



RON GALPERIN
CONTROLLER

June 29, 2016

Honorable Eric Garcetti, Mayor
Honorable Michael Feuer, City Attorney
Honorable Members of the Los Angeles City Council
All Angelenos

Re: Audit of Prop O Clean Water Program: Good Projects—But a Poor Financial Practice

Faced with challenges from environmental advocates and the federal government for failing to comply with the Clean Water Act, City of Los Angeles voters in 2004 agreed to pay higher property taxes to pay for bonds that would finance a series of infrastructure improvements. The improvements were intended to help clean polluted stormwater and thus limit the amount of trash, toxic chemicals and harmful bacteria entering the City's lakes, rivers and the ocean. With the support of a unanimous City Council, environmentalists, and business leaders—and with no organized opposition—Prop O passed with a 76% majority.

The good news is that Prop O's bond-funded projects have, in general, gone well. The bad news is that City taxpayers have paid millions of dollars in unnecessary interest because bonds for Prop O's long-term construction projects were issued before the money was needed to be spent. In an audit issued by my office today, we estimate that unnecessary interest payments on idle funds for Prop O projects totaled \$6.8 million.

We examined three other bond programs to see if this might be indicative of a systemic problem. We found similar patterns of bonds being issued prematurely. We estimate that unnecessary interest payments in these instances may have amounted to another \$47 million.



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Background

Prop O authorized the City to issue up to \$500 million in general obligation bonds to bring the City into compliance with the Clean Water Act and to increase flood and habitat protections and recreational opportunities. The bond measure was categorically specific in how the money was to be allocated: \$250 million for improving water quality in rivers, lakes, bays and the ocean, \$100 million for flood water reduction and for neighborhood parks that would help prevent polluted runoff and \$75 million for stormwater capture, cleanup and reuse, and another \$75 million for water conservation and drinking water protection.

My office has now audited the first ten years of this program. During those years, our audit found, 22 of 43 approved projects were completed and \$300 million spent. Auditors have told my office that the City has enough money left to complete the remaining approved projects, with construction on those projects expected to be finished by 2021.

In our examination, we found that:

- Projects are taking longer than planned and several administrative processes are in need of improvement. Notwithstanding, given the complex set of community, legal, administrative and political challenges involved in designing, selecting and building innovative projects, the audit found that the City agencies with key roles—the Bureau of Engineering, the Bureau of Sanitation and the City Administrative Office—have done a commendable job overall. Seven projects have been recognized with awards by engineering professional societies and environmental groups unaffiliated with the City.¹
- However, the City spent an unnecessary \$6.8 million to finance its Proposition O projects because it sold some of its bonds prematurely—long before the City needed the cash the bond sales would provide. Although the City got advantageous rates on the bonds, it still wound up paying unnecessary interest on idle funds to investors who purchased the bonds.

¹ The Echo Park project alone, which includes a wetlands and recreational opportunities, has won 14 local, state and national engineering and design awards including the 2014 Grand Prize for Environmental Sustainability from the American Academy of Environmental Engineers and Scientists. The South Los Angeles Wetlands Park has been honored four times by the Construction Management Association of America, the American Academy of Environmental Engineers and Scientists and other groups. The Southern California Chapter of the American Public Works Academy has honored both the Santa Monica Bay diversion project and the Machado Lake project with its best stormwater project of the year awards. Other projects have been honored as well.

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Scope of Projects

One of the largest expenditures—\$67 million—went for outfitting stormwater catch basins throughout the City with screens and other devices to stop stormwater-born trash from flowing into waterways or into man-made outflows leading to the ocean.

Other significant projects include:

- Rehabilitation of Echo Park Lake, which serves as a way station for storm water heading to the Los Angeles River, and which has become the centerpiece of a much-used, revitalized neighborhood park.
- Restoration of the ecosystem at Machado Lake in the Ken Malloy Harbor Regional Park, which is still underway. The lake serves as a waystation for stormwater heading from the Wilmington Drain—a 150-foot wide channel that collects stormwater from 19 square miles—to the Los Angeles Harbor.
- Creation of a wetlands park in South Los Angeles at a former bus and rail yard. Stormwater arriving via underground piping is treated to remove pollutants such as motor oil that have been washed away from city streets. The stormwater is then circulated through wetlands for additional natural treatments before heading to the Los Angeles River and the ocean.
- Diversion of some stormwater flows along the coast to sewers so that some pollutants can be removed at treatment plants before the stormwater is discharged to the sea.

Measuring Impacts

Some betterments in coastal water quality in recent years have been attributable to improvements in the City's separate sewer and wastewater treatment system, in accord with a federal consent decree, and some to the prolonged drought, which has meant less rain and therefore, less stormwater. However, measurements by the regional water quality control board and by the Bureau of Sanitation, suggest that Proposition O projects have also contributed significantly to the improved water quality.

Among the favorable indicators are these:

- The regional water quality control board has estimated a decline in the amount of trash entering the Los Angeles River and Ballona Creek watersheds, and ultimately the Santa Monica Bay, by more than 90%.

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- The Bureau of Sanitation has measured declines in stormwater-born bacteria entering the Santa Monica Bay. One study showed the number of summertime exceedances of Clean Water Act standards dropped from nearly 350 in 2005 to 60 in 2010. In 2013, the Bureau of Sanitation reported a 90 percent reduction in bacteria during wet weather as well as dry.

The audit suggests that more definitive measures be developed.

Financial Practices

The largest problem we turned up came into focus when we noticed what seemed to be large balances in Prop O accounts. Our inquiries suggested that bonds for long-term Prop O construction projects were being issued prematurely. Ultimately, we concluded that this mis-timing left taxpayers paying unnecessary interest on borrowed funds. In the case of Prop O, we estimate that these unnecessary interest payments totaled \$6.8 million. In an attempt to determine if this was a systemic problem, we looked at the history of account balances in other bond programs begun in the last 16 years that were outside the scope of the Prop O audit. We found what appears to have been the same pattern of premature bond issuances, with the result that the bond funds held excess cash. We estimated that City taxpayers may have paid as much as \$47 million in excess interest as a result.

How the Losses Broke Down

In addition to the \$6.8 million in Proposition O, we estimated that taxpayers paid excess interest of roughly:

- \$22.6 million in the case of Proposition F bonds, authorized by voters in 2000 to pay for fire and paramedic facilities and animal shelters.
- \$18.1 million in the case of Proposition Q, approved by voters in 2002 to pay for emergency communications and police facilities.
- And \$6.4 million in the case of Solid Waste Resource Revenue Bonds, authorized by the City Council, beginning in 2005. to finance refuse collection and disposal facilities.

Our Recommendations

Since identifying this issue we have begun conversations with the City Administrative Officer, whose office manages bond issuances, with the City Attorney and with the Bureau of Engineering, which estimates bond funding needs, to develop improved procedures to

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guard against bonds being issued prematurely—sometimes long before contracts are signed. City policy has been to require that a department have all cash on hand to pay for the full amount of a multi-year construction contract at the time the contract is signed.

We are pleased that the City--at our instigation--will be reexamining this practice to determine if, in the case of bond measures that have already been approved by voters, it would be truly advantageous and legally permissible to change City practice, so that the City could fund the starts of long-term projects without issuing enough bonds in advance to pay for the costs of the entire projects.

Commercial Paper

My office also examined the possibility that the City would be wise to explore seriously the use of less expensive short-term financing tools, including commercial paper, which the California Debt and Investment Advisory Commission suggests as a form of interim financing suitable for multi-year construction projects. The Commission, which provides financing guidance to local governments, says in its “California Debt Primer” that commercial paper “may be issued at the beginning of construction phases of large projects and may be retired with long-term bonds when the project is nearly complete. This ‘ramp up’ approach permits an issuer to avoid the sale of long-term bonds at the outset of the project, which might be desirable if unexpended bond proceeds were expected to be invested at a rate of return lower than the interest rate on the bonds or if the issuer did not anticipate being able to spend all of the bond proceeds within the required time frame.” The City of Los Angeles has such a program, but only for certain lease-revenue bonds—not for general obligation bonds such as Proposition O’s. Using commercial paper for general obligation bonds—as the state Treasurer’s office does— creates certain technical challenges for municipalities. However, research by my office suggests these challenges could be overcome.

Transparency

Proposition O voters were promised transparency and that promise has largely been kept. Clean water projects were to be monitored by a Citizens Oversight Advisory Committee, consisting of community leaders and subject matter experts appointed by the Mayor and the City Council president, and overseen by an Administrative Oversight Committee, comprised of the City Administrative Officer, the Chief Legislative Analyst, a representative of the Mayor’s office, a Board of Public Works Commissioner and the general manager of the Department of Water and Power. Projects were to be audited by the City Controller.

Our audit has found that this oversight process has largely worked as intended. Detailed monthly progress reports are posted on a City website at <http://lacitypropo.org/reports.php>

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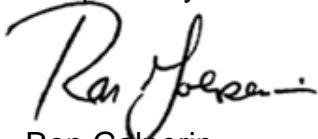
However, the oversight process has not been flawless. For example, the audit found that monthly progress reports from the Bureau of Engineering understated expenditures because the Bureau's manual procedures did not involve reconciliations with computerized records, and that the City Administrative Office was late in preparing its annual reports.

In Summary

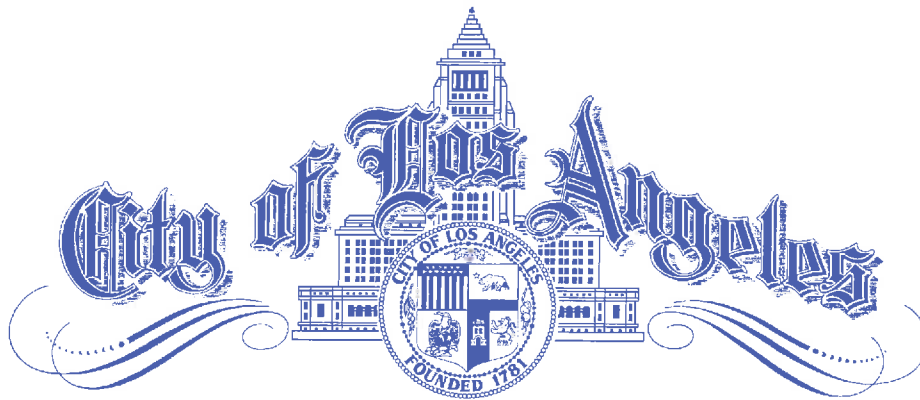
Our audit found that, although projects are taking longer than expected and certain administrative practices are in need of improvement, the performance of City agencies has been mostly positive.

The City must, however, address financial practices that we estimate cost taxpayers an unnecessary \$6.8 million in the case of Proposition O and up to an additional \$47 million on other bond projects in recent years.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Ron Galperin". The signature is written in a cursive, flowing style.

Ron Galperin
CITY CONTROLLER



RON GALPERIN
CONTROLLER

June 29, 2016

Gary Lee Moore, PE, ENV SP City Engineer
Department of Public Works – Bureau of Engineering
1149 S. Broadway, Suite 700
Los Angeles, CA 90015

Dear Mr. Moore:

Enclosed is the final report of the “Audit of Proposition O – Clean Water Projects.” A draft of this report was previously provided to the Bureau of Engineering and discussed in February 2016; comments provided by your staff were evaluated and considered prior to finalizing this report. In addition, the Bureau’s formal response and action plan related to the recommendations addressed to the Bureau of Engineering is included in Appendix IV of the report.

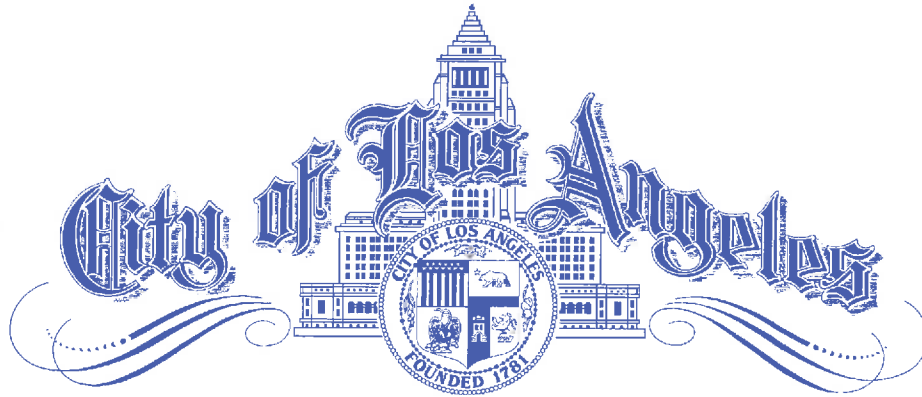
If you have any questions or comments, please contact me at siri.khalsa@lacity.org or (213) 978-7391.

Sincerely,

SIRI A. KHALSA, CPA
Interim Director of Auditing

Enclosure

cc: Kevin James, President, Board of Public Works
Kenneth Redd, PE, Deputy City Engineer
Ana Guerrero, Chief of Staff, Office of the Mayor
Sharon Tso, Chief Legislative Analyst
Holly L. Wolcott, City Clerk
Independent City Auditors



RON GALPERIN
CONTROLLER

June 29, 2016

Enrique C. Zalvidar, Director
Department of Public Works – Bureau of Sanitation
1149 S. Broadway, Suite 900
Los Angeles, CA 90015

Dear Mr. Zalvidar:

Enclosed is the final report of the “Audit of Proposition O – Clean Water Projects.” A draft of this report was previously provided to the Bureau of Sanitation and discussed in February 2016; comments provided by your staff were evaluated and considered prior to finalizing this report. In addition, the Bureau’s formal response and action plan related to the recommendations addressed to the Bureau of Sanitation is included in Appendix IV of the report.

If you have any questions or comments, please contact me at siri.khalsa@lacity.org or (213) 978-7391.

Sincerely,

SIRI A. KHALSA, CPA
Interim Director of Auditing

Enclosure

cc: Kevin James, President, Board of Public Works
Adel Hagekhalil, Assistant Director
Ana Guerrero, Chief of Staff, Office of the Mayor
Sharon Tso, Chief Legislative Analyst
Holly L. Wolcott, City Clerk
Independent City Auditors



RON GALPERIN
CONTROLLER

June 29, 2016

Miguel A. Santana, City Administrative Officer
Office of the City Administrative Officer
200 N. Main Street, Suite 1500
Los Angeles, CA 90012

Dear Mr. Santana:

Enclosed is the final report of the "Audit of Proposition O – Clean Water Projects." A draft of this report was previously provided to the Office of the City Administrative Officer and discussed in February 2016; comments provided by your staff were evaluated and considered prior to finalizing this report. In addition, your Office's formal response and action plan related to the recommendations addressed to the CAO is included in Appendix IV of the report.

If you have any questions or comments, please contact me at siri.khalsa@lacity.org or (213) 978-7391.

Sincerely,

SIRI A. KHALSA, CPA
Interim Director of Auditing

Enclosure

cc: Patricia J. Huber, Assistant City Administrative Officer
Ana Guerrero, Chief of Staff, Office of the Mayor
Sharon Tso, Chief Legislative Analyst
Holly L. Wolcott, City Clerk
Independent City Auditors



Crowe Horwath LLP
Independent Member Crowe Horwath International
15233 Ventura Boulevard, Ninth Floor
Sherman Oaks, California 91403-2250
Tel 818.501.5200
Fax 818.907.9632
www.crowehorwath.com

June 29, 2016

Mr. Ron Galperin
Controller
Office of the Los Angeles City Controller
200 North Main Street, Suite 300
Los Angeles, California 90012

Subject: Task Order No. 15-002-0-10 – Audit of Proposition O Projects

Dear Mr. Galperin:

Crowe is pleased to submit our final report, Audit of Proposition O Projects. This report was prepared in response to your office's request for an evaluation of Proposition O – Clean Water Bond, passed by voters of the City of Los Angeles in November 2004. The primary objective of the audit was to ensure that Prop O bond funds are being properly accounted for and that expenditures incurred were being properly supported and met Prop O eligibility requirements.

