotline and provide updates to the Audit Committee.

**FISCAL IMPACT:**

None

**ATTACHMENT:**

None