



SOUTHERN CALIFORNIA  
**ASSOCIATION of  
GOVERNMENTS**

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Human Development

Bill Jahn, Big Bear Lake

Energy & Environment

Deborah Robertson, Rialto

Transportation

Alan Wapner, San Bernardino

Associated Governments

## MEETING OF THE

# AUDIT COMMITTEE

***Monday, December 14, 2015***

***1:00 p.m. – 2:30 p.m.***

### **SCAG Offices**

**818 W. 7<sup>th</sup> Street, 12<sup>th</sup> Floor**

**Policy Committee Rm. A**

**Los Angeles, CA 90017**

**(213) 236-1800**

### **Teleconference and Videoconference will be available**

**(Location information included in packet)**

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 [summers@scag.ca.gov](mailto:summers@scag.ca.gov).

Agendas & Minutes for the Audit Committee are also available at:

[www.scag.ca.gov/committees.htm](http://www.scag.ca.gov/committees.htm)

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# *Audit Committee Membership*

## *December 2015*

### **Members**

1. Hon. Margaret Finlay, Duarte, (**Chair**)
2. Hon. Cheryl Viegas-Walker, El Centro
3. Hon. Michele Martinez, Santa Ana
4. Hon. Carl Morehouse, San Buenaventura
5. Hon. Greg Pettis, Cathedral City
6. Hon. Glen Becerra, Simi Valley
7. Hon. Edward H. J. Wilson, Signal Hill

### **Representing**

**District 35, SCAG, 2<sup>nd</sup> Vice-President**  
**District 1, SCAG, President**  
**District 16, SCAG, 1<sup>st</sup> Vice-President**  
**District 47, SCAG, Imm. Past President**  
**District 2**  
**District 46**  
**Gateway Cities COG**

## **Teleconference Locations**

Hon. Margaret Finlay, Chair  
2221 Rim Road  
Duarte, CA 91008

Hon. Michele Martinez  
300 W. 2<sup>nd</sup> Street,  
Santa Ana, CA 92701

Hon. Greg Pettis  
City Hall  
68700 Avenida Lalo Guerrero  
Cathedral City, CA 92234

Hon. Glen Becerra  
1 Gateway Plaza, 19th Floor, Room 41  
Los Angeles, CA. 90012

Hon. Ed Wilson, CPA (Inactive)  
Mayor Signal Hill  
City Hall  
2175 Cherry Ave.  
Signal Hill, CA 90755

## **Videoconference Locations**

Imperial County SCAG Office  
1405 North Imperial Avenue  
Suite 1  
El Centro, CA 92243

Hon. Cheryl Viegas-Walker



**AUDIT COMMITTEE  
TELECONFERENCE INFORMATION  
Pursuant to Government Code Section §54953**

**INSTRUCTIONS REGARDING TELECONFERENCE**

***Teleconference number provided under separate cover***

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

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



# AUDIT COMMITTEE AGENDA DECEMBER 14, 2015

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**TIME      PG#**

*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 & PLEDGE OF ALLEGIANCE**

*(Hon. Margaret Finlay, 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 Audit Committee must fill out and present a speaker’s card to the Assistant prior to speaking. Comments will be limited to three (3) minutes per speaker provided that the Chair has the discretion to reduce this time limit based on the number of speakers. The Chair may limit the total time for all public comments to twenty (20) minutes.

**REVIEW and PRIORITIZE AGENDA ITEMS**

**SELECTION OF VICE CHAIR**

**CONSENT CALENDAR**

**Approval Items**

- |  |                   |  |          |
|--|-------------------|--|----------|
| 1. <u>Minutes of the April 7, 2015 Special Meeting</u> | <b>Attachment</b> |  | <b>1</b> |
|--|-------------------|--|----------|

**INFORMATION ITEMS**

- |  |                   |               |           |
|--|-------------------|---------------|-----------|
| 2. <u>ALGA Peer Review Report</u><br><i>(Basil Panas, CFO)</i>   | <b>Attachment</b> | <b>20 min</b> | <b>5</b>  |
| 3. <u>Peer Review of Internal Audit Department</u><br><i>(Richard Howard, Internal Auditor)</i>          | <b>Attachment</b> | <b>20 min</b> | <b>25</b> |
| 4. <u>Amendments to Policies and Procedures Manual</u><br><i>(Richard Howard, Internal Auditor)</i>      | <b>Attachment</b> | <b>10 min</b> | <b>27</b> |
| 5. <u>FY 2014-15 Preliminary Financial Audit Report</u><br><i>(Basil Panas, Chief Financial Officer)</i> | <b>Attachment</b> | <b>25 min</b> | <b>61</b> |
| 6. <u>Internal Audit Status Report</u><br><i>(Richard Howard, Internal Auditor)</i>                      | <b>Attachment</b> | <b>5 min</b>  | <b>97</b> |



# AUDIT COMMITTEE AGENDA DECEMBER 14, 2015

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		<i>TIME</i>	<i>PG#</i>
7. <u>Vendor Survey</u> <i>(Richard Howard, Internal Auditor)</i>	Attachment	10 min	99
8. <u>2016 Meeting Schedule</u> <i>(Basil Panas, Chief Financial Officer)</i>	Attachment	5 min	105

## **STAFF REPORT**

### Emergency Preparedness

Catherine Kirschbaum, Chief Information Officer

## **FUTURE AGENDA ITEMS**

Any member or staff desiring to place items on a future agenda may make such a request.

## **ANNOUNCEMENTS**

## **ADJOURNMENT**

*The next regular Audit Committee meeting will be held on March 15, 2016, unless otherwise noted, at the SCAG Los Angeles Office.*

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Special Meeting of the Audit Committee  
of the  
Southern California Association of Governments

April 7, 2015

*Minutes*

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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**

**Representing**

Hon. Michele Martinez, (Chair)

District 16, SCAG 2<sup>nd</sup> Vice-President  
(Via Teleconference)

Hon. Carl Morehouse, San Buenaventura

District 47, SCAG President  
(Via Teleconference)

Hon. Margaret Finlay, Duarte, (Vice Chair)

District 35 (Via Teleconference)

Hon. Greg Pettis, Cathedral City

District 2, SCAG Imm. Past President  
(Via Teleconference)

Hon. Cheryl Viegas-Walker, El Centro

District 1, SCAG 1<sup>st</sup> Vice-President  
(Via Teleconference)

Hon. Edward H. J. Wilson, Signal Hill

Gateway Cities COG  
(Via Teleconference)

**Members Not Present**

Hon. Glen Becerra, Simi Valley

District 46

**CALL TO ORDER & PLEDGE OF ALLEGIANCE**

Hon. Margaret Finlay, Vice-Chair, called the meeting to order at 2:04 p.m. and asked all to join in the Pledge of Allegiance.

**ROLL CALL**

A roll call was taken at 2:06 p.m. It was determined that a quorum was present. At 2:07 p.m. Hon. Michele Martinez, Chair, joined the meeting and proceeded to preside over the meeting.

**PUBLIC COMMENT PERIOD**

None.

**REVIEW and PRIORITIZE AGENDA ITEMS**

There were no reprioritizations made.

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Special Meeting of the Audit Committee  
of the  
Southern California Association of Governments

April 7, 2015

*Minutes*

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**CONSENT CALENDAR**

**Approval Items**

1. Minutes of March 17, 2015 Meeting

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

AYES: Martinez, Morehouse, Pettis, Viegas-Walker, and Wilson  
NOES: None  
ABSTAIN: None

**ACTION ITEMS**

2. Peer Review of Internal Audit Function

Basil Panas, Chief Financial Officer, provided a brief overview and update of the request for a Peer Review of the Internal Audit Function (Review), of which three (3) options was previously discussed at the March 17, 2015 Audit Committee meeting. Mr. Panas noted that at that meeting, the Committee authorized the Executive Director to award a sole-source contract to Vasquez & Co., LLP (Option 3). Since that time, the Association of Local Government Auditors (ALGA) had contacted the CFO and advised that a Peer Review could commence in six months. As such, Mr. Panas explained that staff was bringing the matter back to the Audit Committee for direction on how to proceed.

Staff responded to the comments and questions from the Committee, including comments pertaining to the scheduling and timing should ALGA do the Peer Review, and the projected cost savings to SCAG with ALGA to do the Peer Review. There was a discussion on the need to rescind the Committee's prior action on March 17, 2015 should the Committee direct staff to proceed with Option 1 (having ALGA conduct Peer Review of SCAG's Internal Audit Function).

A MOTION was made (Viegas-Walker) and SECONDED (Martinez) to have ALGA conduct Peer Review of SCAG's Internal Audit Function which will commence in six months and to rescind the Committee's prior action of March 17, 2015 related to awarding a sole-source contract to Vasquez & Co., LLP. The motion was passed by the following vote:

AYES: Martinez, Morehouse, Finlay, Pettis, Viegas-Walker, and Wilson  
NOES: None  
ABSTAIN: None

**STAFF REPORT**

There was no staff report made.



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Special Meeting of the Audit Committee  
of the  
Southern California Association of Governments

April 7, 2015

*Minutes*

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**FUTURE AGENDA ITEMS**

There were no future agenda items requested.

**ANNOUNCEMENTS**

There were no announcements made.

**ADJOURNMENT**

*Hon. Michele Martinez, Chair, adjourned the meeting at 2:15 p.m. The next regular meeting of the Audit Committee is scheduled for Tuesday, June 9, 2015 at 1:00 p.m., at the SCAG Los Angeles Office.*

**Minutes Approved by:**



Basil Panas, CFO  
Staff to the Audit Committee

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# REPORT

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**DATE:** December 14, 2015  
**TO:** Audit Committee  
**FROM:** Basil Panas, CFO, (213) 236-1817, panas@scag.ca.gov  
**SUBJECT:** ALGA Peer Review Report

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**RECOMMENDED ACTION:**

For Information Only – No Action Required.

**EXECUTIVE SUMMARY:**

*ALGA Peer Review auditor(s) will present their report on SCAG's Internal Function.*

**STRATEGIC PLAN:**

This item supports SCAG's Strategic Plan Goal 3: Enhance the Agency's Long-Term Financial Stability and Fiscal Management.

**BACKGROUND:**

At its May 2012 Audit Committee meeting, the Committee members requested a Peer Review of SCAG's Internal Audit function. SCAG's Internal Audit function follows GAGAS, which is commonly referred to as Generally Accepted Government Auditing Standards. They are for use by auditors of government entities and entities that receive government awards and audit organizations performing GAGAS audits. Therefore, in researching firms to conduct the Peer Review, staff selected the Association of Local Government Auditors (ALGA) because their reviews are in strict compliance with GAGAS standards. ALGA also has performed recent Peer Reviews of the Los Angeles County Metropolitan Transportation Authority (MTA) audit functions. Please see ALGA's website at [www.governmentauditors.org](http://www.governmentauditors.org).

ALGA has completed the review and will present their report today.

**FISCAL IMPACT:**

None.

**ATTACHMENT:**

Peer Review Report.

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*Peer Review of the  
Southern California  
Association of Governments  
Internal Audit Department*

*December 14, 2015*



# *Government Auditing Standards*

I **Government  
Auditing  
Standards**

II A.L.G.A.

III **The Peer  
Review Team**

IV **Review  
Objectives**

V **Results of the  
Review**

- **Issued by the Comptroller General of the United States**
- **Applicable for federal, state, and local government organizations, programs, activities and functions**



# *Government Auditing Standards*

I **Government  
Auditing  
Standards**

➤ **Independence**

II **A.L.G.A.**

➤ **Professional Judgment**

III **The Peer  
Review Team**

➤ **Competence**

➤ **Quality Control and Assurance**

IV **Review  
Objectives**

➤ **Field Work Standards**

V **Results of the  
Review**

➤ **Reporting Standards**



# *Quality Control Standards*

I **Government Auditing Standards**

II **A.L.G.A.**

III **The Peer Review Team**

IV **Review Objectives**

V **Results of the Review**

**“Audit organizations performing audits and attestation engagements in accordance with generally accepted government auditing standards must have an external peer review performed by reviewers independent of the audit organization being reviewed at least once every 3 years.”**





# *Quality Control Standards*

I **Government  
Auditing  
Standards**

II **A.L.G.A.**

III **The Peer  
Review Team**

IV **Review  
Objectives**

V **Results of the  
Review**

**The peer review should determine whether the audit organization's system of quality control was suitably designed and if it is complying with its quality control system in order to provide reasonable assurance of compliance with Government Auditing Standards.**



# *The Association of Local Government Auditors*

I Government Auditing Standards

II A.L.G.A.

III The Peer Review Team

IV Review Objectives

V Results of the Review

➤ **Professional Organization:**

- Over 300 organizational members
- Over 2,000 individual members

➤ **A.L.G.A. Objectives:**

- Improve local government auditing
- Provide a forum for exchanging information and ideas
- Encourage and uphold highest professional standards

➤ **Conducted over 400 peer reviews**



# *Review Team Requirements*

I **Government  
Auditing  
Standards**

➤ **Knowledge of generally accepted government auditing standards and the government environment**

II **.A.L.G.A.**

III **The Peer  
Review Team**

➤ **Independent of the audit organization being reviewed**

IV **Review  
Objectives**

➤ **Knowledge of how to perform a peer review**

V **Results of the  
Review**



# *The Peer Review Team*

I Government  
Auditing  
Standards

II A.L.G.A.