Thank you for providing our firm with the opportunity to prepare this report for the City of Los Angeles. Upon your request, we are available to present the report to the City Council or other City officials and to respond to any questions about this report from you and your staff.

Sincerely,

A handwritten signature in blue ink, appearing to read "Bert Nuehring".

Bert Nuehring, CPA
Partner
Bert.Nuehring@crowehorwath.com

Attachments

A U D I T

City of Los Angeles Audit of Proposition O Projects

June 29, 2016



RON | GALPERIN

Los Angeles City Controller

LAController.org



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SUMMARY

In November 2004, Los Angeles voters overwhelmingly supported Proposition O (Prop O), authorizing the City to issue \$500 million in General Obligation Bonds (GO Bonds) for projects that clean up polluted storm water and bacteria in the City's rivers, lakes, beaches, and ocean. The goals of Prop O projects are to protect public health, improve water quality, conserve water, and reduce flooding. A key driver in the passage of Prop O was the need for the City to meet federal Clean Water Act (CWA) requirements. City waterways, including the Los Angeles River, Ballona Creek, Santa Monica Bay, Marina Del Rey Harbor, and Cabrillo Beach were not in compliance with federal water quality requirements for trash, bacteria, and water toxins.

Prop O implementation is led by the Bureau of Engineering (BOE), Bureau of Sanitation (LASAN), and City Administrative Office (CAO), supported by a Citizens Oversight Advisory Committee (COAC) and an Administrative Oversight Committee (AOC). To date, the City has authorized five bond sales, totaling \$439.5 million; as of December 2014 there were 43 approved projects with a total budget of \$550.1 million which will utilize \$482.3 million in Prop O funds (the difference was provided by other funding sources).

Ten years into implementation, the Prop O program has \$60.5 million in bond sales remaining, over twenty projects to be completed, and over \$144 million in unspent bond funds (as of May 31, 2015). There are several potential projects that are not yet selected or approved, and it will likely take at least four to five more years, through 2020, to spend the remaining Prop O funds based on current project timelines. Due to the innovative nature of Prop O projects full implementation has taken longer than expected. Prop O differed significantly from the City's other bond-funded capital projects, such as animal shelters and fire stations (Prop F); or police and emergency operations facilities (Prop Q), as it was not used to fund "brick and mortar" buildings. Prop O funded a wide variety of capital projects ranging from habitat improvements, to catch basins, to stormwater diversion and treatment, and construction of best management practices aimed to improve and protect Los Angeles' water quality.

This audit provided an opportunity to verify that the program is meeting Prop O requirements, and to identify areas that should be improved for the remaining years of project implementation.

The bond measure specified that "projects will be audited periodically by the City Controller". This audit focused on whether Prop O bond funds were being properly accounted for and whether expenditures incurred were properly supported and met Prop O eligibility requirements. The scope of the audit was from program inception (November 2004) through December 31, 2014. The

audit primarily focused on a transaction-level review of seven projects selected through a risk assessment; however, the audit also analyzed bond transactions and assessed the governance structure and reasons for inactive and canceled projects, and evaluated processes to capture and report costs, including general program costs not charged to specific projects. The City departments included in the scope of this audit include BOE, LASAN, CAO, Bureau of Contract Administration (BCA), and the Department of Public Works' Office of Accounting.

I. Overall Assessment

Projects funded by Prop O will make a positive impact on the City by directly supporting compliance with Clean Water Act requirements, improving water quality and conservation, reducing flooding, protecting public health, and providing educational, recreational, and community benefits. Approximately two-thirds of bond funding directly addresses Clean Water Act compliance, a key measure of a high quality project outcome. The BOE, LASAN, and CAO, along with the oversight and advisory committees, have generally done a commendable job in implementing an innovative and unique bond program.

The audit findings identified relate to program management, project costs, project oversight and monitoring, and contract conditions. These findings should be considered relative to the improvements in water quality that the program has achieved.

The audit found that the program has had challenges in completing projects and expending bond funds, according to the originally envisioned timeframes. The large balance in unexpended bond funds has resulted in, conservatively, \$1.36 million per year in unnecessary interest expenses to the City for each of the last five years, totaling approximately \$6.8 million through FY 2015. The audit also identified some internal control weaknesses related to reporting, consultant billing, and monitoring. Several of these process control issues extend beyond Prop O to other Department of Public Works' construction projects.

II. Key Points

Prop O's large balance of unexpended bond funds has cost the City approximately \$1.36 million per year in interest expense.

Program Management

The program incurs an interest rate expense on each bond issuance. In approving the bond measure, voters indicated their support of this expense to meet the intended goals of Prop O. However, the City is accruing interest rate expense without the expected project benefits. Given the timing of bond issuance, project development, and construction, it is expected that a program such as Prop O would maintain a reasonable balance of available funds. However, even after subtracting outstanding encumbrances from the year end cash balances, the five funds still had an average of \$171 million in "available funds" for the periods FY 2010 through FY 2015.

LASAN's project scoring methodology evolved over time.

Project scoring criteria were not fully developed at the start of the program, and evolved over time. LASAN did not consistently document those changes, making it difficult to determine whether eligibility criteria were followed for some projects. Auditors concluded that the City followed appropriate project selection and approval processes for projects, based on criteria in place at the time.

Comprehensive tracking of optimization efforts and related costs is necessary.

For Prop O projects, the optimization phase is a period in which the project’s physical, chemical, and biological characteristics are assessed, the balance between hydraulic, vegetation, and treatment elements optimized, and proper operation and maintenance (O&M) protocols established that will allow for sustainable operation for each Prop O water quality protection project. As optimization activities are considered an “improvement of real property”, they are an allowable use of funds in accordance with bond covenants. LASA and CAO have taken steps to ensure Prop O bond funds are properly used for optimization expenditures, but should develop a more comprehensive tracking and reporting mechanism for optimization expenditures as projects move from the optimization phase to operations and maintenance.

BOE did not have a system in place to validate consultant hours and rates

Project Costs

BOE utilizes pre-qualified consultants for Prop O project pre-design and design work. Consultant billings are to be based on actual cost. BOE establishes overhead rates at the time the Master Services Agreements are executed. The consultant agreements allow for the payroll costs, plus the overhead multiplier and profit mark-up, to be included on hours worked if such overhead hours are paid, but not for uncompensated overtime.

BOE did not have a process to validate consultant hours, overtime hours and rates. As a result, BOE paid selected consultants for hours worked that were not subsequently paid to the employees. Although the amount of non-verified payment for hours worked was not material, the lack of review process applies beyond Prop O to other Department of Public Works (Department) construction projects that utilize pre-qualified contracts for consultants and sub-consultants.

Improving codes for time reporting will support accuracy of labor costs by project phase

Strong internal controls require adequate supporting documentation be developed and maintained to ensure project charges are recorded to the proper phases, and reported to the governing bodies. LASAN, and BCA did not utilize clear timesheet task and subtask codes, making it difficult to determine if internal labor project costs were categorized to the proper Prop O project phase.

BOE's contract provisions did not provide independence between parties for a unit price contract.

Project Oversight and Monitoring

For unit price contracts, strong internal controls require independence between parties to ensure an independent evaluation of quantities (usually performed by a professional registered surveyor) for which a prime contractor is paid. A professional bathymetric surveyor hired to verify quantities for a unit price contract was not independent of the contractor performing work for the Lake Machado Project. The construction contract specifications stated that the survey "...shall be conducted by a registered land surveyor in the State of California whose work is procured and paid for by the CONTRACTOR". In accordance with the contract, the prime contractor procured and paid for a professional registered land surveyor. There is the potential that lack of independence could lead to contractors' overcharging for measured quantities.

LASAN has been slow to report on project outcomes.

The projects funded by Prop O make a positive impact on the City by directly supporting compliance with Clean Water Act requirements, improving water quality and conservation, reducing flooding, protecting public health, and providing educational, recreational, and community benefits. However, LASAN has been slow to report on interim or final project outcomes, making it difficult to measure project effectiveness and compliance with bond requirements. LASAN did not have a structured approach and formal procedures to measure, monitor, and report Prop O project performance and outcomes to demonstrate if or how benefits have been achieved for funded projects.

III. Significant Recommendations

At the current rate of project expenditures and completion, it will be several years before all Prop O projects are completed. Implementing the audit recommendations could result in cost savings as well as improve project controls, management, and reporting.

Program Management

- The CAO, Controller-Operations Division, City Attorney and BOE should work together to develop improved processes that would prevent the accumulation of excess, idle cash within the City's bond Funds.
- CAO should implement procedures to ensure the CAO timely submits SB 165 reports in accordance with statute, and prepare an annual Prop O report that clearly summarizes activities, expenditures, and performance for an entire fiscal year.

Project Costs

- BOE should work with the City Attorney to review the contract language to ensure that consultants compensate their employees for actual hours worked.
- BOE should perform a "true-up" of all indirect costs calculated through each fiscal year with the updated, approved rates and include these updated amounts in monthly reporting to the governing bodies.

Project Oversight and Monitoring

- BOE should separately procure an independent firm prior to when the work begins, for projects requiring the expertise of a professionally designated party to verify unit price, quantity, and payment.
- LASAN should develop and regularly report project-specific and overall Prop O performance metrics.

IV. Review of the Report

A draft of this report was provided to BOE, LASAN and the CAO. We met with each of those Departments at separate exit conferences (BOE on February 4, 2016; CAO on February 9, 2016, and LASAN on February 25, 2016). We

considered managements' comments and additional information that was provided as we finalized this report.

A revised report was provided to each respective entity on April 1, 2016, requesting a formal response and Action Plan to implement the recommendations addressed to that entity. These are included as Appendix IV.

BOE

BOE agreed with six of the eight recommendations (Recommendations 3.1; 7.1; 8.1; 9.1; 14.1; and 15.1). We now consider Recommendations 3.1 and 8.1 as Implemented, and Recommendations 7.1, 9.1, 14.1, and 15.1 as In-Progress/Partially Implemented.

In response to Recommendation 11.1, to consider establishing procedures to periodically verify consultant and sub-consultant billing rates on a sample basis, BOE indicates that they will develop a policy to review and approve billing rates at the beginning of the contract and after three years. However, this will not address the need to provide better oversight of project costs that would result from periodic verification. We encourage BOE to implement this recommendation as written. We consider Recommendation 11.1 as Not Implemented.

BOE disagreed with Recommendation 12.1 to procure an independent firm, separate from the Contractor, for projects requiring the expertise of a surveyor or other professionally designated party for unit price, quantity, and payment purchases. Lack of independence between measurement and payment in unit price contracts results in a conflict of interest. We encourage BOE to implement this recommendation.

LASAN

LASAN agreed with each of the five recommendations addressed to the Bureau (Recommendations 4.1; 5.1; 5.2; 10.1; and 13.1). Based on the response, we consider Recommendation 4.1 as Implemented, and four recommendations (5.1, 5.2, 10.1, and 13.1) as In-Progress/Partially Implemented.

CAO

The CAO indicated that they agreed with the three recommendations addressed to CAO (Recommendations 2.1; 2.2 and 5.1) and we consider all three

recommendations In-Progress/Partially Implemented. CAO provided additional context to Finding 2 regarding Program transparency. Based on this input, we agree that while the annual SB 165 reports were consistently late, CAO has worked to maintain Program transparency through numerous other reports, public meetings, and weekly communications with BOE and LASAN.

BACKGROUND

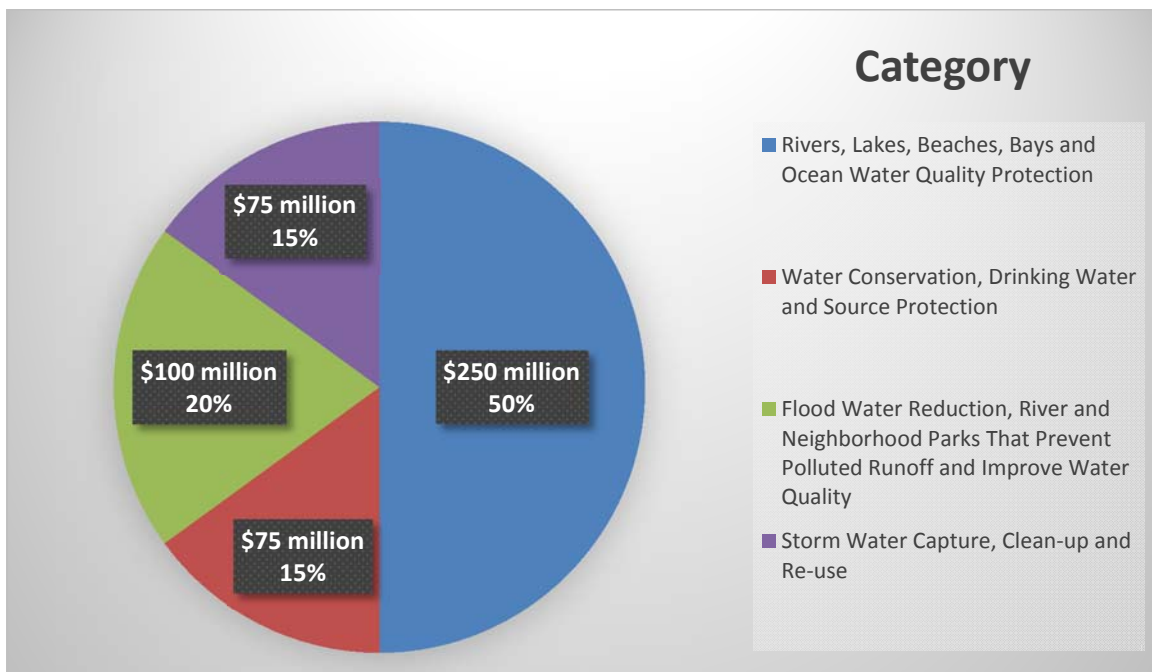
In November 2004, the voters of the City of Los Angeles, via the passage of Prop O, authorized the City to issue \$500 million in GO Bonds for projects that clean-up polluted storm water and bacteria in the City's rivers, lakes, beaches, and the ocean. The goals of the Prop O projects were to protect public health, improve water quality, conserve water, and reduce flooding. Whenever feasible, projects were to be designed:

- To provide multiple benefits and purposes including water supply, flood management, open space, habitat, and recreation benefits.
- With consideration of source control measures, leveraging of funds and collaboration with other agencies.
- To utilize a strategic adaptive management approach that incorporates assessment, feedback, adaptation, and flexibility.

A key driver in the passage of Prop O was the need for the City to meet federal Clean Water Act (CWA) requirements. City waterways, including the Los Angeles River, Ballona Creek, Santa Monica Bay, Marina Del Rey Harbor, and Cabrillo Beach were not in compliance with federal water quality requirements for trash, bacteria, and water toxins.