III **The Peer  
Review Team**

IV Review  
Objectives

V Results of the  
Review

## ➤ **Mike Edmonds-Team Leader**

- **35 years of government auditing experience**
- **Participated in 18 peer reviews of various types of governmental audit agencies**
- **Certified Internal Auditor**



# *The Peer Review Team*

I Government  
Auditing  
Standards

II A.L.G.A.

III **The Peer  
Review Team**

IV Review  
Objectives

V Results of the  
Review

## ➤ **Emilyzen Cervantes**

- **First peer review**
- **Internal Auditor-LA City  
Controller's Office-1 year**
- **Governmental Consultant-6  
years**
- **MPP from the Kennedy School  
of Government at Harvard**



# *Review Objectives*

I Government  
Auditing  
Standards

II A.L.G.A.

III The Peer  
Review Team

IV **Review  
Objectives**

V Results of the  
Review

- **Assess the adequacy of the audit organization's internal quality control system to provide reasonable assurance of compliance with Government Auditing Standards**



# *Review Objectives*

I Government Auditing Standards

➤ **Assessed whether Government Auditing Standards were followed:**

II A.L.G.A.

- **Assessed the organization's policies and procedures**
- **Examined 7 audit engagements**
- **Reviewed training and personnel records**
- **Interviewed Internal Audit and SCAG staff**

III The Peer Review Team

IV **Review Objectives**

V Results of the Review



# *Results of the Review*

I Government  
Auditing  
Standards

II A.L.G.A.

III The Peer  
Review Team

IV Review  
Objectives

V Results of the  
Review

## ➤ Peer Review Report:

- Pass with deficiency

## ➤ Management Letter:

- Areas where the office excels
- Suggestions for improvement





# *Pass with Deficiency opinion*

I Government Auditing Standards

- **Internal Audit does not meet the independence standard for internal auditing**

II A.L.G.A.

III The Peer Review Team

- **Internal Auditor reports to the CFO but should be accountable to the head or deputy head of the organization**

IV Review Objectives

V **Results of the Review**

- **Recommend that Internal Audit and SCAG officials discuss options to change the auditor's reporting relationship**



## *Areas where the office excels*

I Government Auditing Standards

➤ Certifies that staff are qualified and independent prior to undertaking the engagement

II A.L.G.A.

➤ Uses a checklist to assess compliance with standards

III The Peer Review Team

IV Review Objectives

➤ Uses standard audit programs for pre-award contract audits

V Results of the Review



# *Suggestions for Improvement*

I Government Auditing Standards

➤ **Develop policies and procedures for:**

II A.L.G.A.

- **Assessing threats to independence by providing nonaudit services**

III The Peer Review Team

IV Review Objectives

- **Monitoring and reporting on its quality control system**

V **Results of the Review**

- **Documenting an overall assessment of evidence**



# *Suggestions for Improvement*

I Government Auditing Standards

II A.L.G.A.

III The Peer Review Team

IV Review Objectives

V Results of the Review

## ➤ **Audit reports should include:**

- **A section describing the scope, objectives, and methodology, and more well-defined audit objectives**
- **Appropriate language for citing compliance with Government Auditing Standards**
- **Views of responsible officials**



# *QUESTIONS*

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# REPORT

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**DATE:** December 14, 2015

**TO:** Audit Committee

**FROM:** Richard Howard, Internal Auditor, (213) 236-1905, [howard@scag.ca.gov](mailto:howard@scag.ca.gov)

**SUBJECT:** Peer Review of Internal Audit Department

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**RECOMMENDED ACTION:**

For Information Only – No Action Required.

**STRATEGIC PLAN:**

This item supports SCAG's Strategic Plan, Goal 3 – Enhance the Agency's Long Term Financial Stability and Fiscal Management.

**BACKGROUND:**

The Audit Committee requested a peer review of the Internal Audit Department in May, 2012. The review was performed by the Association of Local Government Auditors (ALGA). ALGA requires that audit departments be members of ALGA for at least two years before a peer review can be conducted.

ALGA performed a peer review of the Internal Audit Department the week of November 2 through November 6, 2015. The written findings of ALGA were shared with SCAG on November 6, 2015. The peer review team's report is included as a separate agenda item in today's meeting. Mr. Mike Edmonds will present the Peer Review report to the Committee.

The peer review team's report concluded that the Internal Audit Department's internal quality control system was suitably designed and operating effectively to provide reasonable assurance of compliance with Government Auditing Standards, except for the following deficiency.

The deficiency noted by the review team is that the Internal Auditor is not independent and is not in compliance with Government Auditing Standards. To be considered independent for the purposes of reporting internally, the Internal Auditor should report to either the Audit Committee, Executive Director, or to the Chief Deputy Executive Director.

The ALGA peer review team also issued a companion letter to offer observations and suggestions to enhance Internal Audit's demonstrated adherence to Government Auditing Standards. The letter offered six (6) observations and recommendations. Following are the six observations and Internal Audit's plan to address the corrective actions. Five of the recommendations require changes to the Internal Audit Policy and Procedures manual. These are addressed in the next agenda item.

1. *The Department lacks policies and procedures for assessing threats to independence related to providing nonaudit services.*

# REPORT

---

Internal Audit has strengthened its Policies and Procedures Manual dealing with threats to independence by providing nonaudit services.

- 2. The Department has not developed a process to monitor its Quality Control System and summarize the results, at least annually.*

Internal Audit has added a procedure to the Policies and Procedures Manual to monitor, at least annually, the Quality Control System, analyzing and summarizing the results of the monitoring.

- 3. The Department lacks formal policies and procedures for performing and documenting an overall assessment of the evidence used to support the findings and conclusions in the audit reports.*

Internal Audit has added policies and procedures to its Policies and Procedures Manual for performing and documenting an overall assessment of the evidence used to support the audit report's findings and conclusions.

- 4. The Department's audit reports do not have a separate section of the report defining the audit objectives scope and methodology. Also, two performance audits had overly broad objectives.*

Internal Audit has revised its report format to include a separate section for describing the audit objectives, scope and methodology. In addition, Internal Audit will develop well-defined audit objectives that are limited to the work performed.

- 5. The Department's compliance statement is not consistent with the language in Government Auditing Standards Section 7.30.*

Internal Audit has been using a compliance statement that paraphrases the language in Section 7.30. The exact language in Section 7.30 will be used in all future reports.

- 6. The Department does not provide responsible officials of the audited entity with a written draft of the report for review and comment and does not usually include written comments from responsible officials of the organization.*

Internal Audit already has a policy in its Policies and Procedures Manual to obtain and report views of responsible officials of the audited entity and to provide a draft report for review and comment. The policy also states that if written comments are obtained from responsible officials of the audited entity, these comments will be included in the final report. Internal Audit will ensure that these policies are enforced in regard to future reports.

## **FISCAL IMPACT:**

None.

## **ATTACHMENTS:**

None.





# REPORT

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**DATE:** December 14, 2015

**TO:** Audit Committee

**FROM:** Richard Howard, Internal Auditor, (213) 236-1905, [howard@scag.ca.gov](mailto:howard@scag.ca.gov)

**SUBJECT:** Approval of Amendments to Internal Audit Department's Policies and Procedures Manual

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**RECOMMENDED ACTION:**

Approve Amendments to the Internal Audit Policies and Procedures Manual suggested by the ALGA Peer Review.

**STRATEGIC PLAN:**

This item supports SCAG's Strategic Plan, Goal 3 – Enhance the Agency's Long Term Financial Stability and Fiscal Management.

**BACKGROUND:**

As noted in the previous agenda item, the Association of Local Government Auditors (ALGA) has performed a peer review of the Internal Audit Department and issued a companion letter to its report to offer observations and suggestions to enhance Internal Audit's demonstrated adherence to Government Auditing Standards. The letter offered six (6) observations and recommendations which the Internal Audit department has addressed with changes to its Policies and Procedures Manual as described below. The changes are shaded in yellow in the attached Manual on the pages indicated below.

1. *The Department lacks policies and procedures for assessing threats to independence related to providing nonaudit services.*

Internal Audit has strengthened its Policies and Procedures Manual dealing with threats to independence by providing nonaudit services. Actions are highlighted in Section C. 20, Page 22 of the Policies and Procedures Manual. Internal Audit staff will assess and document the impact of prior nonaudit services if they are related to a current audit. Prior to performing a nonaudit service, Internal Audit staff will apply the conceptual framework [as outlined in Government Auditing Standards] to evaluate independence and will document the results of the evaluation.

2. *The Department has not developed a process to monitor its Quality Control System and summarize the results, at least annually.*

Internal Audit has added a procedure to the Policies and Procedures Manual to monitor, at least annually, the Quality Control System, analyzing and summarizing the results of the monitoring. Action is highlighted in Section C.12, Page 16, Quality Control, of the Policies and Procedures Manual. On an annual basis, Internal Audit staff will perform a Quality Control Review of work performed during the year. The auditors will document the results of the Quality Control Review.

3. *The Department lacks formal policies and procedures for performing and documenting an overall assessment of the evidence used to support the findings and conclusions in the audit reports.*

Internal Audit's Policies and Procedures Manual, Section C.13, Page 16 and 17, prescribes the methods used to develop the elements of findings and to document the process.

- 4. The Department's audit reports do not have a separate section of the report defining the audit objectives scope and methodology. Also, two performance audits had overly broad objectives.*

Internal Audit has revised its Manual in Section C.15, Pages 17 and 18, to include a description of the objectives, scope and methodology of the audit. A scope and methodology section will be included in the audit report. In addition, Internal Audit will develop well-defined audit objectives that are limited to the work performed.

- 5. The Department's compliance statement is not consistent with the language in Government Auditing Standards Section 7.30.*

Internal Audit has been using a compliance statement that paraphrases the language in Section 7.30. The exact language in Section 7.30 will be used in all future reports. This exact language is as follows:

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

- 6. The Department does not provide responsible officials of the audited entity with a written draft of the report for review and comment and does not usually include written comments from responsible officials of the organization.*

Internal Audit already has a policy in its Policies and Procedures Manual to obtain and report views of responsible officials of the audited entity and to provide a draft report for review and comment. Please see Sections C.16 and C.17, Pages 18 and 19 of the Manual. The policy also states that if written comments are obtained from responsible officials of the audited entity, these comments will be included in the final report. Internal Audit will ensure that these policies are enforced in regard to future reports. Thus, no change to the Manual is needed for this recommendation.

We request approval by the Audit Committee of the changes to the Policies and Procedures Manual outlined above.

**FISCAL IMPACT:**

None.

**ATTACHMENTS:**

Internal Audit Department Policies and Procedures Manual.  
(Updated December 2015)

# **INTERNAL AUDIT DEPARTMENT**

## **POLICIES & PROCEDURES MANUAL**

**NOVEMBER 4, 2014  
(REVISED DECEMBER 2015)**

**SOUTHERN CALIFORNIA**



**ASSOCIATION of  
GOVERNMENTS**

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**APPENDIX A PREAWARD AUDIT PROGRAM**

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**APPENDIX D WORKPAPER INDEX**

## A. Organization

### A.1. Internal Audit Charter

The internal audit function was established by the Regional Council and the SCAG Executive Director, pursuant to the Internal Audit Charter adopted in 2002. The objective of the internal audit function is to assist all members of management in the efficient and effective discharge of their responsibilities by furnishing them with independent analysis, appraisals and recommendations. The Internal Auditor is authorized to conduct such audits/reviews of any department system or function as are necessary to accomplish its objective. The Internal Auditor is authorized complete and unrestricted access to all SCAG records, personnel and physical properties relevant to the performance of the audit/review. The Internal Auditor reports to the Audit Committee. Administratively, the Internal Auditor has a dotted-line reporting responsibility to the Chief Financial Officer.

### A.2. Code of Ethics

Generally Accepted Government Auditing Standards (GAGAS) establishes fundamental principles of ethical behavior.<sup>1</sup> The public expects auditors who conduct their work in accordance with GAGAS to follow ethical principles. Other ethical requirements or codes of professional conduct may apply to auditors who conduct audits in accordance with GAGAS. For example, Certified Public Accountants (CPAs) are required by their state boards of accountancy to have ethics training to renew their licenses.

The ethical principles that guide the work of the auditors who conduct audits in accordance with GAGAS are: a. the public interest; b. integrity; c. objectivity; d. proper use of government information, resources and positions; and e. professional behavior.

As an employee of SCAG, the Internal Auditor is required to abide by the SCAG Ethics Policy which was approved by the SCAG Regional Council on April 2, 2009.<sup>2</sup> All employees are required to affirm each year that they have read, accept and will abide by all provisions of the Ethics Policy.

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<sup>1</sup>GAO, *Government Auditing Standards 2011 Revision*, [GAO-12-331G](#), (Washington, D.C.: Dec. 11, 2011). Also see <http://www.gao.gov/yellowbook> for an electronic version of GAGAS.

<sup>2</sup>See <http://info/policies/pdfs/scagEthicsPolicy062811.pdf> on SCAG's intranet for a copy of SCAG's Ethics Policy.

### A.3. Standards

The SCAG Internal Audit Charter requires that the Internal Auditor adhere to GAGAS promulgated by the Comptroller General of the United States. Use of GAGAS also provides a framework for conducting high quality audits with competence, integrity, objectivity and independence.

In addition, the SCAG Regional Council has voted to adopt GAGAS for the internal audit function.

## B. General Standards

### B.1. Independence

The Internal Audit Department (Internal Audit) staff must be independent in mind and independent in appearance so that their findings, conclusions and recommendations are impartial and will be viewed as impartial by reasonable and informed third parties.

The Internal Audit staff should be independent of the entity being audited during the period covered by the audit.<sup>3</sup> Threats to independence should be considered, as set forth in GAGAS 3.07 et seq.<sup>4</sup> These threats should be documented. If the threats are not acceptable, the auditors should document the categories of threats and the safeguards to reduce threats to an acceptable level. If threats cannot be eliminated or reduced to an acceptable level, the audit should be declined.

The auditor should evaluate the following categories of threats to independence for each audit:

- a. Self-interest threat;
- b. Self-review threat;
- c. Bias threat;
- d. Familiarity threat;
- e. Undue influence threat;
- f. Management participation threat; and
- g. Structural threat.

Threats after the audit report is issued should be evaluated and the auditor should take appropriate steps, as described in GAGAS 3.26.

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<sup>3</sup>See GAGAS 3.02-3.06 for a discussion of independence.

<sup>4</sup>GAGAS 3.07-3.26.

The auditor should document any considerations of independence and any judgments made regarding independence. Threats identified and safeguards applied to eliminate the threats or reduce them to an acceptable level should be documented.

At the end of each fiscal year the Internal Audit staff should document that there were no impairments to the independence of the Internal Audit staff on audits performed in the fiscal year then ending.

The Internal Audit staff should be sufficiently removed from political pressures to conduct audits and report findings, opinions and conclusions objectively without fear of political reprisal.

## B.2. Professional Judgment

Professional judgment includes exercising reasonable care and professional skepticism. Reasonable care includes acting diligently in accordance with applicable professional standards and ethical principles.<sup>5</sup> Professional skepticism is an attitude that includes a questioning mind and a critical assessment of evidence. In exercising professional skepticism, the auditor assumes neither that management is dishonest nor of unquestioned honesty. Judgments made are dependent upon the auditor's competence.

## B.3. Competence

Internal Audit staff must have adequate professional competence to address audit objectives and perform the audit work in accordance with GAGAS.<sup>6</sup> Competence is derived from a blending of education and experience.

Audit staff must have the knowledge and skills appropriate for the work being performed. For example, if the audit work involves review of information systems, knowledge and skill in information technology is appropriate. The Internal Auditor must evaluate and determine if staff has the qualifications and competency for the audit work to be performed. With limited audit staff, it is particularly important that Internal Audit staff meet the qualifications and competency for performing the audit work.

Auditors performing work in accordance with GAGAS should maintain their professional competence through continuing professional education (CPE). Generally, the auditors are required to obtain 80 hours of CPE in each two-year period, with at least 20 hours of CPE in each year.

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<sup>5</sup>GAGAS 3.60-3.68.

<sup>6</sup>GAGAS 3.69-3.81.



Auditors performing work in accordance with GAGAS should also complete, every two years, at least 24 hours of CPE that directly relates to government auditing.

Auditors enter annual CPE requirements in a common file. Auditors' CPE status should be reviewed at least quarterly.

Auditors should be knowledgeable of relevant American Institute of Certified Public Accountants (AICPA) standards. Internal Audit should have a process for recruitment, hiring, continuous development, assignment and evaluation of staff to maintain a competent workforce.

#### B.4. Quality Control and Assurance.

Internal Audit must establish and maintain a system of quality control.<sup>7</sup> The system should provide Internal Audit with reasonable assurance that it is complying with professional standards and applicable legal and regulatory requirements.

Internal Audit should document its quality control policies and procedures and should document its compliance with these policies and procedures. This should be reviewed at least annually. The policies and procedures should address:

- a) The Internal Audit management has leadership responsibilities including designation of responsibility for quality of audits performed in accordance with GAGAS;
- b) Maintaining independence and complying with applicable legal and ethical requirements;
- c) Providing reasonable assurance that Internal Audit will undertake audits only if it can comply with professional standards, legal requirements and ethical principles;
- d) Having the human resources that are capable and competent to perform audits in accordance with professional standards and legal and regulatory requirements. Internal Audit management should assess skill needs to consider whether its workforce has the essential skills that match those necessary to perform the particular audit. Internal Audit should have a process for recruitment, hiring, continuous development, assignment, and evaluation of staff to maintain a competent workforce;

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<sup>7</sup>GAGAS 3.82-3.107.

- e) Providing reasonable assurance that audits are performed and reports issued in accordance with professional standards and legal and regulatory requirements;
- f) Monitoring compliance with quality control policies and procedures to determine if professional standards and legal and regulatory requirements have been followed, the quality control system has been properly designed and the quality control policies and procedures are operating effectively and complied with in practice. Monitoring is required to be done at least annually.

Internal Audit should obtain an external peer review at least once every three years. For the first peer review the review should cover a period ending no later than three years from the date internal audit began its first audit in accordance with GAGAS. A copy of the peer review report should be provided to the Audit Committee and also to the Regional Council.

## B.5. Types of Audits

Financial audits provide an opinion about whether an entity's financial statements are presented fairly in all material respects. Included in financial audits are compliance relating to government programs and forming opinions on specified items of financial statements. Internal Audit does not normally perform a financial audit of SCAG. This is done by an independent CPA firm. The independent CPA firm is selected by the Audit Committee through a competitive procurement and reports to the Audit Committee. The procurement is done at least every three years.

Attestation engagements are examinations or reviews on a subject matter that is the responsibility of another party. Included are agreed-upon procedures in which the auditor does not express an opinion.

Performance audits provide findings or conclusions based on an evaluation of evidence against criteria. These are program audits that assess efficiency and effectiveness of a particular program.

Auditors shall adhere to the audit standards that are appropriate for the audit being performed, i.e., attestation, performance, etc.

Nonaudit services are defined as professional services other than audits or attestation engagements. GAGAS does not cover nonaudit services.

## **C. SCAG Internal Audit Procedures**

### **C.1. Audit Committee**

The Audit Committee was formally established by the SCAG Regional Council to be responsible for the independent review and oversight of SCAG's financial reporting processes, internal controls and independent auditor. The Internal Audit staff reports to the Audit Committee with a dotted-line administrative responsibility to the SCAG Chief Financial Officer (CFO).

The Audit Committee reviews and approves the Internal Audit staff's annual workplan. The Committee also receives and reviews draft internal audit reports directly from the Internal Auditor.

The Internal Auditor provides status reports to the Audit Committee throughout the year, usually at the time of Audit Committee meetings. These reports give the Committee the current status of ongoing audits, recently completed audits and future audits planned.

The Audit Committee will meet with the Internal Audit staff on an as needed basis to discuss any matters that the Committee or the Internal Audit staff believes should be discussed privately.

The Audit Committee is responsible for establishing the overall policy for SCAG's internal control systems and for ensuring that the Regional Council and SCAG management are in full support of the system of internal controls. The Audit Committee is also responsible for evaluating the effectiveness of SCAG's internal control systems.

### **C.2. Risk Assessment**

The level of risk at SCAG may vary from department to department or program to program. The internal audit staff should perform an assessment of these risks. The risk assessment is necessary to establish the annual audit workplan.

The internal audit staff begins the process by requesting input from the Regional Council, the Audit Committee and senior SCAG management on areas that they see as potential high-risk. The internal audit staff also asks where these groups would like to see audit resources focused.

Internal audit uses this information to establish impact and probability risk factors. A matrix is developed showing the highest to lowest risks for SCAG. From this ranking, an audit workplan can be prepared, making the most efficient use of audit resources.

### C.3. Audit Workplan

Internal Audit staff prepares an annual workplan based on the Risk Assessment described above. The workplan is for the fiscal year, from July through June. The audit workplan is submitted to the Audit Committee for approval, usually in May of each year. The Audit Committee will either approve the audit workplan or request changes. If changes are requested, the plan will be amended and resubmitted at the next Audit Committee meeting, usually in June, for approval.

The audit workplan is a broad, higher level plan describing the types of audits planned and the estimated hours needed to complete the audits. Examples of types of audits in the workplan are: Contract Preaward audits- 500 hours; Information Technology- 400 hours; Travel Expenses – 200 hours, etc.

### C.4. Preliminary Survey

A preliminary survey is usually required before starting an audit. The preliminary survey is undertaken to review the subject and determine whether an audit is required and, if so, what type of audit should be performed. The survey will determine whether audit resources should be applied to an audit or, if an audit is not recommended, a report should be issued explaining the reason for the recommendation.

### C.5. Planning

A written audit plan must be prepared for each audit. Internal Audit staff must adequately plan and document the planning of the work necessary to address the audit objectives. The audit is intended to accomplish the objectives. Planning takes into account the objectives, the scope and the methodology of the audit. Scope is the boundary of the audit and is directly tied to the audit objectives. Methodology describes the nature and extent of audit procedures for gathering and analyzing evidence to address the audit objectives. Audit management should assign sufficient staff with adequate competence to perform the audit.

Auditors should identify criteria needed to evaluate the matters subject to audit. Criteria represent the laws, regulations, contracts, grant agreements, standards, specific requirements, measures, expected performance, defined business practices, and benchmarks against which performance is compared or evaluated.

Auditors should also evaluate whether to use the work of other auditors and specialists to address some of the audit objectives. If it is decided to employ specialists, auditors must assess the professional qualifications and independence of the specialists. Assessing the independence of specialists includes identifying threats and applying any necessary safeguards in the same manner as would be done for auditors performing work on those audits.

Auditors should have an understanding of the nature of the programs, internal controls, information systems controls, laws, regulations, contracts and grant agreements, as well as any ongoing investigations or legal proceedings within the context of the audit objectives. Auditors should also review any previous audits or attestation engagements relating to the current audit objectives.

## C.6. Audit Program

There are several types of audit programs to be used by the Internal Audit staff.

### Contract Preaward Audit

SCAG follows the preaward audit program that was based on the California Department of Transportation (Caltrans) Local Assistance Procedures Manual, Exhibit 10-M. This program is to be used and modified as required by the circumstances. See Appendix A.

### Incurred Cost Audits

This type of audit program is used for internal audits of SCAG financial systems and for SCAG subregions. It includes reviews of labor charging including timekeeping, fringe benefit and overhead rates and charges and paid bills. See Appendix B.

### Specialized Audit Programs

Occasionally modifications to the standardized programs are necessary for special purpose reviews. Examples are travel expenses, procurement reviews, etc.

## C.7. Contract Preaward Audits

Internal Audit staff is required to perform preaward audits on all contract proposals above \$250,000. The program noted above under C.6 is used for these audits. Internal Audit staff is also required to perform a preaward review of amendments to contracts if either the original contract was over \$250,000 or the amendment raises the contract value to greater than \$250,000.

The objectives of a preaward audit are to determine: whether the costs are current, reasonable, accurate and allowable; whether the consultant is financially capable to perform the contract; and whether the consultant's accounting system is adequate to record costs under government contracts.

On occasion, Internal Audit staff will be requested to perform preaward reviews of proposals under \$250,000. If the proposed consultant or a subconsultant submits direct labor, overhead or fringe benefit rates that are unusually high or, the consultant is new to SCAG or the consultant's financial capability is not clearly evident, a review might be requested.

If, in a contract proposal over \$250,000, any subconsultant is less than \$25,000, that subconsultant is not normally audited, unless the subconsultant's proposal contains some unusual item. The Internal Auditor will determine whether an item is considered to be unusual.

## C.8. Entrance Conference

Internal Audit staff should arrange a formal entrance conference with auditees at the start of an audit. The objectives of the conference are to meet key members of the auditee staff, discuss the scope of the audit and the audit program, determine key contact persons and discuss the timeframe of the audit. Other subjects related to the audit may also be introduced into the entrance conference, as well.

Prior to the entrance conference, the auditor must review any prior audits, findings and recommendations. These should be used to set the scope of the current audit. Prior audit findings and recommendations should be discussed at the entrance conference.

Not all audits will have a formal entrance conference. For example, contract preaward audits will usually begin with phone calls and emails between Internal Audit staff and the consultants' key contacts. At that point document requests are usually made and time estimates are discussed.

Document requests should be made formally for all types of audits. See Appendix C, Information Document Request.

## C.9 Performing Audits

Internal Audit staff must obtain sufficient, appropriate evidence to provide a reasonable basis for their findings and conclusions. Sufficiency is a measure of the quantity of evidence used to support the findings and conclusions related to the audit objectives. Appropriateness is the measure of the quality of evidence that encompasses the relevance, validity and reliability of evidence used for addressing the audit objectives and supporting findings and conclusions.

Auditors must use professional judgment in planning, performing and reporting audits. Professional judgment must be used to determine the sufficiency and appropriateness of evidence taken as a whole.

Auditors may use different types of evidence. Evidence obtained through direct physical examination or observation is the most reliable. Other types of evidence may be used such as original documents, copies of original documents, testimony from individuals who are not biased and can speak freely and evidence from a knowledgeable, credible and unbiased third party.

Evidence is sufficient and appropriate when it provides a reasonable basis for supporting the findings or conclusions within the context of the audit objectives.

### C.10. Testing and Sampling

Testing is a necessary step in audits. Internal Audit staff shall review internal controls as part of audits at SCAG. After reviewing internal controls with auditees and completing questionnaires, the next step is to test the assertions made and questions answered to verify that the controls are working as claimed.

Tests should be of such a size and nature to substantiate what is actually happening in the processes under examination. For example, a test of accounts payable must be of such magnitude that it represents what is actually being done in processing invoices and is not just a rare exception.

Internal Audit staff may use statistical sampling whenever possible in performing audits. Sampling can be classified into two main categories of estimation and acceptance sampling. Estimation sampling provides an answer to the question of how many or how much. For example, estimation sampling would be used to estimate how many invoices were processed without proper documentation. Acceptance sampling's purpose is to accept or reject a statement of condition.