The \$500 million in funding was to be used on projects for one or more of the following project categories, as shown in **Exhibit 1**:

EXHIBIT 1: PROP O FUNDING BY CATEGORY



Based on the City's policies, each project must meet the following eligibility requirements:

- The project must reduce loads of pollutants to impaired waters.
- The project shall not negatively affect flood protection.
- The project shall not lead to a net loss of habitat or hardening of creeks or rivers.
- The project shall not exacerbate any existing environmental problems in the vicinity or downstream of the project.

1. Program Structure and Governance

The City developed, and has followed, a Prop O governance structure that provides a clear delineation of authority and approvals for Prop O projects and for operation of the program. The governance structure established a process whereby program activities implemented by the BOE and LASAN are reviewed and recommended or approved first by a Citizens Oversight Advisory Committee (COAC), then the Administrative Oversight Committee (AOC), followed by the City Council and Mayor.

The Council and Mayor have final authority for approving the program and individual project budgets, the specific scope of each project, the program schedule, specific scope changes for individual projects requiring overall program budget adjustments, additions and deletions to the program based on availability of funds and feasibility, and staffing levels based on identified needs and availability of funds.

Citizens Oversight Advisory Committee

Prop O required the establishment of a Citizens Oversight Advisory Committee (COAC) to monitor the Program, the projects, budgets and schedules and to report to the Mayor and City Council at least semi-annually. The committee was to consist of four members appointed by the Mayor and five appointed by the President of the City Council. At least two appointments by the Mayor and three by the President of the City Council were to be based upon the appointee's expertise and experience in clean water issues. The other four members were to be knowledgeable community representatives.

Administrative Oversight Committee

Prop O also required an Administrative Oversight Committee (AOC) to oversee and direct the Program and the projects in order to comply with approved schedules and budgets. The City Administrative Officer served as the AOC chair, and members included the Chief Legislative Analyst, a representative from the Mayor's Office, a Board of Public Works Commissioner and the General Manager of the Department of Water and Power. The AOC's responsibilities included:

- Developing and reviewing criteria for the selection of projects in consultation with the COAC per bond ordinance requirements.
- Reviewing project proposals to determine if they meet the adopted project criteria and recommending to the Council projects that meet the criteria.
- Working with the COAC in reviewing and assessing project proposals.
- Authorizing the Bureau of Sanitation Project Planning Program Manager to transmit to Council for consideration recommended project proposals.
- Overseeing, directing, and monitoring the Program and projects to ensure timely completion within approved schedules and budgets.
- Monitoring utilization and costs of City personnel, personal services contracts, expense and equipment for the projects.

Exhibit 2, on the following page, provides an overview of major Prop O activities, including project identification and selection, project delivery, and project optimization and implementation. Exhibit 2 illustrates that the City has developed and implemented an integrated and complex program implementation process that requires a high degree of communication, coordination, and accountability across the key program entities. The Monthly Reports prepared by BOE are the primary project reporting mechanisms, and provide comprehensive and transparent documentation of Prop O activities dating from August 2005 to current.

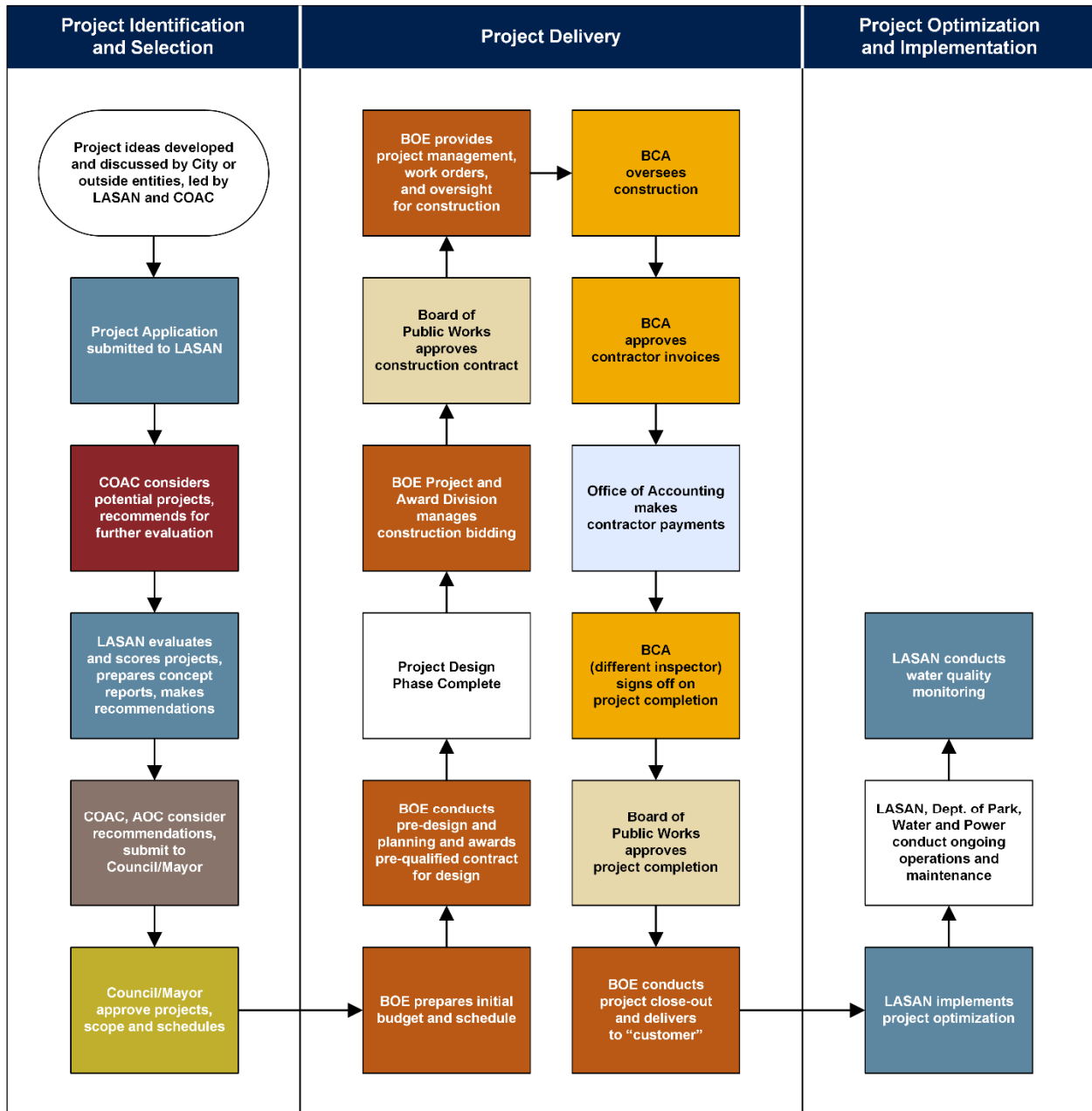
Other Requirements

Prop O also dictated the following:

- Salaries for administrators not directly involved in the Program shall be ineligible for reimbursement from bond funds.
- All bond funds shall be deposited into a special fund and can only be used for the purposes of the Program.

- The City Administrative Officer shall file an annual report on the amount of funds collected and expended and on the status of the Projects.
- Projects will be audited periodically by the City Controller.

EXHIBIT 2: OVERVIEW OF PROP O PROCESSES



More than one entity
 COAC/AOC
 Bureau of Contract Administration (BCA)

LASAN
 Council/Mayor
 Board of Public Works

COAC
 BOE
 Office of Accounting

Overall, the Proposition O governance structure and the City's implementation of that governance structure has resulted in an effective program that meets the intent of the bond measure. Projects funded by Prop O make a positive impact on the City by directly supporting compliance with Clean Water Act requirements, improving water quality and conservation, reducing flooding, protecting public health, and providing educational, recreational, and community benefits. Approximately two-thirds of bond funding directly addresses Clean Water Act compliance. The BOE, LASAN, and CAO, along with the oversight and advisory committees, have generally done a commendable job in implementing an innovative and unique bond program.

2. Overall Project and Financial Summary Data

According to the December 2014 Monthly Progress Report prepared by the BOE Prop O Bond Division, there were 43 approved projects. These projects had a total budget of \$550.1 million, utilizing \$482.3 million in Prop O funds, with the difference provided by other funding sources. \$300.7 million had been spent as of December 31, 2014.

Examples of Prop O Eligible Projects:

- Storm water cleanup, control, and diversion
- Water quality, pollution and bacteria control
- Trash capture
- Urban lakes and bay improvements
- Habitat/wetlands restoration and development
- Storm water retention facilities/parks/greenbelts
- Water conservation/reuse facilities.

Exhibit 3, on the following page, provides a complete list of projects by status as of December 31, 2014

Exhibit 3: Listing of Prop O Projects By Phase as of December 31, 2014

Pre-Design/Design			
Albion Riverside Park	\$59,885	Westchester Stormwater BMP	\$2,574,787
Aliso Creek-Limekiln Creek Restoration	\$19,823	Broadway Neighborhood Stormwater Greenway	\$373,054
Rory M. Shaw Wetlands Park	\$20,460		
Land Acquisition			
Taylor Yard River Park – Parcel G2 Land Acquisition	\$50,732		
Bid & Award			
Avalon Green Alley South	\$21,312	Temescal Canyon Park Stormwater BMP Phase II	\$492,350
Penmar Water Quality Improvement Phase II	\$124,709		
Construction			
Catch Basin Inserts & Opening Screen Covers Ph IV	\$438,783	Santa Monica Bay Low Flow Diversion Upgrade Pkg 3 Phase II	\$4,421,931
Machado Lake Ecosystem Rehabilitation	\$24,991,522	Temescal Canyon Park Stormwater BMP Phase I	\$13,651,250
Machado Lake Phase I (Wilmington Drain)	\$21,963,767		
Post-Construction			
Albion Dairy Park – Demolition & Remediation	\$6,282,828	Penmar Water Quality Improvement Phase I	\$16,886,751
Elmer Avenue Phase II: Elmer Paseo	\$745,776	Santa Monica Bay Low Flow Diversion Upgrades Pkg 3	\$12,198,102
Completed			
Albion Dairy Park – Land Acquisition	\$17,560,000	Mar Vista Recreation Center Stormwater BMP	\$4,051,496
Catch Basin Inserts and Coverings Phase I	\$14,702,886	Oros Green Street	\$198,924
Catch Basin Opening Screen Covers Phase II	\$9,630,788	Peck Park Canyon Enhancement	\$4,804,670
Catch Basin Opening Screen Covers Phase III	\$43,185,456	Rosecrans Recreation Center Stormwater Enhancements	\$2,977,701
Cesar Chavez Ground Water Improvement	\$2,527,873	Santa Monica Bay Low Flow Diversion Upgrades Pkg 1	\$4,613,088
Echo Park Lake Rehabilitation	\$36,644,308	Santa Monica Bay Low Flow Diversion Upgrades Pkg 2	\$2,032,342
Glenoaks/Sunland Stormwater Capture	\$30,988	Santa Monica Bay Low Flow Diversion Upgrades Pkg 4	\$3,892,511
Grand Blvd. Tree Wells	\$713,039	South Los Angeles Wetlands Park	\$9,843,372
Hansen Dam Wetlands Restoration	\$1,812,744	Strathern Pit Multiuse - Land Acquisition	\$8,559
Imperial Highway Sunken Median Stormwater BMP	\$1,301,724	Westminster Dog Park Stormwater BMP	\$687,888
Inner Cabrillo Beach Bacterial Water Quality Improvement	\$6,927,197	Westside Park Rainwater Irrigation	\$4,556,504
Los Angeles Zoo Parking Lot	\$6,240,455		
Inactive/Cancelled			
La Cienega/Fairfax Stormwater BMP (CANCELLED)	\$668,159	Cabrillo Paseo (CANCELLED)	

Source: December 2014 Monthly Progress Report

Exhibit 4, below, provides a summary of project expenditures by phase as of December 31, 2014. Exhibit 4 shows that a significant portion of the approved budgets for pre-design/design and construction remain to be spent for the 14 projects that are in those two phases.

EXHIBIT 4: SUMMARY OF PROP O PROJECT STATUS AS OF DECEMBER 31, 2014

Phase	Number of Projects	Approved Budget	Total Expenditures	Remaining Expenditures	Percent Remaining
Pre-Design/Design	5	\$58,198,591	\$3,048,009	\$55,150,582	95%
Land Acquisition	1	50,732	50,732	0	0%
Bid & Award	3	11,831,407	638,371	11,193,036	95%
Construction	5	166,809,378	65,467,253	\$101,342,125	61%
Post-Construction	4	37,619,308	36,113,457	\$1,505,851	4%
Completed	23	207,136,267	178,944,513	\$28,191,754	14%
Inactive/Cancelled	2	668,159	668,159	\$0	0%
Totals	43	\$482,313,842	\$284,930,494	\$197,383,348	41%

Source: December 2014 Monthly Progress Report

Note: The Program budget also included non-project specific allocations for Program consultants, Program City staff, arbitrage, and contingency. As of December 31, 2014, these budget items totaled approximately \$57 million, while total expenditures were approximately \$16 million. In addition, the Westchester Stormwater BMP project was reported as "inactive" on the December 2014 monthly status report. However, during audit fieldwork the project was reclassified as "active". The project has been reported in an "active" project phase above.

Financial Data

To date, there have been five bond sales, totaling \$439.5 million. For each bond sale, the proceeds were recorded to a different special revenue fund. **Exhibit 5**, below summarizes this data:

EXHIBIT 5: SUMMARY OF PROP O FUND NAMES, ORDINANCES, AND BOND PROCEEDS

Special Revenue Fund	Ordinance Number	Ordinance Approval Date	Bond Proceeds	Bond Proceeds Deposit Date
#16F GOB 2005A Clean Water Cleanup	No. 176839	7/28/2005	\$37,000,000	8/16/2005
#16M GOB 2006A Clean Water Cleanup	No. 177733	7/24/2006	\$8,000,000	8/10/2006 and 8/30/2006
#16Q GOB 2008A Clean Water Cleanup	No. 180090	7/30/2008	\$101,000,000	8/8/2008 and 8/20/2008
#16T GOB 2009 Clean Water Cleanup	No. 180808	7/27/2009	\$176,500,000	8/18/2009
#16V GOB 2011A Clean Water Cleanup	No. 181755	6/28/2011	\$117,000,000	8/3/2011

Source: December 2014 Monthly Progress Report

Generally every spring, BOE reports its Prop O funding needs for the following year based on project budgets as approved by the Administrative Oversight Committee (AOC). Forecasts are based on estimated project expenditures and assumes that projects will be implemented with no delays. Forecasts for land acquisition and construction contracts are made at their full cost during the period, while forecasts for pre-design and design activities are spread over the duration of the activity. The forecasted appropriation needs support a recommendation to the AOC, which then authorizes the CAO to issue bonds up to the approved amount. There have been five Prop O bond issuances since its inception, with the latest occurring in August 2011.

A significant portion of Prop O bond funds have not been expended ten years after the first bond proceeds were deposited in August 2005. **Exhibit 6**, on the next page, provides an overview of bond proceeds, interest earnings, expenditures, and remaining bond funds, by bond sale. These data illustrate

that 31% of total bond funds had not been expended or committed as of May 31, 2015.

EXHIBIT 6: SUMMARY OF PROP O BOND PROCEEDS, INTEREST, AND EXPENDITURES BY BOND FUND

Special Revenue Fund	Bond Proceeds	Interest Earnings ^a	Total Bond with Interest	Expenditures ^a (Unaudited)	Remaining Bond Funds (Unaudited)	Percent Remaining
#16F GOB 2005A	\$37,000,000	\$3,088,802	\$40,088,802	\$42,292,717	(\$2,203,915)	-5%
#16M GOB 2006A	8,000,000	897,657	8,897,657	8,452,297	445,360	5%
#16Q GOB 2008A	101,000,000	6,283,171	107,283,171	97,839,725	9,443,446	9%
#16T GOB 2009	176,500,000	11,044,318	187,544,318	136,563,279	50,981,039	27%
#16V GOB 2011A	117,000,000	4,956,108	121,956,108	37,975,048	83,981,060	69%
Total	\$439,500,000	\$26,270,056	\$465,770,056	\$323,123,066	\$142,646,990	31%

^a Interest earnings and expenditures by Bond obtained from Department of Public Works, Office of Accounting (Prop O Expenditures.xlsx); expenditures included through 5/31/2015 to incorporate current program activity. These data do not include outside funding sources.

Large Cash Balances

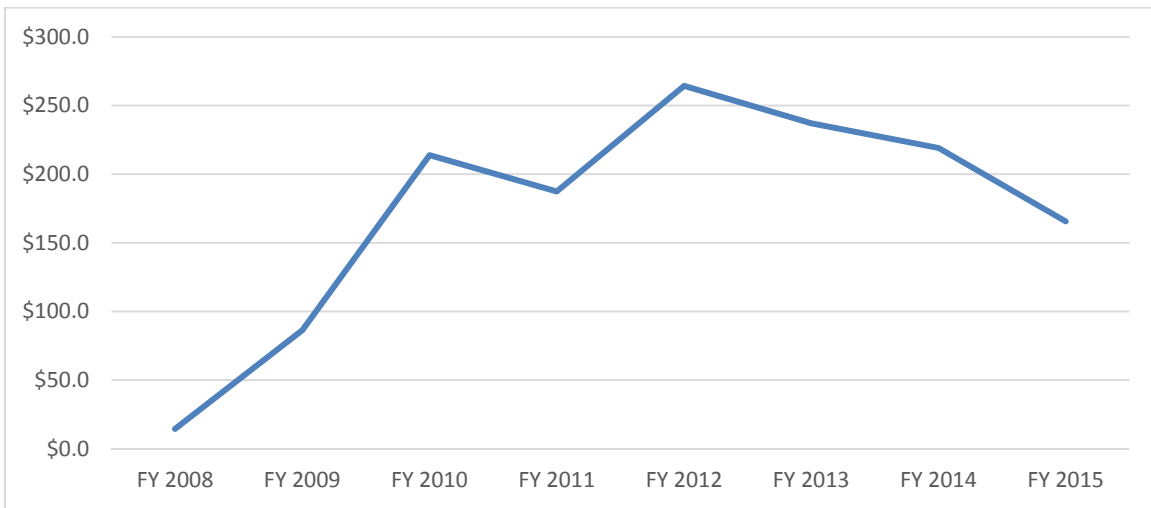
Consistent with the slow rate of expenditures, a review of Financial Management System (FMS) reports showed large cash balances at the end of each fiscal year (FY) beginning with FY 2009. As of June 30, 2008, total cash in the five funds was \$14.4 million. As of June 30, 2010, the balance had increased by 1385% to \$213.9 million.¹ The balance reached as high as \$264.3 million as of the end of FY 2012.

Exhibit 7, on the next page, shows the cash balance as of the end of each fiscal year, beginning with FY 2008. Even after subtracting outstanding

¹ Some of the increases in early years would be understandable because new projects were just being approved.

encumbrances from the year end cash balances, the five funds still had an average of \$171 million in “available funds” for the periods FY 2010 through FY 2015.

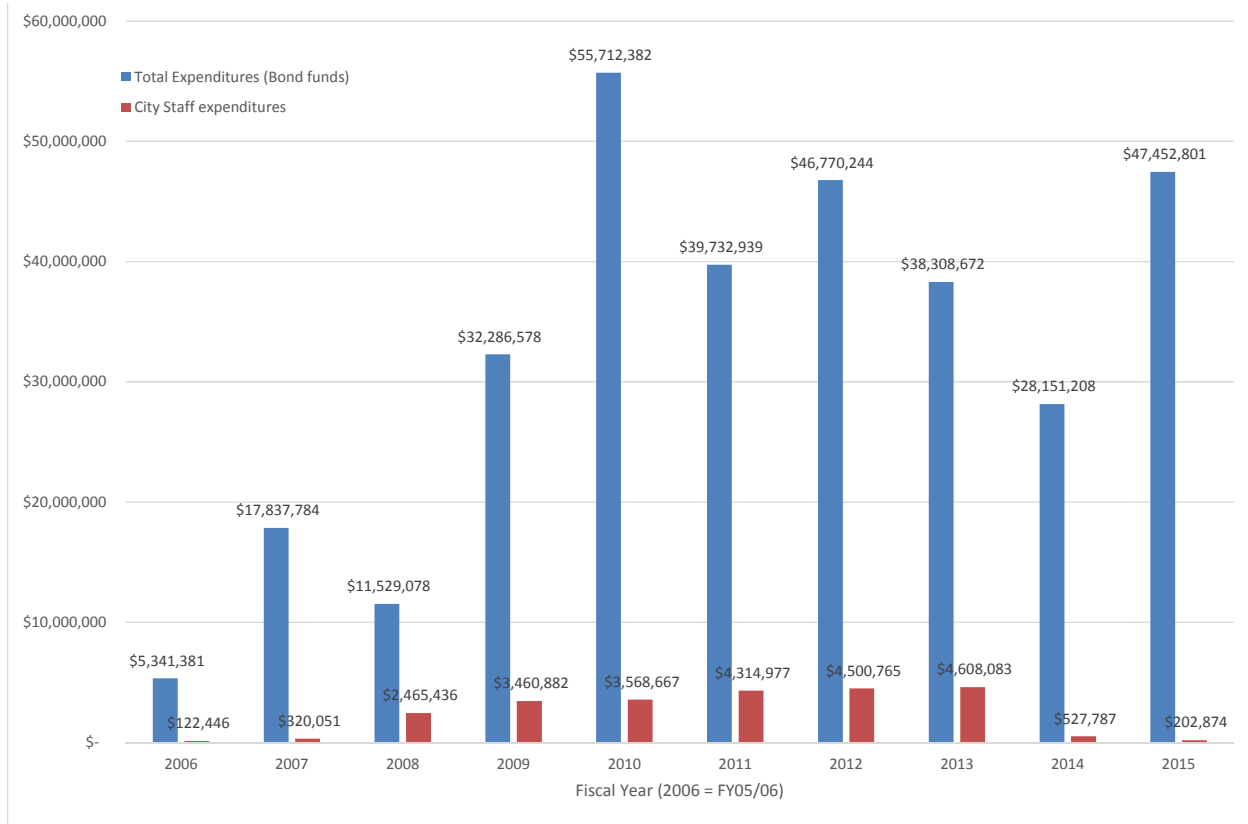
EXHIBIT 7: PROP O BOND CASH BALANCES AS OF THE END OF EACH FISCAL YEAR



An analysis of the five bond issuances disclosed that over the past six years, the City has paid an effective interest rate of approximately 3.4% on the monies received through the bond sales. However, based on a review of the City Treasurer’s Investment Reports, the City has earned only about 1.5% on invested funds during the same period. Thus, for every \$100 million in “excess cash”, the City “loses” about \$1.9 million by making debt service payments on idle funds.

Exhibit 8, on the next page, illustrates Prop O total bond expenditures by fiscal year as compared to Prop O expenditures for City staff (BOE, LASAN, BCA, Board of Public Works, and Controller (including for this audit)). Exhibit 8 illustrates an early build up in program expenditures over the first three years as projects were being developed, with increased, but not consistent, expenditures starting in 2009. Expenditures fell significantly in 2014, but increased again in 2015. With \$60.5 million in bond sales remaining, and the current annual rate of bond expenditures, it will take at least four to five more years, through fiscal year 2019 or 2020, to spend the remaining Prop O funds. Exhibit 8 also illustrates that City staff represent a small share of Prop O expenditures.

**EXHIBIT 8: PROP O BOND EXPENDITURES BY FISCAL YEAR (THROUGH 5/31/2015)
TOTAL EXPENDITURES AND CITY STAFF EXPENDITURES**



Source: Prop O Bond Expenditures.xlsx, provided by Department of Public Works, Office of Accounting (Note FY 2015 data as of May 31, 2015).

Contingency Funding

As standard operating practice, BOE builds contingencies into the preliminary budget estimate when developing the City Engineer Estimate of project costs. BOE develops contingencies based on project phases (concept report, pre-design, design, right-of-way, bid and award, construction, post-construction, and optimization). Contingencies take into account escalation/inflation of construction and other project costs. According to BOE, project contingencies are generally “reprogrammed” after the City Engineer is confident in the progress of the project and that the contingency will not be required for that particular project.

Reprogramming refers to the process of releasing the contingency to support other Prop O projects. City staff prepares a recommendation and report identifying the contingency to be released and reprogramming of the funds.

The COAC, AOC, City Council Energy and Environment Committee, City Council, and Mayor evaluate reprogramming contingencies. As with all Prop O funding decisions, the City Council and Mayor approve reprogramming of contingencies. Existing projects that appear to require additional funds are given priority for reprogramming over new projects. As of September 2015, \$97.9 million in Prop O funds have been reprogrammed from closed projects to other projects, representing 16.8 percent of original Council/Mayor approved project budgets. According to BOE, there is an estimated \$16.3 million in contingencies that could be reprogrammed as projects complete close-out. The seventeen active projects as of our audit fieldwork date have an estimated contingency of approximately \$24 million, representing 8 percent of the current budgets for those projects.

3. Selected Project Descriptions, Budgets, and Timelines

Project Descriptions

Based on a risk assessment that considered factors such as the project phase, total expenditures incurred to date, number and dollar amount of change orders, and number and dollar amount of contract amendments, the following seven projects were selected for more detailed transaction-level review.

- South Los Angeles Wetlands Park (includes Site Readiness)
- Santa Monica Bay Low Flow Diversion Upgrades, Pkg 1
- Westside Park Rainwater Irrigation
- Machado Lake - Phase I (Wilmington Drain)
- Echo Park Lake Rehabilitation
- Santa Monica Bay Low Flow Diversion Upgrades, Pkg 3
- Penmar Water Quality Improvement Phase 1

The seven selected projects represented approximately 35% of expenditures incurred from program inception through December 31, 2014. Except for assessing the governance structure, bond expenditures, reasons for inactive and canceled projects and for evaluating processes to capture and report costs, including general program costs not charged to specific projects, the audit focused on a review of these seven projects. Approved budget and expenditure figures reported below are as of December 31, 2014, unless otherwise noted.

Selected Project Descriptions

South Los Angeles Wetlands Park

Description: Construct a wetlands park at 54th St. and Avalon Blvd to improve area stormwater quality and provide recreational space for the surrounding community.

Approved Budget: \$12,378,202

Total Expenditures: \$9,843,372

Status: Completed December 2011



Santa Monica Bay Low Flow Diversion Upgrades, Pkg 1

Description: Upgrade Marquez, Bay Club, Thornton, Venice Pavilion, and Imperial Low Flow Diversion systems to divert both summer and winter dry-weather flows, in order to comply with the bacteria TMDL winter dry-weather regulations.

Approved Budget: \$4,613,088

Total Expenditures: \$4,613,088

Status: Completed July 2010



Westside Park Rainwater Irrigation

Description: Treat pollutants from on-site and off-site stormwater by installing a stormwater lift station, a subsurface irrigation system, and a dry creek with a perforated pipe for collecting and returning excess irrigation water to the existing storm drain.

Approved Budget: \$4,556,504

Total Expenditures: \$4,556,504

Status: Completed August 2010



Machado Lake - Phase I (Wilmington Drain)

Description: Install trash netting systems, install smart irrigation in landscaped areas, use biofilters or similar vegetated BMPs, and recontour and align the channel.

Approved Budget: \$21,049,911

Total Expenditures: \$21,963,767²

Status: Estimated Completion April 2016



Echo Park Lake Rehabilitation

Description: In-lake improvements, in-lake vegetation (wetlands) and habitat improvements, and parkland structural best management practices (swales), lake recirculation system, lake aeration system, relocate fountain pump house.

Approved Budget: \$45,296,789

Total Expenditures: \$36,644,308

Status: Completed September 2013



² Total expenditures includes spending to be paid from non-City agencies. The Los Angeles County Flood Control District (LAFCD) is contributing \$8.1 million to the Wilmington Drain project. The BOE expects receipt of the \$8.1 million from LAFCD in December 2015. At this time, actual Prop O Wilmington Drain expenditures will be reduced by \$8.1 million to approximately \$14 million.

Santa Monica Bay Low Flow Diversion Upgrades, Pkg 3

Description: Construct a relief sewer (CIRS) to the Coastal Interceptor Sewer in order to comply with the bacteria TMDL winter dry-weather regulations.

Approved Budget: \$14,079,108

Total Expenditures: \$12,604,684³

Status: Completed October 2012



Penmar Water Quality Improvement Phase I

Description: Capture & treat dry/wet weather runoff. Dry weather runoff to be diverted to sanitary sewer for treatment. Wet weather runoff to be diverted to the underground storage tank for discharge to sanitary sewer.

Approved Budget: \$17,754,800

Total Expenditures: \$16,886,751

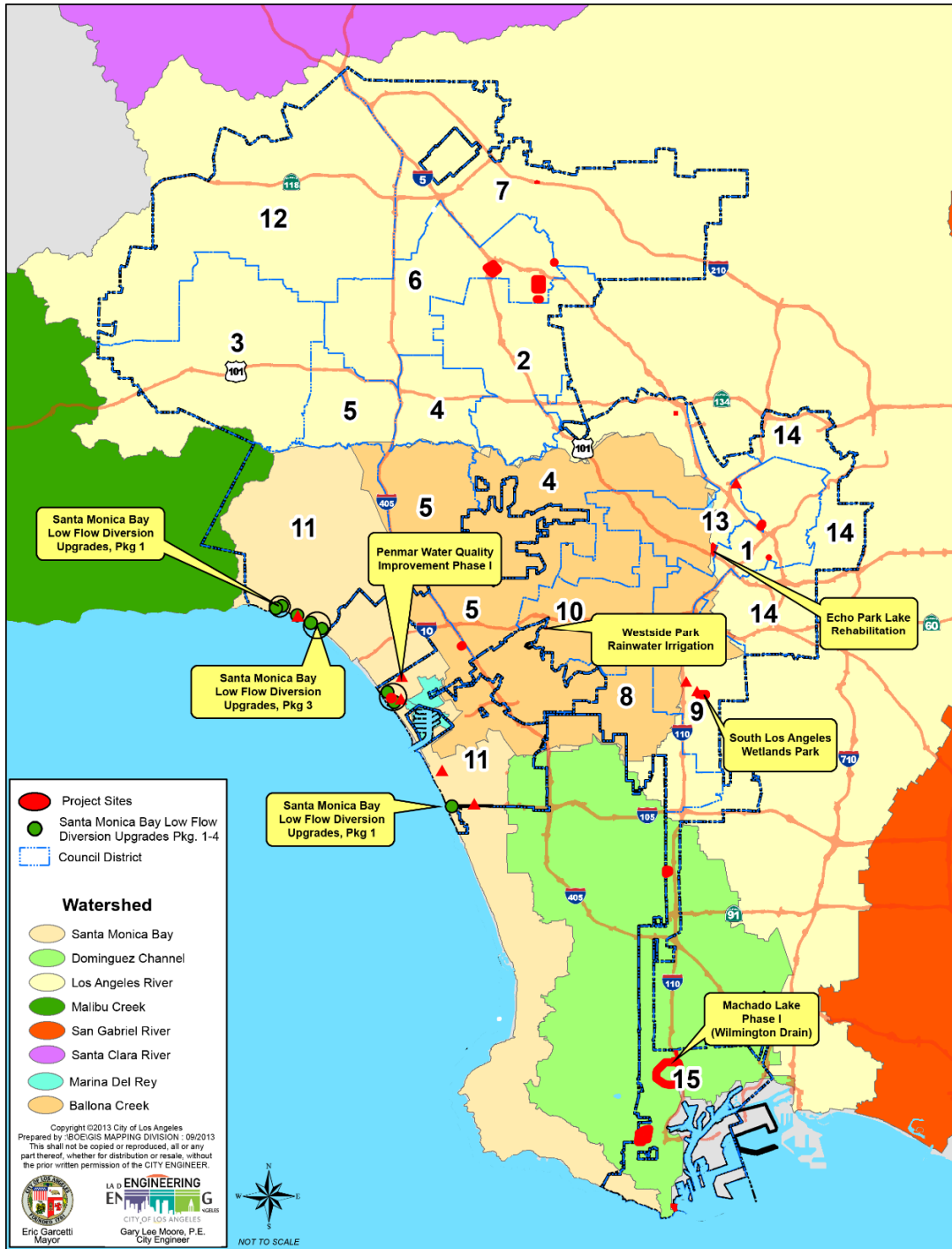
Status: Completed December 2013



³ Expenditures as of June 30, 2015. While the project is complete, the project incurred expenditures for right of ways in June 2015.