### C.11. Work Papers

Work papers are a record of the work done on an audit. Work papers support the information presented in the final audit report, especially the findings and recommendations. Work papers also are used to allow others to review the audit work and to do a quality review.

Work papers should be organized according to the Workpaper Index. This index should be used for all types of audits. Modifications can be made for differences in the type of audit performed. See Appendix D, Workpaper Index.

Each page of the work papers should be indexed, in line with the Workpaper Index. Each page should be indexed in red pencil in the lower right corner of the page.

Where large documents are included in the work papers, such as the Request for Proposal (RFP) or a contract, only the first page should be indexed rather than every page. An exception to this is where a certain page of the document is referenced to another work paper or to the audit report.

Work papers should be cross-referenced to other work papers and to the audit report. The work papers should be complete, clear and accurate. Another auditor who is unfamiliar with the audit should be able to read and understand the work paper, the work done and the conclusions drawn.

The work papers should indicate the evidence examined to form conclusions or opinions. The evidence should be sufficient and appropriate to provide a reasonable basis for the findings and conclusions.

Evidence obtained through direct physical examination or observation is generally the most reliable. Evidence obtained from a credible and unbiased third party is generally more reliable than evidence obtained from management of the entity being audited.

Examination of original documents is more reliable than examining copies.

Auditors should evaluate and document the objectivity, credibility and reliability of testimonial evidence. When information is provided by officials of the audited entity, auditors should determine what the officials did to obtain assurance over the reliability of the information. It may require testing of management's procedures by the auditor to obtain assurance or perform direct testing of the information.

Auditors should assess the sufficiency and appropriateness of computer-processed information. The effectiveness of the audited entity's internal controls will affect the nature, timing and extent of the audit procedures.

When assessing the sufficiency and appropriateness of evidence, auditors should evaluate the expected significance of evidence to the audit objectives, findings, and conclusions, available corroborating evidence, and the level of audit risk. The steps to assess evidence may depend on the nature of the evidence, how the evidence is used in the audit or report, and the audit objectives.

- a. Evidence is sufficient and appropriate when it provides a reasonable basis for supporting the findings or conclusions within the context of the audit objectives.



- b. Evidence is not sufficient or appropriate when using the evidence carries an unacceptably high risk that it could lead the auditor to reach an incorrect or improper conclusion, the evidence has significant limitations, or the evidence does not provide an adequate basis for addressing the audit objectives or supporting the findings and conclusions. Such evidence should not be used by auditors to support findings and conclusions.

Evidence has limitations or uncertainties when the validity or reliability of the evidence has not been assessed or cannot be assessed, given the audit objectives and the intended use of the evidence. Limitations also include errors identified by the auditors in their testing. When the auditors identify limitations or uncertainties in evidence that is significant to the audit findings and conclusions, they should apply additional procedures, as appropriate.

Work paper retention should be in accordance with SCAG's record retention policies.<sup>8</sup> Work papers should be available to other auditors upon request.

## C.12. Quality Control

Quality control procedures should ensure that Internal Audit staff are independent, use professional judgment, are competent, and adequately plan audits. The procedures also should ensure that Internal Audit staff obtains sufficient appropriate evidence to support findings, document the audit findings and present them in an audit report.

Auditors should determine the overall sufficiency and appropriateness of evidence to provide a basis for findings and conclusions. Auditors should perform and document an overall assessment of the collective evidence used to support findings and conclusions, including the results of any specific assessments conducted to conclude on the validity and reliability of specific evidence.

As part of the quality control system, monitoring procedures should be established. The monitoring should evaluate whether a) professional standards and legal and regulatory requirements have been followed, b) the quality control system has been appropriately designed and c) quality control policies and procedures are operating effectively and complied with in practice.

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<sup>8</sup>See [http://info/legal/pdfs/Records\\_Management\\_Policy.pdf](http://info/legal/pdfs/Records_Management_Policy.pdf) on SCAG's intranet for a copy of SCAG's Records Management Policy and Procedures.

The Internal Audit staff consists of two auditors. On an annual basis, Internal Audit staff will perform a Quality Control Review of work performed during the year. Each auditor will review the work of the other (to include any audit reports and non-audit services as well as associated documentation) to determine whether: (1) the audit work is in compliance with professional requirements, including GAGAS and Internal Audit policies and procedures (as outlined in this manual) and (2) addressing any recommendations stemming from a peer review. The auditors will document the results of the Quality Control Review.

Internal Audit should analyze and summarize the results of its monitoring process at least annually, with identification of any systemic or repetitive issues needing improvement, along with recommendations for corrective action. This should be documented as Quality Control Review. Deficiencies should be communicated to appropriate personnel.

Auditors must document any departures from GAGAS and the impact of such departures on the audit and the auditor's conclusions.

At least once every three years Internal Audit should undergo a peer review. During this time frame—every three years—Internal Audit will review the Policies and Procedures manual and update as needed.

### C.13. Audit Findings

The elements of audit findings are as follows:

**Criteria:** These are the laws, regulations, contracts, grants or other benchmarks against which performance is compared or evaluated. Criteria are the desired state of a program or operation.

**Condition:** This is the situation that exists. It is determined and documented during the audit.

**Cause:** This is the reason for the condition found. It is the factor or factors that lead to the difference between the condition that exists and the criteria.

**Effect:** This is the result or the impact of the difference between the condition and the criteria.

These elements should be clearly identified and documented in the audit work papers. Then they should be clearly shown in the audit report. Clearly means that a reasonable person reading the report or the work paper will be led to the same conclusion as the auditor.

Auditors should plan and perform procedures to develop the elements of a finding necessary to address the audit objectives. In addition, if auditors are able to sufficiently develop the elements of a finding, they should develop recommendations for corrective action if they are significant within the context of the audit objectives. A finding or set of findings is complete to the extent that the audit objectives are addressed and the report clearly relates those objectives to the elements of a finding.

As noted above, the findings should be those that will achieve audit objectives. The auditor should place findings in perspective by describing the nature and extent of issues being reported and the extent of work performed. The findings should be related to the population or number of cases examined or other measures as appropriate.

#### C.14. Exit Conference

After completion of audit field work and determination of findings, an exit conference is to be held with the auditee's representatives. The audit results are summarized and presented to the auditee at the conference. If the auditee has no disagreement with the findings, the next step will be to prepare a draft audit report. If there is disagreement with the findings, this should be discussed at the exit conference. The nature of the disagreement dictates whether further research or audit work will be necessary.

Similar to what was discussed for entrance conferences, contract preaward audits may not have an exit conference. SCAG's contract administrators may notify the consultants of the findings and any questioned costs as they prepare to negotiate the contract.

#### C.15. Draft Audit Report

After the exit conference and completion of any additional audit work, a draft audit report is prepared and a copy sent to the auditee. A response is requested from the auditee. Usually the response is requested within thirty days. This time frame may vary, depending on the nature or significance of the findings.

The results should be communicated to appropriate officials and should present sufficient, appropriate evidence to support the findings.

The draft report should describe the objectives and clearly identify the scope of the audit, including the time period audited. A narrative of the audit work and the findings and recommendations should be included. In addition, the report should include a discussion on the methodology used to address the audit objectives and how it relates to the scope of the audit (this discussion can take the

form of a “scope and methodology” section in the audit report). The findings should be described clearly so that a third party who reads the draft will understand what the facts and circumstances of the findings are. Including such information in audit reports will help to ensure the collection and assessment of audit evidence supports the findings and conclusions in the audit report.

The recommendations should flow naturally and should resolve the problem. The report should show the scope of work on internal control, any significant deficiencies in internal control and which are material weaknesses. Also the report should show instances of fraud, noncompliance with laws, regulations, contracts or grant agreements that are significant within the context of the audit objectives.

The draft report should be reviewed by management of Internal Audit before a copy is sent to the auditee. Any questions or discrepancies should be discussed and clarified before the draft report is sent to the auditee or any other outside parties.

The report should state that the audit was performed under GAGAS, if that is the case. In instances, where the audit work does not fully comply with GAGAS, the audit report will include a modified GAGAS statement.<sup>9</sup> The report also must state that use of the report is restricted to specified parties, if such is the case.

## C.16. Auditee Response

As noted above, the auditee receives a copy of the draft audit report with a request to provide a written response to the findings within a certain period of time. The auditee's response is reviewed by the Internal Audit staff. If there is a difference between the response and the auditee's comments at the exit conference, Internal Audit will attempt to reconcile the difference.

If there is some misunderstanding of the findings on the part of the auditee, Internal Audit will give the auditee the opportunity to revise the response. Otherwise, the auditee's response will be included in the final audit report, along with Internal Audit's analysis of the response.

## C.17. Final Audit Report

After the auditee has provided a response, the final audit report will be prepared. Usually the findings, discussion and recommendations will be the same as in the draft report. However, if the auditee does not concur with the report and submits credible

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<sup>9</sup>GAGAS 2.24b.

evidence that changes the findings or recommendations, Internal Audit staff is required to review and evaluate the new evidence. If further audit work is required, this should be performed. Internal Audit should not ignore any new evidence since failure to fully investigate the auditee's response could damage the credibility of the audit report.

The auditee's response should be included verbatim in the final audit report. The Internal Audit staff should analyze the response and include an analysis of the response immediately following the response. As mentioned in the preceding paragraph, any new evidence that changes materially the original findings or recommendations should be thoroughly discussed.

If an audit is terminated and a report is not issued, the auditor should document this and why the audit was terminated. If confidential information is excluded from the report, the auditor should disclose that information was omitted and the reason why. Any limitation on report distribution should be documented. Reports should be distributed to those charged with governance, the appropriate audited entity officials and to appropriate oversight bodies or those organizations requiring or arranging for the audit.

All audit reports are available to the public upon request through SCAG's Regional Council clerk. The only exceptions would be those which deal with confidential personnel matters and these would generally be available but would have confidential sections redacted.

If, after the report is issued, the auditors discover that they did not have sufficient, appropriate evidence to support the reported findings or conclusions, they should communicate in the same manner as that used to originally distribute the report to those charged with governance, the appropriate officials of the audited entity, the appropriate officials of the organizations requiring or arranging for the audits, and other known users, so that they do not continue to rely on the findings or conclusions that were not supported. If the report was previously posted to the auditors' website, it should be removed and noted on the website. The auditors should then determine if additional audit work is needed to reissue the report and if there are any revised findings or conclusions.

A copy of the final report should be cross-referenced to the work papers and kept in the work paper file.

The same procedures as outlined above should be followed with respect to contract preaward audits. The only difference is that a draft and final report are not sent to the consultant and a response from the consultant is not included in the report.

## C.18. Audit Follow-up

Generally, follow-up reviews will be made of audit report recommendations, except in the case of contract preaward audits. The follow-up activity should be directed to encouraging the implementation of recommendations, rather than finding examples of lack of action.

The follow-up activity may be either a brief, simple review of the status of recommendations or a full-blown audit of the particular area that was previously audited. The importance or materiality of the previous findings will dictate the level of follow-up work.

The follow-up activity may be considered nonaudit services. See Section C.20 for further discussion of nonaudit services.

A report should be issued describing the follow-up results. The type and size of the report will depend on whether the follow-up was only a simple review or a full audit. The report will describe the progress made on recommendations and whether further work is necessary.

## C.19. Fraud

Fraud involves obtaining something of value through willful misrepresentation. Internal Audit staff should report any detected instances of fraud in accordance with GAGAS.<sup>10</sup> The severity of the fraud detected and the response by the auditee's management dictates the manner of reporting by the Internal Audit staff.

Tips from third parties should be followed up. SCAG Internal Audit maintains a hot line to receive any tips from whistleblowers. The number is (213) 236-1979.

Audit procedures should be extended when there are indications of fraud. Auditors should exercise professional judgment so as not to interfere with potential investigations or legal proceedings.

Internal Audit staff should report known or likely fraud, noncompliance with provisions of laws, regulations, contracts, or grant agreements, or abuse directly to parties outside the audited entity in the following two circumstances:

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<sup>10</sup>GAGAS A.09-A.10.

- a. When entity management fails to satisfy legal or regulatory requirements to report such information to external parties specified in law or regulation, auditors should first communicate the failure to report such information to those charged with governance. If the audited entity still does not report this information to the specified external parties as soon as practicable after the auditors' communication with those charged with governance, then the auditors should report the information directly to the specified external parties.
- b. When entity management fails to take timely and appropriate steps to respond to known or likely fraud, noncompliance with provisions of laws, regulations, contracts, or grant agreements, or abuse that (1) is significant to the findings and conclusions and (2) involves funding received directly or indirectly from a government agency, auditors should first report management's failure to take timely and appropriate steps to those charged with governance. If the audited entity still does not take timely and appropriate steps as soon as practicable after the auditors' communication with those charged with governance, then the auditors should report the entity's failure to take timely and appropriate steps directly to the funding agency.

Internal Audit staff should also consider abuse as they perform their audits.<sup>11</sup> Abuse involves behavior that is deficient or improper when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate.

## C.20. Other Matters

Nonaudit services, which are defined as professional services other than audits or attestation engagements, are not covered by GAGAS.<sup>12</sup> Internal Audit staff should notify requestors that nonaudit services requested do not constitute audits conducted in accordance with GAGAS. Internal Audit staff should be cognizant of any threats to their independence in performing nonaudit services and should document the fact.

Management is responsible for designating an individual who has the skill, knowledge or experience to oversee the services to be performed. The Internal Auditor should document consideration of management's ability to effectively oversee nonaudit services to be performed.