Exhibit 9, below, identifies each selected project's geographical location:

EXHIBIT 9: SELECTED PROJECTS MAP



Prop O Project Budget Development

Prop O projects cover a wide variety of infrastructure components, including both traditional aspects such as catch basins, berms, and dams, and untraditional aspects such as wetland and plantings. As a result, there was limited prior experience regarding project budgets. LASAN and BOE developed a multi-step approach to project budgeting that has generally been conservative.

Prior to project approval, LASAN prepares a Concept Report that includes a preliminary cost estimate based on the scope elements. These preliminary costs are determined by LASAN staff and LASAN engineering consultants based on market prices in the Los Angeles area, required quantities of project components, and standard price and contingency estimates. Costs are broken down by unit prices (cubic yard, square foot, number of units, lump sum, etc.) for specific project components such as sediment removal, grading and compacting, storm drains, excavation, backfill, filters, irrigation systems, plants, and aeration systems. The preliminary cost estimate identifies costs specific to water quality improvements, other beneficial improvements, and contingencies.

BOE reviews LASAN's preliminary budget and develops contingencies. BOE evaluates the data supporting the cost estimate, and adds estimating contingencies, escalation/inflation contingencies, and construction contingencies. BOE also utilizes a template, adjusted based on individual project needs, to determine design and delivery (labor) costs. The delivery cost plus the preliminary construction budget becomes the total project budget.

BOE presents the total project budget to the COAC and AOC. Once the total project budget is approved by the AOC, the City Administrative Office (CAO) prepares a report to Council Committee, City Council, and the Mayor for approvals. (Any of these entities may adjust the budget).

Once the original budget has been approved by the Council and Mayor, any increases in budget must go through the same approval process. All budget increases must be justified. In the pre-design phase, the consultant evaluates alternatives to the project that still meet the project scope and budget, including assessing rough costs of the different alternatives. At the conclusion of the pre-design phase, BOE and LASAN select the best alternative. The selected project alternative must be within the total project budget, unless special budgeting circumstances allow otherwise.

In the design phase, the design consultant (professional engineers, including structural engineers and geotechnical engineers) estimate construction costs at different phases of design completion. This is standard practice in the

construction industry. For Prop O projects, there is generally a preliminary estimate, mid-term estimate, and final estimate. The timing of these estimates occurs at different points depending on the project, but might typically be at 50% design completion, 90%, and 100% completion. The Deputy City Engineer reviews this cost estimate, and signs off on the plans. BOE staff and the design consultant team use the 100% cost estimate to prepare the City Engineer Estimate of project construction costs. The City Engineer Estimate's format and grouping of major construction line items are adjusted to best meet individual project bidding and awarding needs. The 100% cost estimate is developed by a team of professional engineers and cost estimators and includes detailed information.

Bid Development

Under Section 14.2 of BOE's Project Design Manual, the lowest responsive and responsible bidder is to be awarded the construction contract. For the seven projects tested, the lowest responsive and responsible bidder was selected. The bid documents include a general project description with a schedule of work and prices. The Technical Specifications provide the project details (the Technical Specifications in the Echo Park Lake bid package were 711 pages in length). Construction contractors must meet the technical specifications within the schedule of work and prices.

For five of the seven projects tested, the construction contract award was less than the construction cost estimate. The bids selected for the 2 projects over the City's construction cost estimate were the lowest responsive and responsible bidder and were 0.74% and 2.74% higher than the estimate. In addition, all of the six completed projects had final costs lower than the original approved budget for the project, with cost savings ranging from \$2.2 million to \$39.0 million.

Exhibit 10, on the next page, provides the concept design construction and total cost estimates, the construction contract bid, the difference between the original construction estimate and the construction bid, the original approved budget, the current (final for completed projects) approved budget, and the difference between the original approved budget and the final budget for the six completed projects.

EXHIBIT 10: COMPARISON OF PROJECT COST ESTIMATES AND BUDGETS FOR SEVEN PROP O PROJECTS

Project	Concept Design Preliminary Cost Estimate (Construction Only)	Concept Design Preliminary Cost Estimate (total)	Construction Contract Bid	Construction Difference: Preliminary Construction – Construction Bid	Original Council/ Mayor Approved Budget ^a	Council/Mayor Approved Budget (as of July 2015 monthly report)	Difference Council/Mayor Approved Original Budget & Current Budget (as of April 2015 monthly report)
South LA Wetlands	\$6,200,000	\$14,665,000	\$6,370,000	(\$170,000)	\$16,678,202	\$12,378,202 (completed)	\$4,300,000
Santa Monica Bay Low Flow Diversion Upgrades^b Package 1	\$5,500,000	\$8,500,000	\$2,993,000	\$2,507,000	\$6,814,377	\$4,613,087 (completed)	\$2,201,290
Westside Park	\$4,265,821 ^c	\$6,904,589 ^c	\$2,675,964	\$1,589,857	\$6,904,589	\$4,556,504 (completed)	\$2,348,085
Machado Lake – Wilmington Drain Phase 1	\$14,383,863	\$17,942,534	\$14,490,264	(\$106,401)	\$21,049,911	\$21,049,911 (in construction)	\$0
Echo Park Lake	\$64,693,522	\$84,263,313	\$24,485,000	\$40,208,522	\$84,263,313	\$45,296,789 (completed)	\$38,966,524
Santa Monica Bay Low Flow Diversion Upgrades^b Package 3	Full upgrades budget not in Concept Report. City Council approved an increase in funding of \$31,139,028 for SMLBFD Upgrades Packages 1 to 4 on 3/16/2009, as well as a transfer of \$7 million from the Sewer Construction and Maintenance Fund.		\$8,784,278	NA	\$20,634,036	\$14,079,108 (completed)	\$6,554,928
Penmar Water Quality Improvements Phase 1	\$19,098,831	\$23,585,000	\$11,360,700	\$7,738,131	\$17,754,800	\$17,754,800 (completed)	\$0

^a From December 2014 Monthly Report

^b Santa Monica Bay Low Flow Diversion Upgrades (SMLBFD) Packages 1 to 4 not treated as separate projects for purposes of Concept Design Reports

^c From Westside Park Final Pre-design Report

City and Construction Costs by Project

Prop O project expenditures include City labor, pre-design and design consultants, construction contracts, and in some cases land acquisition. We compared City labor and construction costs to total expenditures. **Exhibit 11**, on the next page, provides a summary of total labor, construction, non-City labor (including pre-design, design, construction, and land acquisition) and total Prop O bond expenditures for the seven selected projects. City labor expenditures encompass all City staff expenditures, including public outreach,

planning, project management, and construction management. Construction expenditures include only expenditures for the construction contractor. City labor as a percent of project Prop O expenditures averaged seven percent for the selected projects, and ranged from 6 percent to 19 percent. Variation between projects was due to project variability in factors such as public outreach, design, and planning. Construction contractor costs as a percent of project Prop O expenditures for the seven projects averaged 72 percent, and ranged from 33 percent to 75 percent. Again, projects with more significant planning, outreach, and project management requirements, had lower relative construction costs. Overall, City labor and construction shares of overall project costs are consistent with industry norms.

EXHIBIT 11: PROP O EXPENDITURES BY CATEGORY FOR SELECTED PROJECTS

Project	Total City Labor Expenditures	Total Other Expenditures	Total Bond Expenditures ⁴	Percent Labor	Construction Expenditures (December 2014 Monthly Report)	Construction Cost % of Total Bond Expenditures
South LA Wetlands	\$1,825,807	\$8,003,566	\$9,829,374	19%	\$3,196,017	33%
Santa Monica Bay Low Flow Pkg 1	\$553,213	\$6,327,322	\$4,613,088	12%	\$3,199,746	69%
Westside Park	\$512,081	\$4,044,527	\$4,556,608	11%	\$2,984,142	65%
Machado Lake – Wilmington Drain (in progress)	\$1,236,087	\$20,801,064	\$22,037,151	6%	\$15,835,643	72%
Echo Park Lake	\$2,115,189	\$34,429,920	\$36,545,109	6%	\$25,970,821	71%
Santa Monica Bay Low Flow Pkg 3	\$899,981	\$10,303,976	\$12,588,102	7%	\$8,449,604	67%
Penmar Water Quality Improvements Phase 1	\$1,508,096	\$15,805,979	\$17,314,075	9%	\$12,316,360	71%
Total	\$8,650,454	\$99,716,354	\$107,483,507	8%	\$71,952,333	67%

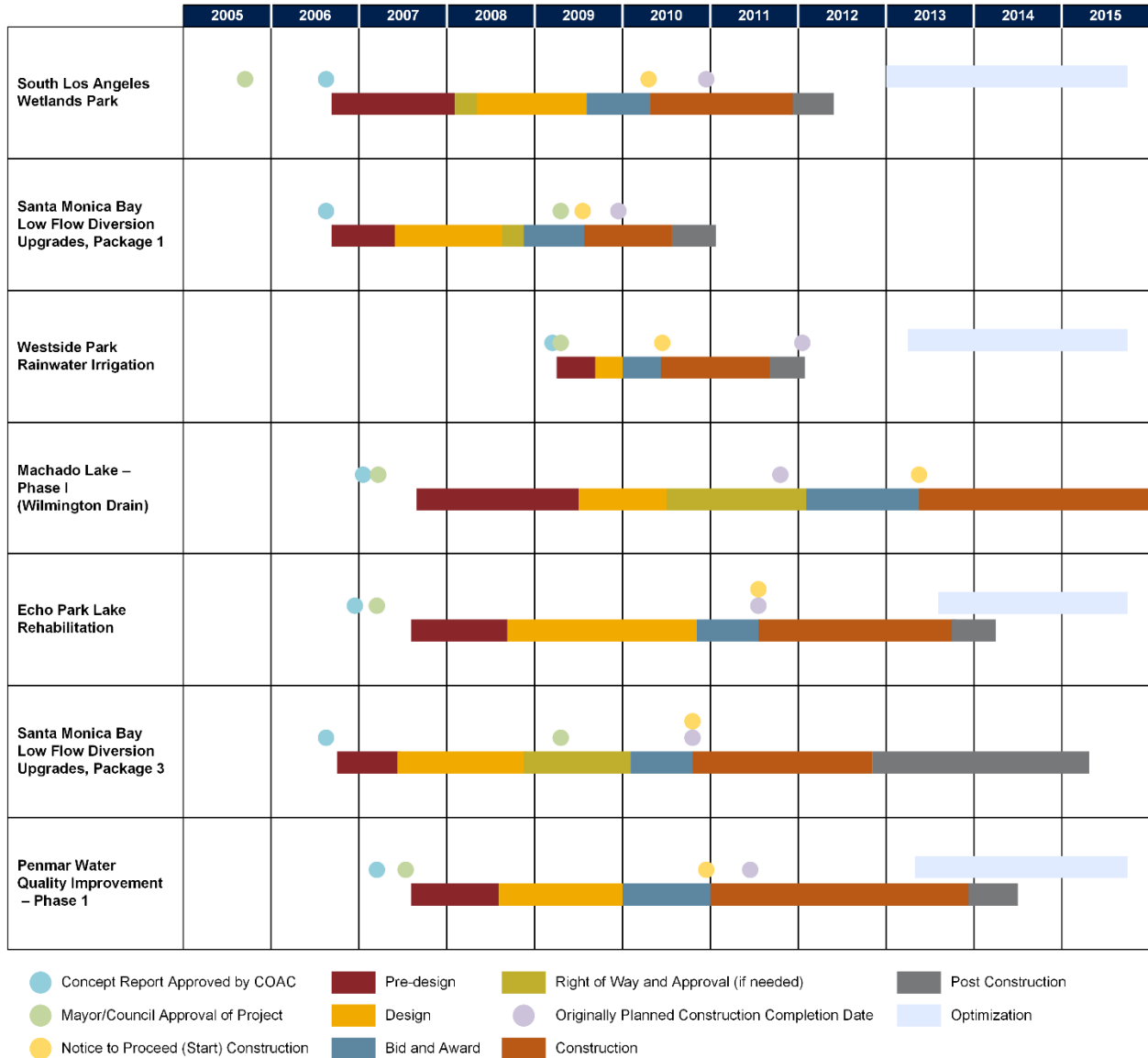
Source: Project specific MERLIN reports through December 2014 (for City labor and other expenditures), December 2014 Monthly Report for construction expenditures, and BOE reconciliation of SMLFD project expenditures (2/4/2016).

⁴ Total bond expenditures will be less than total project expenditures for projects with additional sources of funding outside of Prop O.

Project Timelines

The 43 Prop O projects, and the subset of seven selected projects, represent a wide cross section of unique, innovative, and ambitious efforts to improve water quality in the City. Designing, constructing, and completing these projects has generally taken longer than originally anticipated. This is reflected across program metrics such as the slow pace of bond expenditures, long pre-design and design phases, and construction delays. There are many valid reasons for Prop O project delays, including those that were outside the program's control, such as identification of endangered species in project sites, slow construction permitting on the Pacific Coast Highway, and lengthy land acquisition negotiations. The net result is that over ten years after passage of Prop O, the program has \$142.6 million in budgeted bond funds and \$60.5 million in unsold bond funding yet to expend. **Exhibit 12**, on the next page, provides a timeline of key project metrics for the seven selected projects. Only one project, Westside Park Rainwater Irrigation, was completed (through construction) before the originally planned construction completion date.

EXHIBIT 12: TIMELINE OF KEY PROJECT METRICS FOR THE SEVEN SELECTED PROJECTS



Objectives

This audit was conducted to assess whether Prop O bond funds were being properly accounted for and that expenditures incurred are properly supported and meet Prop O eligibility requirements. The specific objectives, phrased as questions to be answered through the audit process, are noted below.

1. Is the governance structure and oversight effective in achieving high quality project outcomes?
2. Are there adequate systems in place to capture project costs?
3. Are costs accurately reported in Monthly reports to City Council?
4. Are contracts awarded based on established eligibility criteria?
5. Are adequate processes in place to ensure contracts are awarded for reasonable amounts? Are the amounts reasonable in comparison with similar contracts for other jurisdictions and market conditions?
6. Are contract amendments and change orders properly approved?
7. Are transactions being properly recorded, and are expenditures adequately supported by documentation, including proper approval for payment?
8. Are payments to contractors in accordance with contract terms? Are costs billed allowable and reimbursable per contract and bond requirements, including costs related to change orders?
9. Are project costs appropriately categorized by phase? For completed projects, this will include assessing costs charged to "optimization" as capital project costs, rather than as operations or maintenance costs.
10. Was there a reasonable basis for cancelling projects? What is the reason for inactive projects?

Notable Accomplishments

As summarized in the December 2014 Prop O – Clean Water Bond Program Monthly Report, and listed below, four Prop O projects have been recognized by a variety of organizations for both water quality and multi-use benefits. For example, in presenting the Sustainable Stormwater Project Award to the City for Echo Park Lake Rehabilitation, the California Stormwater Quality Association noted that the project "not only captures and treats dry- and wet-weather runoff in an effort to conserve water, but it also enhances the natural habitat and recreational space in the urban core of Los Angeles⁵." Prop O projects received the following awards:

⁵ California Stormwater Quality Association 2014 Annual Report, www.casqa.org, page 9

- Elmer Avenue Green Street Project
 - National Association of Clean Water Agencies, 2011 Operations and Environmental Performance Award
- South Los Angeles Wetlands Park
 - Construction Management Association of America – Southern California Chapter, 2013 Project Achievement Award – Parks less than \$10M
 - Institute for Sustainable Infrastructure, Envision Platinum Award
 - American Council of Engineering Companies – 2014 Engineering Excellence Awards Competition, National Recognition Award
- Echo Park Lake Rehabilitation Project
 - Engineering News Record – California, 2013 California Best Projects (Southern California) – Water/Environment
 - American Public Works Association – Southern California Chapter, 2013 BEST Project Award - Drainage, Water and Wastewater
 - American Society of Civil Engineers – Metro Los Angeles Branch, 2013 Outstanding Public Civil Engineering Project – (Water) over \$10M
 - American Society of Civil Engineers – Los Angeles Section, 2013 Outstanding Government Civil Engineering Project
 - California Water Environment Association - Los Angeles Basin Section, 2013 Engineering Achievement Award
 - Southern California Development Forum, 2013 Urban Design and Planning Award and 2014 Operations and Environmental Performance Award
 - American Society of Civil Engineers - Region 9, 2013 Outstanding Parks & Recreation Project
 - American Academy of Environmental Engineers and Scientists, 2014 Grand Prize for Environmental Sustainability
 - Construction Management Association of America – Southern California Chapter, 2014 Project Achievement Award – Public Works Project

- California Preservation Foundation, 2014 California Preservation Design Award - Rehabilitation Category
- American Society of Civil Engineers – National, 2015 Outstanding Civil Engineering Achievement Award Finalist
- California Stormwater Quality Association (CASQA), 2014 Outstanding Sustainable Stormwater BMP Project
- American Society of Landscape Architects - Southern California Chapter, 2014 Quality of Life Design Award - Honor Award, Recreation and Parks
- American Society of Landscape Architects - Southern California Chapter, 2014 Quality of Life Design Award - Award of Excellence
- Santa Monica Bay Low Flow Diversion Upgrades
 - American Public Works Association – Southern California Chapter, 2013 BEST Project Award – Storm Water Quality.

FINDINGS & RECOMMENDATIONS

Section I: Program Management

Prop O is an innovative, complex, and large-scale infrastructure program. Sound management of Prop O bond funds, projects, and the overall program is necessary to ensure that bond funds are being properly accounted for and that expenditures incurred are properly supported and meet eligibility requirements. Strong program management is necessary to ensure that the program is meeting its intended goals of protecting public health, improving water quality, conserving water, and reducing flooding. This audit analyzed a number of areas related to Prop O program management, including: governance structure; adequate systems, reporting, and contracting procedures; monitoring and timing of bond expenditures; compliance with Prop O project eligibility requirements; and project outcomes.

The audit team conducted interviews with City management and reviewed the Prop O Governance Structure, financial and management systems, reporting to the public and governing entities, project eligibility criteria, bond issues and expenditures, and procurement/contracting procedures. We identified and evaluated project performance metrics for the seven selected projects.

Overall, the Proposition O governance structure and the City's implementation of that governance structure has resulted in an effective program that meets the intent of the bond measure. Projects funded by Prop O make a positive impact on the City by directly supporting compliance with Clean Water Act requirements, improving water quality and conservation, reducing flooding, protecting public health, and providing educational, recreational, and community benefits. Approximately two-thirds of bond funding directly addresses Clean Water Act compliance, a key measure of a high quality project outcome. BOE, LASAN, CAO, and BCA, along with the oversight and advisory committees were charged to implement an innovative and unique bond program.

The results of our testing of the seven selected projects award documentation indicate that contracts were awarded based on established eligibility criteria and adequate processes were in place resulting in contracts being awarded for reasonable amounts in comparison with other bids received and the City's estimates. For the two cancelled projects, the City had a reasonable basis and process for the cancellation. In addition, the City utilized Financial Management Information System (FMIS) and Financial Management System (FMS) to capture project costs.

However, we identified significant issues related to slow expenditure of bond funds, and delayed and inaccurate reporting. We also identified deficiencies not significant to the objectives of the audit related to documentation of project selection criteria and optimization, project expenditure file maintenance, and

organizational communication. These program management issues indicate control weaknesses that should be addressed by management.

Finding 1: The program has maintained a large balance of unexpended bond funds over time. As a result, since FY 2010, the City has incurred an average of \$1.36 million per year in net interest costs on idle funds.

The program incurs an interest rate expense on each bond issuance. In approving the bond measure, voters indicated their support of this interest rate expense in order to meet the intended goals of Prop O. However, when there are high cash balances, the City is accruing interest expense without the expected project benefits. Given the need to balance the timing of bond issuances, project development, and construction, it is expected that a program such as Prop O would maintain a reasonable balance of available funds. However, even after subtracting outstanding encumbrances from the year end cash balances, the five Prop O bond funds still had an average of \$171 million in "available funds" for the periods FY 2010 through FY 2015.

The interest cost to the program is the difference between the effective interest rate of the bonds (expense), and the interest yield to the City on those unexpended funds (earnings).

The Controller auditor determined the average interest rate expense for Prop O bond issuances was approximately 3.4 percent on the monies received through bond sales. The Controller auditor also reviewed Office of Finance (formerly the Treasurer) monthly Investment Reports, noting that for 2010 to 2015, the effective earnings rate averaged 1.5 percent. Thus, the net interest rate expense to the program is the difference between the 3.4 percent interest expense rate and the 1.5 percent interest earnings rate, or 1.9 percent, on average.

If we assume for purposes of example that it is reasonable that the program maintain a cash balance of approximately one-half of remaining expenditures for current projects (\$100 million), then \$71 million of the average \$171 million cash balance over the last five fiscal years would be considered excess. An excess cash balance of \$71 million results in an interest expense cost of \$1.36 million per year, which could be considered a lost opportunity cost of \$6.8 million over the five-year period. Idle funds are reduced as cash is expended to complete projects, and given the variability of future cash balances, the spend-down rate, and timing of any new bond issuances, we cannot project future excess interest costs that may be incurred.

Reasons for the Large Cash Balances

Prop O's large cash balances are the result of a combination of factors. Due to the innovative nature of Prop O projects, many projects take longer than expected. These delays are further compounded by BOE's conservative approach to project budgeting. To assess the reasons for the large balances, we interviewed BOE staff and reviewed BOE's worksheet that was used to determine the amount for the 2011 bond issuance of \$117 million.

In general, for non-construction costs (e.g., pre-design and design costs), BOE estimates the costs to be incurred over the next year as its anticipated cash needs. However, for construction costs, BOE uses a very conservative approach. First, it estimates which projects will have a construction contract signed during the next year. Then, it "sets aside" this amount, even though some expenditures on the project may not be incurred for another three to four years (or longer if there are project delays).

To illustrate, in calculating the \$117 million bond issuance for 2011, BOE estimated \$279 million was needed for FY 2012 expenditures (which included full estimated project amounts). BOE then estimated how much cash on hand there would be as of June 30, 2011, and subtracted this amount from the \$279 million.

However, FMS shows total FY 2012 expenditures of only \$47 million, which led to the large cash balance as of June 30, 2012. Through June 30, 2015, total expenditures since July 1, 2011 have only been \$169 million, which is \$110 million less than the estimated cash needs of \$279 million.

According to BOE staff, there can be a variety of reasons why projects might be delayed, which would result in the lack of expenditures on projects. In other cases, estimated expenditures could be overstated by material amounts if BOE overstates the level of effort needed to complete the project. Specific examples follow:

Echo Park and Machado Lake Ecosystem Projects

The FY 2012 projected cash requirements for these two projects totaled \$156.8 million, or 56% of the \$279 million noted above.

- **Echo Park** – For purposes of the bond issuance calculation, BOE estimated FY 2012 expenditures of \$71.7 million for this project. However, FY 2012 expenditures were only \$11.7 million, and as of June 30, 2015, total expenditures since July 1, 2011 were only \$29.5 million. This project is essentially complete.

BOE staff indicated that during the period when the Echo Park project was bid for construction (early 2011), the construction industry may have been experiencing an economic downturn. This may have resulted in the bids being substantially less than anticipated. Some firms may have been pleased to secure any type of work, and the bad economy also kept equipment and construction costs low. BOE speculated that some reasons for the low bids were the dry weather during this period (rain would have added complexity to the project) and the bad economy.

- **Machado Lake** – For purposes of the bond issuance calculation, BOE estimated FY 2012 expenditures of \$85.1 million for this project. However, FY 2012 expenditures were only \$1.2 million, and as of June 30, 2015, total expenditures since July 1, 2011 were only \$33.1 million. As of June 30, 2015, the project is about 45% complete.

According to BOE staff, the first delay occurred because the City had to wait for approval from the U.S. Army Corps of Engineering, Regional Water Quality Control Boards, and the California Department of Fish and Game, which took longer than anticipated.

A second delay occurred because the project was rebid. The bids came in significantly higher than anticipated, which may have been because the contractor community in Southern California has limited experience with fresh water lakes in California.

BOE's methodology to determine the amount of each bond issuance would tend to lead to large cash balances in the Prop O funds at certain times. Also, funding the full amount of the approved project at, or sometimes long before, the time of the contract award is a conservative approach, and may not be reasonable when the construction phase of a project will take two to four years.

The City Attorney's Office has advised that state law requires the City to have enough cash on hand to pay for all obligations incurred via a contract at the time the contract is signed. The City Attorney's Office further advised that including an appropriations clause in the contract could eliminate this requirement. Such a clause would commit the City to funding only that portion of a project for which it has cash on hand, and allow the City to delay issuances of additional bonds to raise the additional cash necessary to complete the project.

Given BOE's long-term approach to appropriating and encumbering project funds, the issue of large cash balances for special fund projects likely extends beyond Prop O to other general obligation bond infrastructure programs.

Recommendation:

1.1 The CAO should work with the Controller-Operations Division, City Attorney and BOE to develop improved processes that would prevent the accumulation of excess, idle cash within the City's bond Funds. These could include developing procedures to:

- a. Better estimate the amount and timing of cash flow needs and periodically reassess the cash needs and the proposed bond issuances after taking into account project delays, cost savings and availability of other sources of funds, such as grants and accumulated interest.**
- b. Periodically monitor available cash balances and consider the use of unexpended bond funds from prior issuances for eligible future projects before issuing additional bonds.**

The City should also:

- c. Consider, where feasible, adding an appropriations clause to eliminate the need for having cash for the full amount of the contract at the time of execution of contracts.**
- d. Explore the use of short term financing, such as commercial paper, to provide cash for the early phases of approved projects and subsequently retire those instruments with the proceeds from bond sales.**

Finding 2: The CAO did not timely submit the annual SB 165 report to the Mayor and City Council as required by State Statute, lessening the relevance of this oversight control.

The Local Agency Special Tax and Bond Accountability Act (SB 165, Statutes of 2000, Chapter 535) enacted by the California State Legislature through Senate Bill 165 found that it was important for local agencies to demonstrate to voters that bond funds are expended on the intended facilities and services. SB 165 requires an annual report be filed by the local agency levying a special tax and/or issuing a bond measure with its governing body to include (1) the amount of funds collected and expended and (2) the status of any project required or authorized to be funded by the special tax and/or bond measure. The reports should be submitted once per year in accordance with SB 165 that states “the levying local agency shall file a report with its governing body no later than January 1, 2002, and at least once a year thereafter.”

The CAO was late in complying with the Local Agency Special Tax and Bond Accountability Act. Although not entirely accounting for the long delays in completing SB 165 reports, CAO was unclear on whether they had to wait for the CAFR (Comprehensive Annual Financial Report) before submitting the SB 165 report. We believe that CAO may complete the SB 165 report prior to release of the CAFR. During testing of Prop O reporting to the Mayor and City Council, it was noted 10 of 10 (100%) SB 165 reports were submitted untimely as follows:

FY Report	Date Submitted	Days after Jan 1
2013-14	1/23/2015	27
2012-13	1/23/2015	392
2011-12	1/23/2015	757
2010-11	1/23/2015	1,123
2009-10	8/28/2013	975
2008-09	6/14/2011	534
2007-08	10/9/2009	286
2006-07	10/9/2009	652
2005-06	10/9/2009	1,017
2004-05	12/17/2007	720

In addition, the "Proposition O – Clean Water Bond Program Annual Report" attached to the SB 165 reporting package appears to include June monthly status information rather than a comprehensive annual report. For example, the Committee highlights section includes information for the month of June only and the Project Community Meetings Schedule includes information for the upcoming month of July. The annual report should provide comprehensive summary information to the governing bodies by year instead of utilizing the monthly reports. For example, the annual report could include total annual expenditures for each active project.

Compliance with State statute and providing comprehensive and timely information to governing bodies should be considered a high priority by the CAO and procedures should be implemented to ensure the CAO timely submits SB 165 reports in accordance with statute to the governing bodies to strengthen oversight controls. Not providing timely and comprehensive reporting to established governance bodies lessens the responsiveness of oversight controls.

Recommendation:

The CAO should:

- 2.1 Implement procedures to ensure the CAO timely submits SB 165 reports in accordance with statute to the governing bodies to strengthen oversight controls.**
- 2.2 Prepare a single annual Prop O report that summarizes activities, project expenditures, and performance for an entire fiscal year.**

Finding 3: The Monthly Status Reports of Prop O projects submitted to various City offices and committees contained inaccurate project expenditure data.

The Prop O Governance Structure requires the BOE and LASAN to report monthly to the AOC on the status of planned versus actual expenditures and to provide monthly status reports. The Governance Structure also requires BOE to provide quarterly reports to the Mayor, City Council, the AOC, COAC and various City Boards and Commissions on the status of project implementation/construction. BOE submits the reports monthly instead of quarterly. The monthly status reports are the primary public reporting tool for Prop O. The reports are detailed and comprehensive. They promote transparency, and provide extensive project information on status, schedules, and expenditures. However, we found that project expenditure data were not accurate.