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<sup>11</sup>GAGAS A.07-A.08.

<sup>12</sup>GAGAS 2.12-2.13. For examples of activities considered by GAGAS to be management responsibilities and would impair auditor independence if performed for an audited entity, see GAGAS 3.36-3.38.

If an auditor has performed nonaudit services for an entity that is a prospective auditee, the auditor should evaluate the impact of those services on independence before accepting the audit. Internal Audit staff will assess and document the impact of prior nonaudit services if they are related to a current audit. Any impairment due to nonaudit services should be disclosed in the audit report.

When performing nonaudit services not specifically prohibited, the auditor should use the conceptual framework to evaluate independence.<sup>13</sup> Prior to performing these nonaudit services, Internal Audit staff will apply the conceptual framework to evaluate independence, and will document the results of the evaluation. When preparing separate evaluations about the effectiveness of the internal control system, auditors should evaluate the management participation threat and any applied safeguards.

If any specialists are to be used, auditors must assess the qualifications and independence of the specialists and document the assessment. The auditors must identify any threats to independence and apply any necessary safeguards in the same manner as they would for auditors performing work on those audits.

## C.21. Supervision

Audit supervisors or those designated to supervise auditors must properly supervise staff. Audit supervision involves providing sufficient guidance and direction to staff assigned to the audit to address the audit objectives and follow applicable requirements, while staying informed about significant problems encountered, reviewing the work performed, and providing effective on-the-job training.

The nature and extent of the supervision of staff and the review of audit work may vary depending on a number of factors, such as the size of the audit organization, the significance of the work, and the experience of the staff.

With limited staff, the Internal Auditor function should take the necessary actions to ensure that quality audits and work are performed under GAGAS and professional standards.

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<sup>13</sup>GAGAS 3.07-3.26. Also see GAGAS Appendix II p215 for a flowchart of the *GAGAS Conceptual Framework for Independence* to assist with the application of the framework.



**SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS  
INTERNAL AUDIT DEPARTMENT  
CONTRACT PRE-AWARD AUDIT PROGRAM**

DEPT. FINANCE AUDITOR \_\_\_\_\_

RFP NUMBER \_\_\_\_\_

AUDIT PERIOD \_\_\_\_\_ DATE \_\_\_\_\_

DATE & REF  
INITIAL PAGE #

**I. PRE-AUDIT ANALYSIS**

1. Review audit request and determine contact person at consultant.
2. Hold an entrance conference with contract administrator.
  - A. Review RFP.
  - B. Review proposal.
  - C. Review cost proposal and line item budget.


**II. AUDIT REVIEW**

1. Prepare Audit Planning Memorandum.
2. Communicate with consultant's contact person(s) and request supporting documentation for Line Item Budget.
3. Review and verify the direct labor rates in the Line Item Budget. Trace and compare to actual pay rates from payroll journals, records, etc.
4. Review Overhead and Fringe Benefit rates and obtain verification to actual rates.
5. Calculate differences between actual and proposed rates and calculate questioned costs if actual rates are less than proposed rates.


**APPENDIX A**

6. Evaluate Fixed Fee and determine if Fee complies with Federal Acquisition Regulations.
7. Review Other Direct Costs. Verify calculations of Other Direct Costs (ODC).
8. Review Accounting System of Prime consultant and major subconsultants. Obtain any recent audits of indirect costs and accounting system.
9. Review Prime's financial capability and recent audited financial statements. Also review Dun & Bradstreet (D&B) reports on Prime. Evaluate the Prime's financial capability to perform the contract.


III. AUDIT FINDINGS & REPORT.

1. Prepare Evaluation Summary.
2. Summarize findings and any Questioned Costs.
3. Prepare audit report.
4. Distribute copies of audit report to CFO, SCAG Project Manager and SCAG Contract Administrator.

**SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS  
INTERNAL AUDIT DEPARTMENT  
INCURRED COST AUDIT**

INCURRED  
COST  
AUDIT

AUDITOR

AUDIT  
PERIOD

DATE

DATE &  
INITIAL

REF  
PAGE#

**I. PRE-AUDIT ANALYSIS**

- 1. Document the areas of audit.
- 2. Schedule an entrance conference with department managers.
  - A. Review prior audit reports, if applicable.
  - B. Communicate the purpose and scope of the audit.
  - C. Discuss the association's business operations.


**II. AUDIT REVIEW**

**I. Accounting System & Reporting**

- A. Review the accounting system, chart of accounts. Review accounting manual.
- B. Review and verify the internal controls of the accounting system.
- C. Review latest trial balance.
- D. Trace trial balance accounts and amounts to financial statements.
- E. Review journal entries for latest month.


**APPENDIX B**

*DATE &  
INITIAL*

*REF.  
PAGE#*

F. Review check register for the audit period. Make a random sample of checks to review and trace to paid bill files.

G. Review check stock and procedures for controlling access to blank stock.

H. Review procedures for approvals of invoices and other payments.

2. Review Fixed Assets

A. Review capitalization policies.

B. Obtain Fixed Assets files and review.

C. Reconcile amounts in files to amounts in General Ledger.

D. Select sample of charges to Fixed Asset accounts and trace to paid invoices

E. Select sample of Fixed Assets and trace to physical assets.

3. Payroll Review

A. Obtain payroll procedures and review. Examine segregation of duties and authorizations for changes in payroll.

B. Sample employee payroll records and verify payroll rates and other select information to personnel records.

C. Compare employees on payroll to actual employees on site. Review any payroll checks or stubs not handed out on site.


	<i>DATE &amp; INITIAL</i>	<i>REF. PAGE#</i>
4. Human Resources Review		
A. Examine procedures and segregation of duties.		
B. Examine sample of employee files for completeness, authorizations, pay rates, etc.		
C. Examine compliance with regulations and posting of notices.		
D. Review compensation, safety and security policies and procedures.		
E. Review development and training policies and procedures.		
5. Procurement and Contracts Review		
A. Review purchasing & procurement procedures.		
B. Review contract files for completeness and compliance with requirements & regulations.		
C. Review cost/price analysis procedures. D.		
Review contract amendment procedures.		
6. Budget Control Review.		
A. Review budget policies and procedures.		

**APPENDIX B**

*DATE &  
INITIAL*

*REF.  
PAGE#*

B. Review process of approvals.

C. Review variance comparisons & procedures.

7. Grants Management.

A. Review policies & procedures.

B. Obtain list of open grants and review.

C. Review required reports to funding agencies.

8. Overhead.

A. Review Cost Allocation Plan.

B. Review policies on direct & indirect costs.

9. Cash Management.

A. Review procedures on cash receipts.

B. Review bank statements & reconciliations.

C. Review bank agreements & transfer procedures.



**APPENDIX B**

10. IT/MIS.

- A. Obtain Organization Chart
- B. Review any steering committee.
- C. Review policies and procedures manuals.
- D. Obtain copy of physical controls & security procedures.
- E. Obtain copy of Business Continuity Plan or disaster recovery plan.
- F. Review any plan for future changes in hardware, software, etc.
- G. Review User Access policy & procedure.
- H. Review password security procedures.
- I. Review procedures for disposal of old equipment.

<i>DATE &amp; INITIAL</i>	<i>REF. PAGE#</i>

- II. Travel Expenses
  - A. Sample expense reports for Regional Council members and employees.
  - B. Review samples for compliance with Federal, State and SCAG travel regulations.
  
- 12. Project Management
  - A. Select sample of major projects for fiscal year.
  - B. Obtain files of selected sample.
  - C. Review files for compliance with regulations.
  - D. Review compliance with SCAG policies & procedures.
  - E. Trace sample of charges to paid invoices and billings to funding agencies.

III. AUDIT FINDINGS & REPORT.

- A. Summarize findings.
- B. Conduct exit conference & discuss findings with management.
- C. Prepare draft report.

<i>DATE &amp; INITIA</i>	<i>REF. PAGE#</i>
<i>L</i>	



**SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS  
INTERNAL AUDIT DEPARTMENT  
INFORMATION DOCUMENT REQUEST**

ENTITY: \_\_\_\_\_  
ADDRESS: \_\_\_\_\_  
\_\_\_\_\_

AUDITOR: \_\_\_\_\_  
AUDIT TYPE: \_\_\_\_\_  
AUDIT PERIOD: \_\_\_\_\_  
to \_\_\_\_\_

Description of Documents Requested:

- Organization Chart
- Annual Audit Report for June 30, \_\_\_\_\_
- Joint Powers Authority or other Association Agreement
- Copies of Invoices to SCAG
- 
- Payroll Tax Returns (940, 941, W-2, 1099)
- 
- General Ledger Accounts for SCAG Projects
- Chart of Accounts
- Payroll Journals/Time sheets
- Accounts Payable Distribution/Voucher Register/Purchase Journal, including schedules, reconciliations/analysis
- Accountant's Workpapers (Trial Balance and Adjusting Entries)
- Schedule of Direct Labor
- Schedule of Additions to Fixed Assets
- Documentation regarding non-taxable sale or income
- Continuing Cooperative Agreements
- All loan agreements and repayment documentation
- Schedule of Overhead Expenses, including Indirect Labor, if Applicable
- Schedule of Fringe Benefit Expenses
- Other Direct Costs
- Accounts Payable Invoices for Consultants, if Applicable
- Resale and Exempt Certificates
- RAR
- IRS Audit Adjustments
- Other States Audit Adjustments
- Bank Statements and Canceled Checks
- Analysis of Commissions/Outside Labor Expense - including name of payee and social security number
- Officer/Stockholder Income Tax Returns Form 1040
- Detail of Depreciation schedules
- Analysis of Assets Acquired for Investment Tax Credit Purposes
- Analysis of Destination Sales by State
- Miscellaneous Records Pertaining to Leasing Transactions
- Other Records as Required at time of examination

**APPENDIX C**

**SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS  
INTERNAL AUDIT  
WORKPAPER INDEX**

<b>AUDITEE: PERIOD:</b>	<b>Audit # RFP</b>	
<b>A. AUDIT REPORT</b>		<b>A. _____</b>
<b>B. ENGAGEMENT NOTICE</b>		<b>B. _____</b>
<b>C. AUDIT PROGRAM</b>		<b>C. _____</b>
<b>D. REQUEST FOR PROPOSAL (RFP)</b>		<b>D. _____</b>
<b>E. AUDIT PLANNING MEMORANDUM</b>		<b>E. _____</b>
<b>F. CONTRACT OR CCA</b>		<b>F. _____</b>
<b>G. CERTIF. OF QUALIFICATIONS &amp; INDEPENDENCE</b>		<b>G. _____</b>
<b>H. PROPOSAL</b>		<b>H. _____</b>
<b>I. DUN &amp; BRADSTREET REPORTS</b>		<b>I. _____</b>
<b>J. CORRESPONDENCE</b>		<b>J. _____</b>
<b>K. LINE ITEM BUDGETS</b>		<b>K. _____</b>
<b>L. ACCOUNTING SYSTEM</b>		<b>L. _____</b>
<b>M. PREAWARD EVALUATION SUMMARY</b>		<b>M. _____</b>
<b>N. DIRECT LABOR</b>		<b>N. _____</b>
<b>O. OVERHEAD</b>		<b>O. _____</b>
<b>P. FRINGE BENEFITS</b>		<b>P. _____</b>
<b>Q. OTHER DIRECT COSTS</b>		<b>Q. _____</b>
<b>R. AUDITEE BACKGROUND INFORMATION</b>		<b>R. _____</b>
<b>S. SUBCONTRACTOR</b>		<b>S. _____</b>
<b>T. SUBCONTRACTOR</b>		<b>T. _____</b>
<b>U. SUBCONTRACTOR</b>		<b>U. _____</b>

**APPENDIX D**

# REPORT

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**DATE:** December 14, 2015

**TO:** Audit Committee

**FROM:** Basil Panas, Chief Financial Officer, (213) 236-1817, panas@scag.ca.gov

**SUBJECT:** FY 2014-15 Preliminary External Financial Audit Report

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**RECOMMENDED ACTION:**

For Information Only – No Action Required.

**EXECUTIVE SUMMARY:**

*SCAG's external independent auditor will present the preliminary FY 2014-15 audit report.*

**STRATEGIC PLAN:**

This item supports SCAG's Strategic Plan Goal 3: Enhance the Agency's Long-Term Financial Stability and Fiscal Management.

**BACKGROUND:**

SCAG's external independent auditors, Vasquez and Company, have completed their audit of SCAG's FY 2014-15 financial statements. They will present their preliminary audit report to the Committee.

**FISCAL IMPACT:**

None.

**ATTACHMENT:**

FY 2014-15 Preliminary External Financial Audit Report.