The BOE submitted Proposition O – Clean Water Bond Program Monthly Reports (monthly reports) to the Mayor’s Office, CAO, Board of Public Works, AOC and the COAC that contained inaccurate expenditure data. BOE derived project expenditure reports from the City’s Financial Management System (FMIS/FMS), known as “Merlin” reports to prepare the monthly reports. While the monthly reports are an informative and effective resource for the program, the reported total expenditures did not agree and/or reconcile with the expenditures noted in the Merlin reports, and FMS. The differences for the seven projects tested ranged from \$427,324 (-2.5 percent of actual) understated in the monthly reports to \$99,199 (0.3 percent of actual) overstated. The following specific items were noted:

- No reconciliation of the monthly reports to the City’s financial system was performed.
- There were issues with the timing of the information used to generate the monthly reports. When BOE staff queried the financial system on a monthly basis to extract the expenditure records, they were only obtaining the recent month’s expenditures and adding to the prior month’s reported expenditures. Expenditures, such as mileage claims not reported timely, timesheet corrections, and pay dates occurring toward the end of a month, could be missed with this methodology as cumulative data is not being utilized and/or reviewed.

- Cost Allocation Plan (CAP) rates that are applied for overhead calculations can be updated or revised; however, no adjustments are made to the prior amounts included in the monthly reports.
- BOE staff manually applies CAP rates to determine overhead amounts, but no review was performed over the calculations to determine accuracy.

Failure to provide accurate information to the established governance bodies lessens the effectiveness of oversight controls. On a percentage basis, overall the monthly report was understated, and by project ranged from understated by 7.09 percent to overstated by 0.27 percent.

	Merlin Total	Monthly Report	Differences Over/(Under)	% of total
Westside	4,556,608	4,556,504	(104)	0.00%
Machado	22,037,151	21,963,767	(73,384)	-0.33%
Penmar	17,314,075	16,886,751	(427,324)	-2.47%
South LA	9,829,374	9,843,372	13,998	0.14%
SMBLFD Project 1	4,961,789	4,613,088	(348,701)	-7.09%
SMBLFD Project 3	12,588,500	12,198,102	(390,398)	-3.10%
Echo Park	36,545,109	36,644,308	99,199	0.27%
Totals	107,832,606	106,705,892	(1,126,714)	-1.04%

The inaccurate expenditure data reported was due to manual processes being employed to prepare the reports and there were no procedures in place for a supervisory review of the reports and to perform a reconciliation of the reports to underlying accounting records. During the audit period, BOE implemented procedures to reconcile monthly reports.

Recommendation:

BOE should:

- 3.1 Perform a monthly reconciliation of the reports, and automate the monthly reporting process, including programming the Merlin system to apply CAP rates to increase the accuracy of the monthly reports.**

Finding 4: Project scoring criteria were not fully developed at the start of the program, and evolved over time. However, LASAN did not provide consistent documentation of the changes, making it difficult to determine whether eligibility criteria were followed for some projects.

The audit team reviewed the City's Prop O contract award eligibility criteria. Two different criteria were used; an initial "High", "Medium", "Low" narrative criteria and subsequent numeric criteria. The Prop O Project Selection Numerical Criteria states it is a guide for LASAN staff to use in reviewing proposed projects so that staff can select projects that meet the intent of the Prop O bond language. The eligibility section of the document states "Projects can be judged eligible for presentation to the COAC and AOC if projects receive a total of 75 points from any of the project selection criteria. Any project that does not obtain a minimum of 75 points will not be considered for further investigation."

The numeric scoring criteria were guidelines. The "High", "Medium", "Low" narrative criteria were approved by the Council and Mayor at the outset of the program. For many of the early projects, the numeric criteria were not developed until after the projects had been approved under the "High", "Medium", "Low" narrative criteria.

During our testing of project selection, we noted the following:

- There was no project numeric evaluation score sheet completed for the Westside Park Rainwater Irrigation Project (Westside Project) in accordance with Prop O Project Selection Criteria.

BOE was originally funding the La Cienega/Fairfax Stormwater BMP project with Prop O funding but due to concerns expressed by community members, BOE formally put the project on hold and presented a new re-scoped project retitled the Westside Park Rainwater Irrigation Project. The de-obligation of the unspent funds and the removal of the project for the La Cienega/Fairfax Stormwater BMP project followed prescribed procedures. LASAN also followed prescribed procedures for the approval of the Westside Project; however, the project selection criteria was technically not followed, as the project evaluation score sheet was not completed. LASAN stated that the numeric project evaluation score sheet was not completed for the Westside Project because LASAN had completed the score sheet for the original project that Westside replaced and the water quality aspects of the project did not change.

- Two projects, Rosecrans Recreational Center SW Enhancement and LA Zoo Parking Lot: Demonstration of Environmental Sustainability, were implemented by LASAN but neither project met the Prop O Project Selection Criteria of a 75 point rating. The Rosecrans project received a score of 72 while the LA Zoo Parking Lot project received a score of 68. These projects were approved under the initial criteria prior to the development of the numerical scoring criteria implemented by BOE and LASAN. Despite their lower scores, the projects were approved due to both being high visibility, new technology, best management projects that highlighted the proactive steps BOE and LASAN were taking to improve water quality.
- LASAN did not document the variances from the selection criteria for the issues noted.

The LASAN should review its policies to ensure they are worded to meet the intent of the program, and to allow flexibility while maintaining adequate controls. In the event that LASAN, COAC, AOC, the Council, or Mayor deviate from an agreed-upon selection criteria, there should be formal documentation of the reasons and considerations to support the decision to implement a project that did not meet the initial selection criteria.

Failure to adequately evaluate projects based upon established criteria could lead to the approval and funding of projects that do not fully meet the intent of the Prop O bond.

Recommendation:

In the future, LASAN should:

- 4.1 Always evaluate projects, and document the evaluation process, based upon a single set of established criteria to ensure all projects provide the highest benefit to water quality and meet the intent of the bond language.**

Finding 5: LASAN and CAO should develop a more comprehensive tracking and reporting system as projects move from optimization to operations and maintenance to ensure compliance with Prop O bond funding requirements.

As defined in the January 2015 Monitoring Plan Proposition O Project Optimization Report, the optimization phase is a period in which agencies

“modify project elements so that they maximally achieve intended goals, such as improving runoff water quality and protecting receiving water beneficial use objectives. It is during this phase, that project physical, chemical, and biological characteristics are assessed, the balance between hydraulic, vegetation, and treatment elements optimized, and proper operation and maintenance (O&M) protocols established, to allow for sustainable operation for each Prop O water quality protection facility.”

An optimization phase is standard in infrastructure projects; however, the City did not have experience with optimization for natural infrastructure projects. The CAO consulted with bond counsel in 2011, prior to incurring optimization expenditures, to obtain an independent legal opinion as to whether optimization period activities constitute “improvement of real property” as required by the California Constitution and Prop O. The bond counsel determined optimization expenditures were an allowable use of Prop O bond funds. In addition, LASAN consulted with water quality experts on optimization approaches.

Currently, most completed projects are early in the optimization phase. As of December 2014, four of the seven projects selected for testing were in the optimization phase. The optimization budget for the four projects was approximately \$2 million and the optimization expenditures were approximately \$800 thousand. The first project-specific optimization expenditures were incurred in early 2013. The lack of significant rainfall over the last four years has also slowed the progress of the projects, as there has not been adequate flow to monitor progress towards achieving wet-weather flow Total Maximum Daily Load (TMDL).

The table below details optimization budget and expenditures as of December 31, 2014 for each of the seven selected projects where optimization was applicable. Total optimization expenditures as of December 31, 2014 are below the original optimization budget for the four projects in optimization; however, optimization costs for the South Los Angeles Wetlands Park were higher than original expectations.

SELECTED PROJECTS OPTIMIZATION COSTS THROUGH DECEMBER 31, 2014		
Project	Original Optimization Budget	Optimization Labor Expenditures
Penmar Water Quality Improvement Phase I	\$257,500	\$12,103
South Los Angeles Wetlands Park	301,000	784,279
Echo Park Lake Rehabilitation	1,366,524	21,179
Westside Park Rainwater Irrigation	225,000	10,727
Total	\$2,150,024	\$828,288

Based upon review of documentation provided and testing, there were no issues related to the use of bond funds for project optimization. The CAO and LASAN have taken steps to ensure optimization expenditures are allowable within the terms of the bond, that optimization expenditures are planned and approved by the AOC and the COAC, that optimization is being conducted within the overall optimization budget, and optimization activities are timed and prioritized to address specific project needs. These steps include consultation with bond counsel, consultation with water quality experts, and development of an optimization plan.

In the future, LASAN should carefully track the timing and conclusion of optimization and the transition to operations and maintenance. It is important for the program to closely track optimization and to transition to operations and maintenance on a project-by-project basis. It is also important that the City budget adequate operations and maintenance funds for Prop O projects to protect its investment in these projects.

To ensure that optimization activities support “improvement of real property”, LASAN could develop and provide a more comprehensive tracking of project optimization status in the Monthly Progress Reports, including: (1) all projects with approved optimization budgets, (2) expenditures to date, (3) optimization scope, (4) status, (5) expected end-date (report actual end-date when optimization is complete), (6) issues/problems, and (7) monitoring results to-date. This additional reporting could help ensure that optimization activities support “improvement of real property”, as specified in the California Constitution, Article XIII A Section 1.

Failure to adequately monitor and track optimization expenditures could lead to unallowable operations and maintenance expenditures being charged to Prop O that should not be incurred by the bond funds in accordance with the California Constitution and Prop O.

Recommendation:

The LASAN and CAO should:

- 5.1 Ensure that there is adequate funding to support Prop O project operations and maintenance as projects transition out of the optimization phase.**

LASAN should:

- 5.2 Carefully track the timing and conclusion of optimization and the transition to operations and maintenance.**

Finding 6: Prop O expenditure files were not maintained in a consistent and organized manner by the Public Works' Office of Accounting.

During testing of 60 non-labor expenditures, vouchers and supporting invoices maintained by the Office of Accounting auditors noted a lack of organization related to the maintenance of expenditure files. For example:

- Expenditure support was organized within file folders by vendor; however, the file folders did not include a summary or method of organization to indicate the contents of the folders. The vendor files were often quite large and the support was not maintained in an organized order; therefore once a file was finally located it took additional time to search through the file folder to find the specific expenditure and related support.
- The folders did not indicate the time period of the vouchers included, which spanned across ten years (November 2004 through December 2014).
- The financial system tracks expenditures by project; therefore, it was difficult to find the records since the Office of Accounting is tracking by vendor. There were 43 approved Prop O projects, however, the accounting files did not identify which Prop O projects were included within the file folders.

Proper organization over project files is a best practice. Files should be well organized, using a consistent methodology, allowing ease of access and identification of files not only for external reviews but to allow for ease of use by Office of Accounting employees. Failure to properly organize and track expenditure files may result in loss of data or difficulties obtaining information.

The lack of organization of Prop O expenditure files was due to the age of the vendor files, as the projects selected covered a period of ten years and the Office of Accounting has migrated to electronic files during this time period allowing for the lapse in sound filing procedures. The Office of Accounting felt that files were organized in a method that was useful for their purposes.

Recommendation:

The DPW Office of Accounting should:

- 6.1 Implement a methodology to concisely organize hardcopy expenditure files to allow files to be properly identified and tracked.**

Section II. Project Costs

Budgeting, cost control, and proper accounting are important aspects of public spending accountability. Processes and procedures to ensure contracts are awarded for reasonable amounts, properly account for and track projects costs, properly record transactions, and pay contactors according to requirements, are all important aspects of project management and project controls for an infrastructure bond such as Prop O. Strong internal controls require adequate supporting documentation be developed and maintained to ensure project charges are properly recorded to the proper phases and reported to the governing bodies.

To evaluate the City's performance as it relates to Prop O project costs, we conducted interviews with City management to obtain an understanding of systems in place to capture project costs; of the City's procurement/contracting procedures over Prop O, expenditure approval; and processing and internal control procedures. We selected a sample of 60 labor expenditure transactions totaling \$6,536 and 60 non-labor expenditure transactions totaling \$8,420,866 from the population of all labor (\$8,650,454) and non-labor (\$99,716,355) expenditures for the seven selected projects for control and substantive testing.

Control testing included testing of management reviews of the transactions and the documentation of the review in the systems. Substantive testing included vouching supporting documentation, including the voucher, vendor invoice and detailed billing documents, for each transaction to transaction detail reported in the systems to determine if the project costs were accurately reported in the systems.

We also performed control and substantive testing related to indirect costs charged to the projects. Control testing included testing of the management review of the indirect cost calculations and the system used for calculating the costs. Substantive testing included a recalculation of the indirect costs charged to the projects. The December 2014 monthly report and the underlying records were selected for testing. We obtained supporting documentation for the sample of expenditures selected. The supporting documentation included timesheets and MERLIN reports (contained phase/task information for the sample) for labor expenditures and invoices and MERLIN reports (contained phase/task information for the sample) for the non-labor expenditures. We also obtained the MERLIN Task Code Description Report, the BOE Task Code Description Manual, and the LASAN Task Code Description Manual. We performed testing on the sample of expenditures to determine the expenditures were appropriately categorized by project phase. In addition, for the seven selected projects, we determined whether the projects were completed during

the scope of our audit. Lastly, a sample of 17 program management and planning/feasibility costs were selected for testing from the population of all general program costs for program management and planning/feasibility costs. Utilizing this sample, we tested to determine whether the general costs were properly coded or should have been charged to a specific project code.

For the seven projects, we obtained supporting documentation related to the contract awarding process including bids received from other vendors and documentation of the City's initial estimate of project cost. We reviewed documentation to determine whether the City incorporated contracts for reasonable amounts in comparison with other bids received and the City's estimates. Due to the unique nature of the Prop O projects, direct benchmarking project performance and budgets with other entities and jurisdictions was determined to not be applicable as the information was not available to compare.

The audit team reviewed a variety of literature on related project costs. After evaluating the documents and projects, it was determined that a comparison of projects in other jurisdictions would not be effective in determining whether Prop O project contracts were reasonable as compared to other jurisdictions for three reasons: (1) the types of projects constructed under Prop O were customized and specific to the individual project, natural conditions within the project site, time period in which the project was constructed, and local market conditions; (2) "soft" project characteristics such as environmental permitting, community meetings, and Endangered Species Act compliance cannot reasonably be compared across projects; and (3) existing literature on "natural treatment" projects such as wetlands, infiltration basins, and subsurface infiltration systems are highly variable.⁶

Given the difficulty in comparing costs for similar projects across jurisdictions, we instead reviewed LASAN and BOE processes and procedures in developing project construction and overall budgets, described in the Background section. In addition, the audit compared initial project budget estimates with original

⁶ For example, Boston Water and Sewer Commission's Stormwater Best Management Practices: Guidance Document (January 2013) identifies construction-only cost ranges that vary fivefold for a "stormwater wetland" and no cost estimates for several types of infiltration systems. A 1994 United States Environmental Protection Agency report, "Making Sense of Wetland Restoration Costs" reviewed cost data available at that time and found a range of \$5 per acre to \$1.5 million per acre to restore wetlands. Cost estimates prepared in 2012 for the California Coastal Conservancy to restore wetlands in the Upper Klamath Basin to help meet TMDL requirements ranged from \$15 million to \$27.5 million. In the City of Ontario, California, the recently completed Mill Creek Wetlands Recreation and Restoration Demonstration Project cost \$16 million. The project includes a series of natural water quality treatment ponds, a de-silting basin, UV light treatment, and wetland vegetation. These data illustrate a wide range of costs.

and final project budgets. The audit also compared initial concept report construction estimates with actual construction bids.