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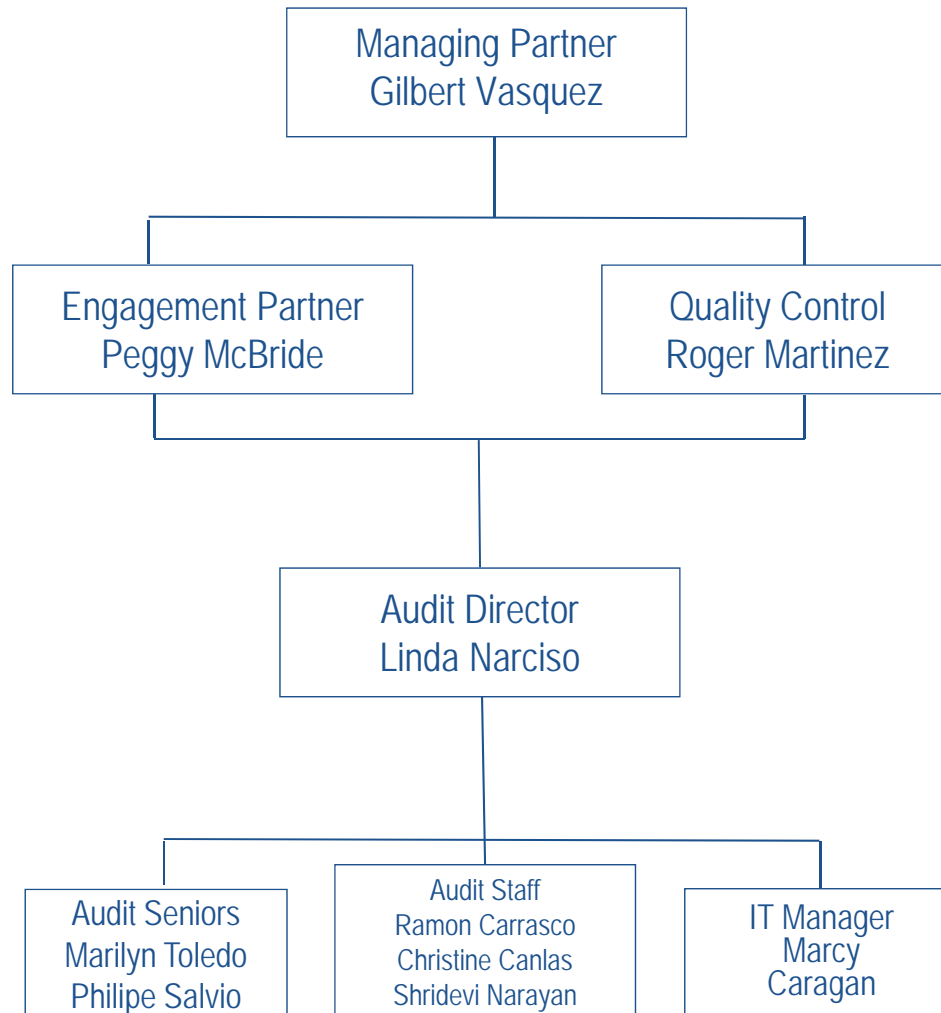
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Members AICPA Division of Firms ♦ Center for Public Company Audit Firms ♦ Registered with Public Company Accounting Oversight Board  
801 S. Grand Avenue, Suite 400, Los Angeles, CA 90017-4646 ♦ Member of the Government Finance Officers Association  
♦ (213) 873-1700 ♦ Fax (213) 996-4242 ♦ [www.vasquezcpa.com](http://www.vasquezcpa.com)  
Contact: Mr. Gilbert Vasquez, CPA ♦ Dated: December 14, 2015

## AGENDA

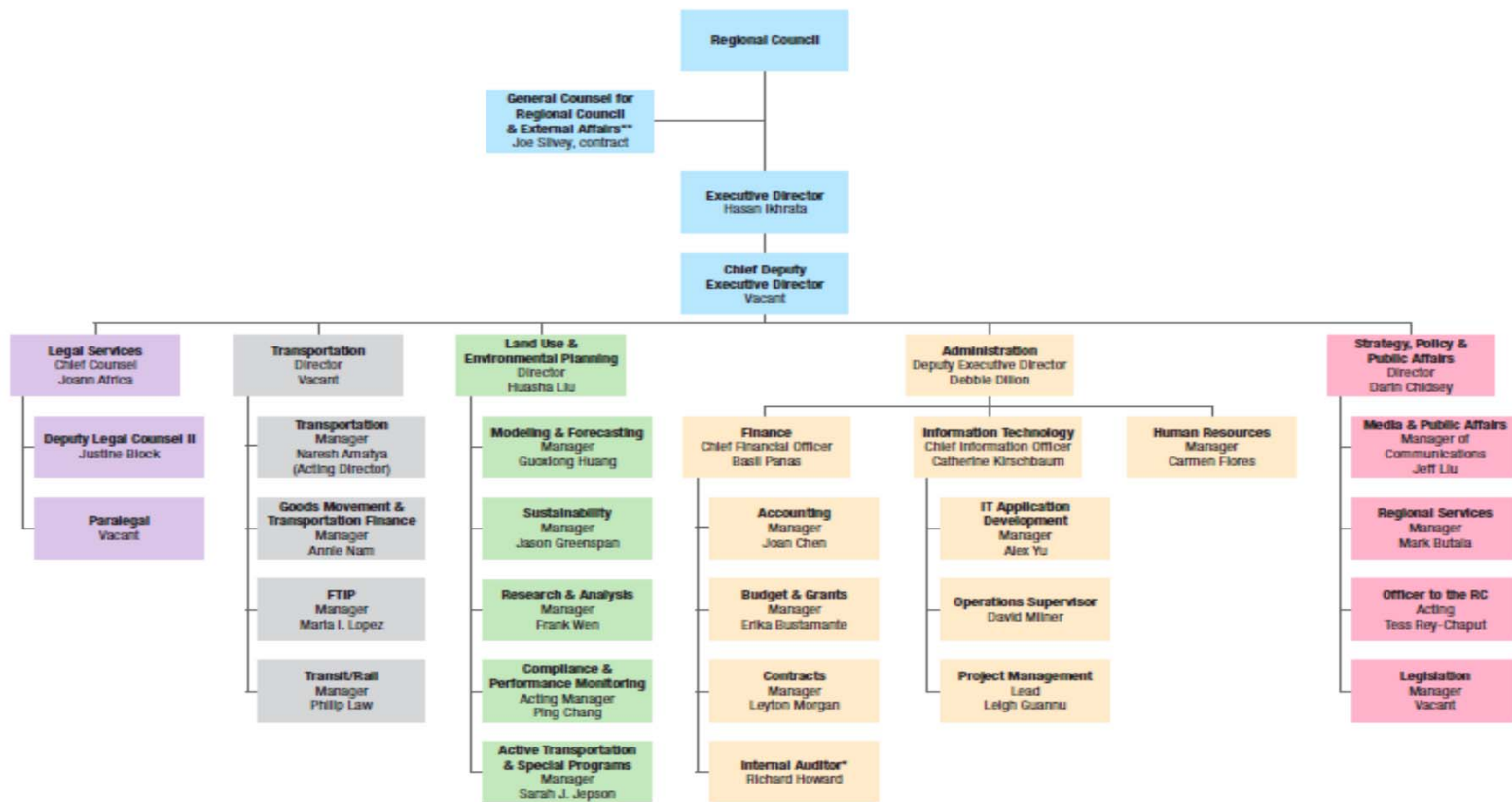
- The Audit Team
- Key SCAG Personnel - Acknowledgements
- Audit Timeline
- Summary of Audit Results
  - Financial Audit
  - Single Audit
  - SAS 114 Communication

# AUDIT TEAM



# KEY SCAG PERSONNEL - ACKNOWLEDGEMENTS

SCAG Organizational Chart December 2015

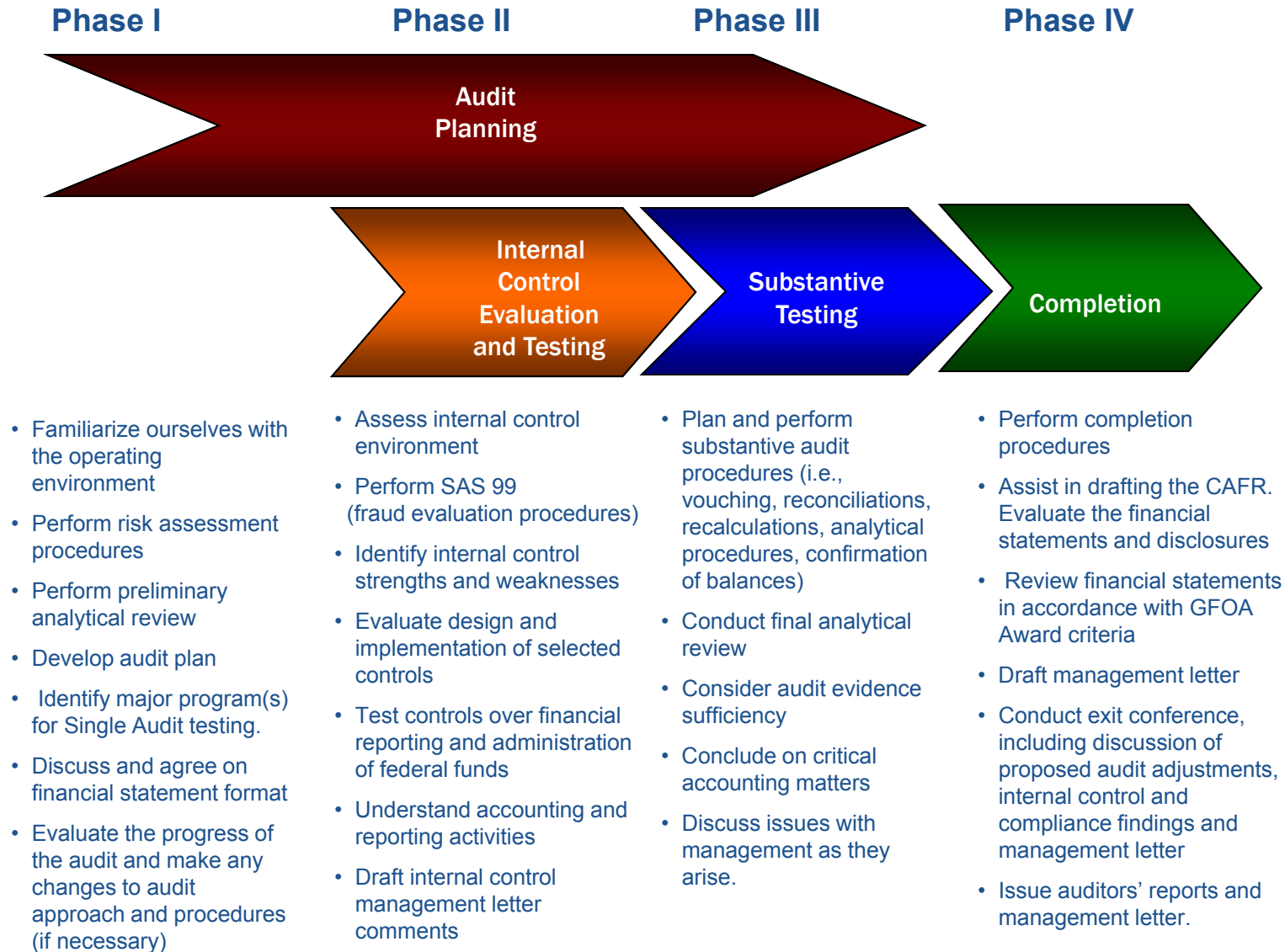


All personnel were receptive to our inquiries, helpful and professional throughout the audit process.



## AUDIT TIMELINE

Description	Responsibility	Scheduled Date
Entrance Meeting (presentation of the audit plan to the Audit Committee)	V&Co	March 17, 2015
Entrance meeting with Finance - Interim Work	V&Co/SCAG	June 1, 2015
Interim Work	V&Co	June 1 to June 12, 2015
Entrance conference - Year End	V&Co/SCAG	September 21, 2015
Year End Fieldwork	V&Co	September 21 to November 6, 2015
Exit meeting	V&Co/SCAG	November 19, 2015
Presentation to the Audit Committee	V&Co	December 14, 2015
<b>Final report</b>	V&Co	December 2015



## Summary of Audit Results

## REPORT OF INDEPENDENT AUDITORS

- **Unmodified Opinion - “Clean” Opinion on SCAG’s financial statements**
  - **Audit performed in accordance with Generally Accepted Government Auditing Standards**
  - **The financial statements fairly present, in all material respects:**
    - **The financial position**
    - **The changes in financial position**

## AUDIT AREAS OF EMPHASIS

<b>Audit Focus Area</b>	<b>Findings or Adjustments</b>
Cash and cash equivalents	None noted.
Revenue and accounts receivable	None noted.
Expenditures and accounts payable	None noted.
Capital assets	No material exceptions noted.
Adjusting journal entries	We noted no material adjustments during the FY14/15 audit.
Budgetary compliance	No instances of noncompliance noted.

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Procurement	<ul style="list-style-type: none"> <li>▪ As part of our procurement testing, we selected 8 out of the 64 contracts entered during the year and performed the following:               <ol style="list-style-type: none"> <li>1. Ensured that the RFP/RFQ was prepared and properly authorized.</li> <li>2. Ensured that the entire Proposal Review Committee signed the non-disclosure/conflict of interest form.</li> <li>3. Reviewed the Proposal Evaluation Form and Consultant Selection Form/Memo to ensure that the selection process was properly documented.</li> <li>4. Reviewed the executed contract to ensure that it was signed by the authorized representative of SCAG.</li> </ol> </li> </ul>	

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Procurement (continued)	<ol style="list-style-type: none"> <li>5. For contracts \$201k and above, we reviewed the minutes of the Regional Council (RC) to ensure that contracts were approved by the RC. For contracts below \$200k, we ensured that a Regional Council report/memo was prepared and submitted to the RC.</li> <li>6. Ensured that the contractor provided proof of insurance and Debarment and Suspension Certification. We independently verified that the vendors were not suspended or debarred parties.</li> <li>7. Determined whether a Purchase Order or Notice to Proceed was issued.</li> </ol>	No exceptions noted.

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Revenue and cash receipts	<p>We selected 11* monthly Request for Reimbursements forms (invoices) initiated by SCAG for FY14-15 and performed the following:</p> <ol style="list-style-type: none"> <li>1. Reviewed invoices and agreed amount billed to supporting detailed or summary report.</li> <li>2. Determined that the invoices were properly approved.</li> <li>3. Traced amount billed to the general ledger to determine whether the revenues were accurately recorded to the project code/account, amount and period.</li> </ol> <p><i>* In accordance with our methodology, sample size of 11 is used when testing daily or continuous controls, 2 or more controls are tested and no significant risk is identified.</i></p>	



## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Revenue and cash receipts (continued)	<ol style="list-style-type: none"> <li>4. Determined cash collections were properly recorded in the check deposit log and copies of the check and remittance data were made, stamped and retained as documentation of cash received.</li> <li>5. Agreed amount received to the bank deposit slip or bank statement and checked whether the cash receipts were deposited promptly and intact.</li> <li>6. Traced the cash receipts to the general ledger to determine that the cash receipts were accurately recorded.</li> <li>7. Checked whether the accounts receivable ledger reconciled to the general ledger.</li> </ol>	No exceptions noted.

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Cash disbursements	<p>We selected 11 expenditures incurred by SCAG for FY14-15 and performed the following:</p> <ol style="list-style-type: none"> <li>1. Verified that the supporting documentations were reviewed and properly approved.</li> <li>2. Traced the disbursements to the general ledger to determine whether the expenditures were accurately recorded to the project code/account, amount and period.</li> <li>3. Reviewed the check signatories for compliance with SCAG's policy.</li> <li>4. Ascertained that the amounts paid were net of applicable credits, discounts, or refunds.</li> </ol>	No exceptions noted.

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Payroll	<p>We selected 25 employees and various pay periods during the year and performed the following:</p> <ol style="list-style-type: none"> <li>1. Verified that the payroll transactions were properly supported by time records reviewed and approved by their supervisors.</li> <li>2. Traced the hourly rates to the approved Personnel Action Form.</li> <li>3. Obtained and reviewed the reconciliation of payroll earnings reports against the general ledger.</li> <li>4. Obtained and reviewed the actual vs. budget report and checked whether labor cost exceeded the budget.</li> <li>5. Traced the payroll to the general ledger and verified that the payroll was properly distributed, recorded and charged to the correct project/fund code.</li> </ol>	<p>We noted 1 employee's pay rate per payroll register did not agree with the authorized pay rate per Personnel Action Form (PAF). The rate per PAF is lower by \$0.40 per hour than the rate reflected in the payroll register. The rate in the GP system was updated in June 2015. The employee agreed to have a salary deduction for the overpayment.</p>

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Subrecipient Monitoring	<p>We selected three subrecipients to which SCAG provided funding during FY14-15 and performed the following:</p> <ol style="list-style-type: none"> <li>1. Reviewed copy of the contract and verified if contract specified the source of funding including the CFDA title and CFDA number.</li> <li>2. Haphazardly selected subrecipient's invoices and verified whether invoices were a) reviewed and approved; and b) adequately supported by sub-contractor's invoices and timesheets, as applicable. We also reviewed supporting documents that showed evidence of project monitoring.</li> <li>3. Obtained proof of review by the CFO of the subrecipient's financial reports.</li> </ol>	<p>We noted that the MOU between SCAG and the 3 subrecipients tested did not clearly identify the CFDA title and number.</p>

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Internal Auditor Recommendations	Reviewed the status of the 7 recommendations made by the Internal Auditor as a result of his review of SCAG's systems of internal control.	<p>We noted that the recommendations were implemented by SCAG.</p> <p>With respect to the Internal Auditor's recommendations that requests for changes of vendor address be verified as to authenticity before being processed, we recommend that SCAG maintain a log to document the requests. Currently, requests are made through emails which are deleted after 60 days.</p>

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
Fraud Considerations	<p>1. We inquired with selected members of the Audit Committee, management, and staff regarding the following:</p> <ul style="list-style-type: none"> <li>• Their knowledge of any actual fraud or suspicions of fraud.</li> <li>• Their awareness of any allegations of fraud or suspected fraud.</li> <li>• How and to what extent they assess the risk that the financial statements might be materially misstated due to fraud and the controls in place to prevent and detect it.</li> <li>• How management communicates to employees the importance of ethical behavior and appropriate business practices.</li> </ul>	

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
<p>Fraud Considerations (continued)</p>	<ul style="list-style-type: none"> <li>• The processes (programs and controls) for identifying, responding to, and monitoring fraud risks, including any:               <ul style="list-style-type: none"> <li>a. Specific fraud risks they have identified or that have been brought to their attention.</li> <li>b. Classes of transactions, account balances, or disclosures for which a fraud risk is likely to exist.</li> </ul> </li> </ul>	<p>Overall, there is a perception from those interviewed that SCAG has a strong control environment and has policies and procedures in place that would deter, prevent, and detect fraud.</p> <p>Employees are aware of the existence of the fraud hotline or they can report to the Internal Auditor or management should they become aware of fraud; employees stated that management is receptive to reports of misconduct, including fraud.</p>

## AUDIT AREAS OF EMPHASIS

Area	Procedures Performed	Findings
<p>Fraud Considerations (continued)</p>	<p>2. Reviewed the Form 700 (Statements of Economic Interests) of 3 General Assembly delegates, 6 Regional Council members and 3 key management. Ensured that the forms were filed on time and checked existence of economic interest with SCAG contractors.</p> <p>3. Requested and obtained written confirmation from selected management (Executive Director, CFO and Contracts Manager) that they had no related party transactions.</p>	<p>We noted the following:</p> <ul style="list-style-type: none"> <li>a. 2 samples selected did not have Form 700 on file.</li> <li>b. There was no list maintained by SCAG which indicated the date the Form 700 was filed.</li> </ul> <p>No related party transactions were identified.</p>



## REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND COMPLIANCE

- ❑ **Unmodified Opinion - “Clean” Opinion**
  - **Audit performed in accordance with Generally Accepted Government Auditing Standards**
  - **Material weakness and significant deficiencies – none noted**
  - **Noncompliance material to the financial statements – none noted**

## SINGLE AUDIT

### MAJOR PROGRAMS:

CFDA No. 20.505      Federal Transit Administration (Federal Expenditures \$9.9 million)  
- Transit Technical Studies  
- FTA 5304 Discretionary Grant

CFDA No. 20.526      Federal Transit Administration (Federal Expenditures \$5.1 million)  
- FTA 5339

Tested 42% of total Federal expenditures (\$35.9 million)

## SINGLE AUDIT (CONTINUED)

### **Report of Internal Control Over SCAG's Major Program**

- Material weakness and significant deficiencies – none noted
- Audit findings identified that are required to be reported in accordance with Section 510(a) of OMB A-133 – yes (subrecipient monitoring)

**Type of Auditors' Report Issued on Compliance for SCAG's major program - unmodified**

## Financial Statements

Statements of Net Position

	<u>June 30</u>		<u>Variance</u>	
	<u>2015</u>	<u>2014</u>	<u>Amount</u>	<u>Percent</u>
<b>ASSETS</b>				
Cash and cash equivalents	\$ 13,400,404	\$ 10,876,162	\$ 2,524,242	23%
Receivables:				
Federal grants	8,521,277	7,178,370	1,342,907	19%
State grants and contracts	354,714	406,331	(51,617)	-13%
Local grants and contracts	342,085	338,157	3,928	1%
Other	239,732	122,154	117,578	96%
Prepaid assets	566,517	652,453	(85,936)	-13%
Other assets	13,646	12,843	803	6%
Capital assets, net	2,251,523	2,766,741	(515,218)	-19%
Total assets	<u>25,689,898</u>	<u>22,353,211</u>	<u>3,336,687</u>	<u>15%</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>				
Pension contribution	2,299,344	-	2,299,344	100%
<b>LIABILITIES</b>				
Accounts and contracts payable	6,018,221	3,616,749	2,401,472	66%
Accrued liabilities	677,876	559,969	117,907	21%
Indirect cost recovery	971,119	1,646,051	(674,932)	-41%
Unearned revenues and advances	483,120	751,791	(268,671)	-36%
Noncurrent liabilities:				
Due within one year	771,110	773,389	(2,279)	0%
Due in more than one year	24,259,201	1,167,350	23,091,851	1978%
Total liabilities	<u>33,180,647</u>	<u>8,515,299</u>	<u>24,665,348</u>	<u>290%</u>
<b>DEFERRED OUTFLOWS OF RESOURCES</b>				
Net difference between projected and actual earnings on pension plan investments	5,470,949	-	5,470,949	100%
<b>NET POSITION</b>				
Net investment in capital assets	2,251,523	2,766,741	(515,218)	-19%
Restricted	9,857,806	8,195,221	1,662,585	20%
Unrestricted	(22,771,683)	2,875,950	(25,647,633)	-892%
Total net position	<u>\$ (10,662,354)</u>	<u>\$ 13,837,912</u>	<u>\$ (24,500,266)</u>	<u>-177%</u>

Statements of Activities

	<u>Years ended June 30</u>		<u>Variance</u>	
	<u>2015</u>	<u>2014</u>	<u>Amount</u>	<u>Percent</u>
<b>REVENUES:</b>				
Charges for services - member dues	\$ 1,871,720	\$ 1,834,522	\$ 37,198	2%
Operating grants and contributions	42,318,755	32,833,285	9,485,470	29%
Interest income	75,652	53,149	22,503	42%
Other income	407,153	378,659	28,494	8%
Total revenues	<u>44,673,280</u>	<u>35,099,615</u>	<u>9,573,665</u>	<u>27%</u>
<b>EXPENSES:</b>				
Transportation	31,710,844	23,153,109	8,557,735	37%
Aviation	585,322	303,773	281,549	93%
Environmental	1,450,795	1,403,147	47,648	3%
High speed rail	281,500	305,054	(23,554)	-8%
Housing	1,128,200	1,505,232	(377,032)	-25%
Sustainability initiatives	5,463,860	2,173,803	3,290,057	151%
Administration	1,863,292	1,986,120	(122,828)	-6%
Total expenses	<u>42,483,813</u>	<u>30,830,238</u>	<u>11,653,575</u>	<u>38%</u>
Changes in net assets	2,189,467	4,269,377	(2,079,910)	-49%
<b>NET POSITION AT BEGINNING OF YEAR, AS RESTATED</b>	<b>(12,851,821)</b>	<b>9,568,535</b>	<b>(22,420,356)</b>	<b>-234%</b>
<b>NET POSITION AT END OF YEAR</b>	<b>\$ (10,662,354)</b>	<b>\$ 13,837,912</b>	<b>\$ (24,500,266)</b>	<b>-177%</b>

## GOVERNMENTAL FUNDS – GENERAL FUND

### Balance Sheets

	June 30		Variance	
	2015	2014	Amount	Percent
<b>ASSETS</b>				
Cash and cash equivalents	\$ 13,400,404	\$ 10,876,162	\$ 2,524,242	23%
Other receivables	239,732	122,154	117,578	96%
Prepaid assets	566,517	652,453	(85,936)	-13%
Other assets	13,646	12,843	803	6%
Total assets	\$ 14,220,299	\$ 11,663,612	\$ 2,556,687	22%
<b>LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCE</b>				
<b>Liabilities</b>				
Accounts and contracts payable	\$ 1,170,466	\$ 811,196	\$ 359,270	44%
Accrued liabilities	677,876	559,969	117,907	21%
Indirect cost recovery	971,119	1,646,051	(674,932)	-41%
Due to other funds	5,676,621	3,525,610	2,151,011	100%
Unearned revenues	293,984	304,097	(10,113)	-3%
Total liabilities	8,790,066	6,846,923	1,943,143	28%
<b>Deferred inflows of resources</b>				
Unavailable revenue	133,511	37,330	96,181	258%
Total deferred inflows of resources	133,511	37,330	96,181	258%
<b>Fund balances</b>				
Nonspendable for:				
Prepaid assets	566,517	652,453	(85,936)	-13%
Unassigned	4,730,205	4,126,906	603,299	15%
Total fund balances	5,296,722	4,779,359	517,363	11%
Total liabilities, deferred inflows of resources and fund balances	\$ 14,220,299	\$ 11,663,612	\$ 2,556,687	22%

## GOVERNMENTAL FUNDS – GENERAL FUND

### Statements of Revenues, Expenditures, and Changes in Fund Balances

	Years ended June 30		Variance	
	2015	2014	Amount	Percent
<b>REVENUES:</b>				
Membership assessments				
Cities	\$ 1,484,363	\$ 1,446,376	\$ 37,987	3%
Counties	292,357	293,146	(789)	0%
Commission	95,000	95,000	-	0%
General assembly	345,195	292,090	53,105	18%
Interest and other	137,610	139,718	(2,108)	-2%
Total revenues	<u>2,354,525</u>	<u>2,266,330</u>	<u>88,195</u>	<u>4%</u>
<b>EXPENDITURES:</b>				
Transportation	9,805,386	9,789,733	15,653	0%
Housing	66,160	147,073	(80,913)	-55%
Administration	1,841,987	1,685,534	156,453	9%
Capital outlay	195,101	735,582	(540,481)	-73%
Total expenditures	<u>11,908,634</u>	<u>12,357,922</u>	<u>(449,288)</u>	<u>-4%</u>
Deficiency of revenue over expenditures	(9,554,109)	(10,091,592)	537,483	-5%
<b>OTHER FINANCING SOURCES (USES):</b>				
Transfers in	10,078,499	10,077,575	924	0%
Transfers out	(7,027)	(15,350)	8,323	-54%
Net change in fund balance	<u>517,363</u>	<u>(29,367)</u>	<u>546,730</u>	<u>-1862%</u>
<b>FUND BALANCE AT BEGINNING OF YEAR</b>	<u>4,779,359</u>	<u>4,808,726</u>	<u>(29,367)</u>	<u>-1%</u>
<b>FUND BALANCE AT END OF YEAR</b>	<u>\$ 5,296,722</u>	<u>\$ 4,779,359</u>	<u>\$ 517,363</u>	<u>11%</u>



## EFFECT OF THE GASB 68 IMPLEMENTATION

### GOVERNMENT-WIDE

Net position at June 30, 2014, as previously reported	\$ 13,818,620
Adjustment to record retroactive effect of implementing GASB Statement No. 68	<u>(26,670,441)</u>
Net position at June 30, 2014, as restated	\$ <u><u>(12,851,821)</u></u>

## SAS 114 – Auditors' Required Communication to Those Charged with Governance

## REQUIRED COMMUNICATIONS

- Management has primary responsibility for the accounting principles used, including their consistency, application, clarity and completeness. During the year, SCAG adopted the following new Statements of the Governmental Accounting Standards Board: GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statements No. 27 and 50*, and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68*.
- We are not aware of any consultations by management with other accountants about accounting or auditing matters.
- We did not encounter any difficulties with management while performing our audit procedures that require the attention of the Audit Committee and the Regional Council.
- We encountered no disagreements with management on financial accounting and reporting matters as it relates to the current year financial statements.
- SCAG's significant accounting policies are appropriate, and management has applied its policies consistently with prior periods in all material respects.

## REQUIRED COMMUNICATIONS

- No significant or unusual transactions or accounting policies in controversial or emerging areas for which there is lack of authoritative guidance or consensus were identified.
- There were no material audit adjustments required in order for the financial statements to be in conformity with GAAP.
- No significant issues were discussed, or subject to correspondence, with management prior to retention.
- No significant deficiencies or material weaknesses were identified.
- No irregularities, fraud or illegal acts or that would cause a material misstatement of the financial statements, came to our attention as a result of our audit procedures.
- SCAG will provide us with a signed copy of the management representation letter.

**QUESTIONS?**

**\*\*\***

**THANK YOU!**

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# REPORT

**DATE:** December 14, 2015  
**TO:** Audit Committee  
**FROM:** Richard Howard, Internal Auditor, (213) 236-1905, [howard@scag.ca.gov](mailto:howard@scag.ca.gov)  
**SUBJECT:** Internal Audit Status Report

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## RECOMMENDED ACTION:

For Information Only – No Action Required.

## STRATEGIC PLAN:

This item supports SCAG's Strategic Plan, Goal 3 – Enhance the Agency's Long Term Financial Stability and Fiscal Management.

## BACKGROUND:

Since the last Audit Committee meeting March 17, 2015, eleven (11) pre-award audits of contract proposals were completed.

The eleven consist of the following:

CONSULTANT	PROPOSAL AMOUNT	QUESTIONED COSTS
EPT DESIGN	\$ 196,669	\$ -
NRDC	\$ 64,545	\$ -
VARIOUS STAFFING AGENCIES		
	RATES REVIEW	
AECOM	\$ 259,605	\$ -
ELP	\$ 865,407	\$ 199,013
GENSLER		
	RATES REVIEW	
STANTEC	\$ 282,078	\$ -
ELP	\$ 198,992	\$ 23,166
AECOM	\$ 747,555	\$ 22,420
STEER DAVIES GLEAVE	\$ 495,836	\$ 14,034
ELP	\$ 199,423	\$ 23,166
TOTALS	\$3,310,110	\$ 281,799

Joshua Margraf was hired as an Assistant Internal Auditor in September 2015. Joshua was formerly with the Government Accountability Office (GAO) where he carried out performance audits of federal defense projects and programs.

# REPORT

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A peer review was performed on the Internal Audit Department during November. A separate report on the results is included in today's agenda.

In July Internal Audit conducted a survey of SCAG's consultants to determine what suggestions the consultants might have to improve SCAG's contracting process. A separate report on this survey is also included in today's agenda.

**FISCAL IMPACT:**

None.

**ATTACHMENTS:**

None.



# REPORT

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**DATE:** December 14, 2015

**TO:** Audit Committee

**FROM:** Richard Howard, Internal Auditor, (213) 236-1905, howardr@scag.ca.gov

**SUBJECT:** Vendor Survey

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## **RECOMENDED ACTION:**

For Information Only – No Action Required.

## **STRATEGIC PLAN:**

This item supports SCAG's Strategic Plan, Goal 3 – Enhance the Agency's Long Term Financial Stability and Fiscal Management.

## **BACKGROUND:**

After receiving a complaint from a consultant about SCAG's invoicing requirements and contract amendment process, SCAG decided to conduct a survey of its consultants. The survey's purpose was to determine what improvements could be made to SCAG's process by identifying any concerns or issues raised by consultants. Internal Audit developed a survey instrument and followed-up with contract administrators (CA) as appropriate. Internal Audit did not conduct an audit of SCAG's contracts process (including invoicing and contract amendments), the objectives of which would be to express an opinion of the effectiveness and efficiency of the overall process. Rather, the focus was to ascertain what, if any, concerns consultants had with SCAG's contracts process so as to help discover potential areas for improvement. Accordingly, Internal Audit does not express an opinion on the process.

## **SCOPE AND METHODOLOGY**

On July 27, 2015, Internal Audit sent a survey to a total of 92 consultants representing all open contracts as of that date. The survey consisted of nine questions related to contract instructions, including clarity of the instructions and ease of compliance with them. The survey also provided an opportunity to comment on how SCAG could improve its invoicing requirements and contract amendment process. To help ensure adequate coverage of consultants doing business with SCAG, Internal Audit developed a set of questions for CAs in order to gain insight on any concerns raised by consultants who did not respond to the survey.

## **ANALYSIS:**

The survey response rate was approximately 29 percent or 27 responses, a majority of which were positive with regard to SCAG's contract process. See Table 1 below:

# REPORT

**Table 1: Responses to Survey Questions—Generally Positive and Negative as Percentages**

Survey Question	Generally Positive	Generally Negative	No Response
1. Are SCAG's contracts easy to understand?	20 (74%)	6 (22%)	1 (4%)
2. Are SCAG's contracts adequately explained?*	22 (81%)	3 (11%)	2 (7%)
3. Are the instructions consistent?	21 (78%)	4 (15%)	2 (7%)
4a. Are contract instructions regarding billable labor rates clear?	18 (63%)	9 (33%)	1 (4%)
4b. Is it difficult to comply with those instructions?	16 (59%)	10 (37%)	1 (4%)
5a. Are the contract instructions regarding timesheets clear?	19 (70%)	7 (26%)	1 (4%)
5b. How difficult is it for you to comply with those instructions?*	19 (70%)	5 (22%)	1 (7%)
6a. The instructions restrict labor billings to only the position titles in the Line Item Budget. Are these instructions easy to understand?	17 (63%)	9 (33%)	1 (4%)
6b. How difficult is it for you to comply with these instructions?	17 (63%)	8 (30%)	2 (7%)

Source: Survey Responses and Survey Results Summary

Total number of responses to survey was 27.

\*Total may not equal 100 percent due to rounding.

Of the 27 respondents, 16 provided comments on how SCAG could improve its invoicing requirements and contract amendment process. The comments fell into three general categories: (1) the need for consistency in applying contract procedures and requirements; (2) the need for increased flexibility with contracts; and (3) the excessive burden due to the number of procedures associated with the contracts process.

A majority of the comments (approximately 69 percent of the total respondents who provided comments) discussed the need for flexibility. For instance, the comments indicated that consultants prefer to add and remove staff from a project and/or transfer funds between direct labor and other direct cost categories without requiring a contract amendment.

In comments regarding SCAG’s excessive procedures, some consultants noted that they had to prepare additional documentation not required by the contract in order for SCAG to process their invoices.

Given the relatively low response rate, Internal Audit took a random sample of consultants who did not respond to the survey and followed-up with the associated CA to determine whether the CAs had experienced any concerns or issues brought up in the survey results. See Attachment 1 for a copy of the questions sent to the CAs.

The CAs’ responses showed some similarities with survey results in that they noted consultants initially had difficulty with invoicing, particularly with providing time sheets. For instance, one consultant expressed difficulty in providing time sheets for multiple individuals when using different staff to perform work on the contract. Although SCAG allows consultants to list the position and title of staff working on a contract rather than a specific individual, it still requires timesheets for each individual performing work on the contract.

In other instances, CA responses indicated that consultants needed help with understanding and meeting time sheet requirements. According to CA responses, SCAG could do more to help educate consultants new to working with SCAG about the contract process, such as holding a vendor conference as was done in the past or directly discussing contract terms and conditions with consultants. Further, SCAG could make it

clearer at the start of a contract that consultants are not bound by estimated labor hours as long as they do not exceed the total estimated cost for direct labor when performing contract work.

Internal Audit held two meetings with Contracts and Accounting staff to discuss survey responses and determine what, if anything, SCAG could do to improve its contracts policies and procedures and to foster better relations with consultants.

Accounting representatives indicated that many of the consultants who provided negative survey responses and comments were relatively new to working with SCAG, and thus unfamiliar with SCAG's contract processes. However, the Contracts representative noted that many contract requirements are clearly described in the request for proposal (RFP) and in the contract itself, so the consultants who provided comments may have not read or fully understood the RFP and contract.

With regard to the consultants' desire for increased flexibility—specifically, shifting funds between direct cost categories—Contracts and Accounting representatives said contract amendments should still be required because the amendments help ensure that both SCAG and the consultants meet federal requirements. Since the funding for many of SCAG's contracts originates from federal grants, they may have stipulations that the consultants may not have encountered when working with non-SCAG entities.

Contracts and Accounting representatives agreed that SCAG should require contract amendments for consultants to add or change staff because amendments help ensure that SCAG receives the level of service agreed upon in the contract. For instance, if a consultant wants to switch a staff member with another individual that may not possess the same level of skills, SCAG needs to know as such a change could impact the quality of deliverables.

All Contracts and Accounting representatives believe that SCAG's requirement to amend a contract in order to transfer funds between direct cost categories and/or to change staff enhances transparency. Further, SCAG holds itself and consultants to high standards to help guarantee that contract performance quality is sustained throughout the life of the contract, and to help ensure consultants do not simply manage to the bottom line, but provide agreed-upon levels of service.

Contracts and Accounting staff did agree that certain changes in SCAG's contract processes are warranted and decided that moving forward:

- SCAG will supply successful bidders with a list of critical action items that will smooth the contract amendment and invoice approval process.
- SCAG will use alternate procedures, such as market surveys, to test Indirect Cost rates in instances where consultants cannot provide documentation to support their rates.
- SCAG will clearly communicate to consultants that only full-time regular employees can be included with Direct Labor. Sub-consultants or independent contractors must be included in Other Direct Costs.

# REPORT

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- SCAG will request that consultants bring staff members responsible for billing and other accounting functions to contract kick-off meetings so as to better inform them about SCAG processes and procedures and ensure both sides (i.e. SCAG and the consultant) share a similar understanding.
- SCAG will provide on-the-job training to Accounting staff responsible for paying consultant invoices to ensure consistency and policy compliance in requesting documentation for the invoicing of billings.
- SCAG will contact consultants to advise them that some of their recommendations had already been implemented some time ago. For example, the direct labor portion of the contract can now include a list of position titles rather than specific employee names so that some personnel changes do not trigger a contract amendment

**FISCAL IMPACT:**

None.

**ATTACHMENT:**

Follow-up Questions for CAs

**Vendor Survey Follow-up for CA**  
**10/05/2015**

SCAG sent a survey to approximately 92 consultants based on a list of open contracts as of 07/20/2015, and received 27 surveys in response. Given the response rate, we are following up with contract administrators (CA) to help better gauge if there are any potential concerns or issues brought up by consultants—see questions below.<sup>1</sup>

1. Have you experienced any issues with the consultant? If so, what types of issues?
  - How were the issues addressed?
2. What size is the consultant? How long has the consultant worked with SCAG?
3. How often have you been in contact with the consultant?
  - Is the amount of time spent communicating with the consultant typical? Why / why not?
4. To what extent has the consultant required assistance with contract terms and conditions?
  - What type of assistance did the consultant require (e.g. billable labor rates, time sheets, line item budgets, etc.)?
5. In your view, does SCAG provide enough information and explanation to consultants with regard to the contract process?
  - In your view, to what extent could SCAG improve the contract process?

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<sup>1</sup>In order to follow-up with the associated CAs to learn about their experience with the contractor and to see if they have experienced any issues/problems, we selected a sample of 12 contractors from the list of contracts used for the survey.

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Alan Wapner, San Bernardino  
Associated Governments

# 2016 Meeting Schedule Audit Committee

*All Regular Meetings of the Audit  
Committee are held on the 2<sup>nd</sup>  
Tuesday of the designated month.*

March 15, 2016

(Note: League of Cities Annual Conference is March 5-9-2016, Washington, DC)

June 14, 2016

November 15, 2016

December 13, 2016 (if needed)

The Regional Council consists of 86 elected officials representing 191 cities, six counties, six County Transportation Commissions, one representative from the Transportation Corridor Agencies, one Tribal Government representative and one representative for the Air Districts within Southern California.

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