We found mixed results related to the City's management of Prop O project costs. The City was properly capturing project costs; adequate processes were in place resulting in contracts being awarded for reasonable amounts in comparison with other bids received and the City's estimates; and expenditure transactions were supported by proper approval for payment and bond proceeds were properly recorded.

However, we also identified a number of process and procedure issues related to project costs that are lacking controls. Several of these issues may go beyond Prop O, potentially applying to other infrastructure programs within the Department of Public Works (Department).

Finding 7: BOE did not have a system in place to validate consultant hours and rates. As a result, BOE paid selected consultants for hours worked that consultants did not, in turn, pay to employees.

BOE utilizes pre-qualified consultants for Prop O project pre-design and design work. Based on the consultant agreements and from discussions with BOE, consultant billings are to be based on actual cost. The consultant agreements allow for the payroll costs, plus the overhead multiplier and profit mark-up to be included on hours worked if such overhead hours are paid, but not for uncompensated time over 40 hours per week. Non-compensated hours billed to BOE, but not paid to the consultant's (or sub-consultant's) employees, would not normally be considered a cost to the consultant since the employees are not actually paid for more than 40 hours per week.

BOE does not have a process in place for consultants and sub-consultants to submit supporting documents (payroll records) with invoices. As a result, BOE could not determine whether consultants or sub-consultants billed BOE for actual hours worked over 40 hours per week that were not, in turn, paid to exempt employees. As documented below, the amount of non-verified payments for hours worked over 40 hours per week to selected consultants and sub-consultants was not material. However, this lack of process to verify consultant and sub-consultant timesheets and payroll applies beyond Prop O to Department of Public Works construction projects that utilize pre-qualified contracts for consultants and sub-consultants.

The audit team tested a sample of invoices from consultants working on Prop O projects. The testing performed was to determine if allowable workers charged to projects were being billed to BOE in excess of 8 hours per day (40 hours per week) based on recorded time, for which the employee may not be "paid" or "compensated" for as a salaried worker. It is generally understood that the consultant employee's actual hourly rate stated in consultant agreements is based on (and computed on) a 2,080 hour work year.

For the sample reviewed, we requested that BOE obtain certified payrolls and timecards from consultants who billed more than 40 hours per week to BOE. We noted that in 8 pay periods tested out of a sample size of 287, employee payroll records indicated employees who worked over 40 hours per week charged to the project along with the overhead multiplier and profit, and were not compensated for hours over 40 billed to BOE. Because non-compensated time to consultant employees billed to BOE inclusive of the multiplier and profit mark-up does not qualify as actual "cost" to the consultant, it would not be billable. In charging BOE, the consultant is profiting from such non-compensated time plus the overhead multiplier and profit mark-up for each hour billed as such.

The hourly billing issue could have been determined, monitored and challenged by the City by performing periodic audits of consultants and sub-consultants to the prime consultant (see separate finding 12), and obtaining certified payrolls and timecards of consultants and sub-consultants to determine if they are actually being paid as a basis for "cost" incurred under their agreement.

For purposes of clarifying the effect of hours billed but uncompensated, it should be noted that BOE's contract agreement with their prime consultants (and sub-consultants to the prime consultant) provides that work will be paid for on an hourly basis plus a multiplier (to cover payroll burden, payroll fringe benefits and consultant overhead costs; e.g., 1.8 or 180%) plus a 10% mark-up to the factor of the combined sum of the two amounts for profit. For sub-consultants to the prime consultant, the prime-consultant's mark-up for administration is 5%. When BOE is being billed for the time, multiplier and profit mark-up allowed in the consultant's agreement on an employee (for which the employee is not paid or compensated for), then such billed amounts would be additional profit to the consulting firms.

Strong internal control includes a careful review of billings for hours in excess of 8 hours per day, periodically obtaining and reviewing certified payrolls and employee timecards, and conducting periodic audits of consultants and sub-consultants to determine if it is overpaying its consultants and sub-consultants for employee overtime that is not an actual cost to the consultant which is in turn billed to the City. As noted, this condition applies beyond Prop O projects

to other Department of Public Works construction projects that utilize pre-qualified contracts for consultants and sub-consultants.

BOE did not have a system in place to validate that hours billed by consultants and sub-consultants would exclude uncompensated hours (or a portion thereof) and the respective overhead multiplier and profit mark-up applied to them. As a result, BOE is paying consultants and sub-consultants for hours worked that the consultants and sub-consultants may not be paying to their exempt employees. The audit team found costs that should have been disallowed for four of the ten consultants tested. We reviewed 287 total pay period records from the ten consultants and found eight pay periods (2.8%) with costs that should have been disallowed.

Within our sample, seven of the ten consultants, representing 20 employees and 24 pay periods conducted more than 40 hours work (of any type) equivalent to \$24,212, and we noted \$2,536.09 in disallowed Prop O costs, which represents 10.5 percent of the dollars invoiced for overtime work. Extrapolating from the payroll records that we reviewed for the seven selected projects and expenditures of the four contractors with exceptions, BOE may have overpaid the selected tested consultants \$11,873. Compared to the amount of total project expenditures, this is an insignificant quantity (0.02 percent).

Because we did not select a random sample of payroll records, or of all projects, it is difficult to quantify the overpayments to Prop O projects more broadly. However, it should be noted that this finding applies beyond Prop O projects to other Department of Public Works construction projects that utilize pre-qualified contracts for consultants and sub-consultants.

Consultant	Total Project Expenditures	Total Expenditures to Consultant	Percentage of Total Project Expenditures	Total Invoice Amount	Total Disallowed Expenditures on Invoice	Percentage of Disallowed Costs for the Consultant	Total Consultant Disallowed Costs at Percentage of Disallowed Costs from Sample	Percentage of Total Project Expenditures Disallowed
Consultant 1	\$21,963,767.00	\$379,588.38	1.73%	\$648.83	\$4.52	0.70%	\$2,644.36	0.01%
Consultant 2	\$4,556,504.00	\$19,529.62	0.43%	\$11,254.24	\$132.31	1.18%	\$229.60	0.01%
Consultant 3	\$9,843,372.00	\$158,455.33	1.61%	\$23,803.61	\$1,351.88	5.68%	\$8,999.16	0.09%
Consultant 4*	\$23,790,763.23		0.00%	\$66,295.77	\$1,047.38	1.58%	\$0.00	0.00%
Total	\$60,154,406.23	\$557,573.33	3.77%	\$102,002.45	\$2,536.09	2.49%	\$11,873.12	0.02%

*Consultant 4 data was for the Machado Lake Ecosystem project. As this was not in the audit scope, we did not obtain total contract expenditures that consultant.

Recommendation:

BOE should:

- 7.1 Work with the City Attorney to revise the contract language to ensure that consultants compensate employees for actual hours worked.**

Finding 8: The BOE did not adjust the amounts calculated for indirect costs for Prop O expenditures as reported in monthly reporting when new cost allocation plan rates for the correct fiscal year were released by the Controller's Office, leading to inaccurate reporting of program and project expenditures.

Determining labor costs for Prop O projects includes application of cost allocation plan (CAP) rates. Each month BOE staff calculates indirect costs on labor charges for the previous month to include in monthly reporting to the governing bodies and the public. BOE staff have been utilizing the most current approved CAP rates provided by the Controller's Office; however, there are timing differences for the approved rates and no adjustment is being performed once the updated rates are released. For example, the CAP 35 rates for expenditures for the period July 1, 2012 through June 30, 2013 were released by the Controller's Office per memo on September 30, 2014. BOE staff did not adjust ("true-up") the calculations of indirect costs for the labor charges for July 1, 2012 through June 30, 2013 utilizing these new rates. This "true-up" was not performed for any period of the Prop O project.

It is City policy to true up rates to the most current year, including for City funds. In addition, accurate costs, not estimates, should be charged against Prop O funds for compliance with the bonds. BOE did not understand the policies for the adjustment of CAP rates due to a lack of training. In addition, the BOE did not have procedures in place to perform a true-up of costs as rates changed.

Failure to perform a true-up of the indirect cost calculations leads to inaccurate amounts being reported to the governing bodies and the public in monthly reporting. For the period July 1, 2012 through June 30, 2013 the amount reported as indirect costs was understated by \$192,482 utilizing the modified CAP 35 rates per GO Bond Policy instead of the modified CAP 33 rates used for monthly reporting.

Recommendation:

BOE should:

- 8.1 Perform a "true-up" of all indirect costs calculated through each fiscal year with the updated, approved rates provided by the Controller's Office, and include these updated amounts in monthly reporting to the governing bodies.**

Finding 9: The BOE did not review or potentially adjust consultant and sub-consultant employee hourly rates and support for labor multipliers after the Master Services Agreement was approved. As a result, rates and multipliers were not evaluated over time, potentially resulting in overbillings to BOE.

BOE pre-qualifies consultants for engineering work such as pre-design and design work on Prop O projects. These Master Services Agreements may extend for several years. BOE established overhead rates at the time the Master Services Agreement was executed. These rates were not revisited or revised on an annual or task order basis.

We noted in our review of the consultant agreements with BOE (i.e., primarily engineering contracts) that the consultant arrangements as procured provide that the consultants, and sub-consultants to the prime consultants, are allowed to bill on an actual hourly rate basis for approved workers. BOE obtains consultant and sub-consultant hourly rates at the beginning of a project for authorized project personnel. The hourly rate is then increased by a multiplier (sometimes referred to as an “overhead multiplier” to cover overhead, payroll burden and fringes) for a final agreed upon hourly rate for authorized workers (call this the “billable rate”). The multiplier varies depending on whether or not it is for “Consultant personnel located in the Consultant’s Office” (typically a higher multiplier) or for “Consultant personnel located in a City Office” (i.e., this can also be referred to as “Field Office” and is typically a lower multiplier).

BOE typically obtains support for the multipliers from its prime consultant who also provides multiplier information from its sub-consultants. In reviewing the information provided, we noted there is inconsistency in the multipliers such as:

- Some consultants and sub-consultants provide an independently-prepared audit report to support the rate (i.e., FAR Overhead Audit Rate, which would be preferred form of support) while others prepare a letter on company letterhead with or without support attached, some provide a spreadsheet calculation, some provide another format of support, etc.
- Some sub-consultants provided both the “Consultant Office” based overhead multiplier rates and the “City Office” based overhead multipliers, while others provided only one rate (the “Consultant Office” rate).

The multiplier is used to compensate workers at a straight time basis.

BOE's contract agreement with their prime consultants (and sub-consultants to the prime consultant) also provides that work will be paid for on an hourly basis plus a multiplier (to cover overhead, payroll burden, fringe and overhead costs; e.g., 1.8 or 180%). The employee's actual direct labor rate multiplied by the multiplier results in a final hourly "billing rate" per worker. These billing rates are used in the monthly billing process when the amount of labor hours charged by the consultant or sub-consultant for each employee is multiplied by the billing rate to arrive at an extended amount for each employee. The extended amounts for all employees are then marked up by a profit factor for the consultant (10%) and administrative costs for the sub-consultant (5%).

BOE has been obtaining the multiplier rates but has been relying upon the information and only reviewing it for reasonableness. In cases where the rate is too high or exceeds a cap as established in the specifications, the Consultant may call this to BOE's attention but it is unclear if BOE is following up to review and challenge the higher rates.

Strong internal controls related to multiplier rates would include detailed evaluation and potentially more frequent adjustment of overhead rates. In adopting such practices, BOE may wish to establish a not-to-exceed rate in the original contract. BOE may require consultants and their sub-consultants to provide an annual independently-prepared overhead audit to support their overhead multiplier rates annually, or at the time they negotiate a new task order. BOE should make sure that whatever the information received, the rate is being calculated properly and consistently, and that there is sufficient support to validate the rate. BOE should also verify that each sub-consultant is submitting both a "Consultant Office" rate and a "City Office" rate or note why only one is being provided (as a part of this, it should also note which workers fall into each classification). This condition applies beyond Prop O projects to other Department of Public Works construction projects that utilize pre-qualified contracts for consultants and sub-consultants.

Overstated multiplier overhead rates may result in overbillings to BOE, and consequently overpayments to consultants. The specific impact to BOE depends on the extent to which the overhead rate may be overstated. As an example of the potential impact, a multiplier difference of 0.2 (1.8 contractually set overhead multiplier rate versus a 1.6 actual overhead multiplier rate) for one consultant charging 40 hours a week for 45 weeks of a year, and a billable rate of just over \$75 per hour, would result in an additional cost of almost \$30,400 for the year to BOE, inclusive of the profit mark-up.

Recommendation:

BOE should:

- 9.1 Develop a policy to review and approve submitted multiplier information for consultants and sub-consultants at the beginning of the contract and then again after three years for those firms who are issued new task orders, and revise the Project Delivery Manual accordingly.**

Finding 10: The LASAN, BCA, and Office of Accounting, did not utilize clear timesheet task and subtask codes, making it difficult to determine if internal labor project costs were categorized to the proper Prop O project phase.

Strong internal controls require adequate supporting documentation be developed and maintained to ensure project charges are properly reported to the proper phases and reported to the governing bodies. Within a project-specific work order, the Bureaus use five phases for project delivery of Prop O projects: pre-design, design, bid and award, construction and post-construction. Budgets are established for these phase levels. In order to track project costs against the budgets, the Bureaus' employees enter labor charges to a specific work order that includes a suffix that indirectly aligns with the phases of the project. In addition, the employees charge labor costs to task/subtask codes, established at the Bureau level, to provide more detailed information on the work performed. Below are the suffixes utilized by BOE within the project work orders:

- A – (GEN): project management
- B – (ODC): Bureau of Engineering Support Services consisting of Geotechnical, Environmental, Survey, Plan Check, Art, Printing, etc.
- C – (DEV): development of full proposals
- D – (DES): City and Consultant Pre-design and Design Staff cost including: Architectural; Electrical; Mechanical; Structural; Landscaping; Drainage/Site Work; Street Lighting and Signals; and Bid & Award.
- F – (CON): Design Services during Construction, Construction Management, Hard Construction Cost, Demo Cost, and other city department cost during construction (ITA, Contract Ad. & General Services)
- L – (LAN): Land Acquisition and Relocation, Right of Way and all cost associated with Land Acquisition.

There are also work orders specific to Prop O Program Management, Prop O Planning & Feasibility, and several work orders specific to optimization. The BOE and LASAN provided task and subtask descriptions utilized by its employees. The BOE has the phases of the project built into their task codes, while LASAN codes were more generic and did not include the phases which required

judgment to determine if the proper phase was charged. The BCA did not provide a separate task description listing, but used the task code description listing stored and generated in MERLIN. Based upon this information we performed the following:

- A sample of 60 labor expenditure costs were selected for testing from specific Prop O projects to determine the proper phase code was charged. Of the 60 expenditures tested, we could not determine if 41 (68%) BCA expenditures, totaling \$5,073, were charged to the proper phase code because the task code definitions were too generic, such as "meetings" (task code 018) or "machine cleaning major sewers" (task code A31). For 4 of the 41 expenditures, no task code was listed.
- A sample of 17 program management and planning/feasibility general costs were selected for testing to determine whether the general costs were properly coded as such or should have been charged to a specific project code. Of the 17 expenditures tested, we could not determine if 14 (82%) LASAN and Office of Accounting expenditures, totaling \$24,006, were properly charged as general program costs. Based upon the Bureau charging the time to the work orders, it appears general cost categories could be appropriate, but the coding was not detailed enough to provide sufficient evidence. For example, under the Prop O Program Management work order, task code 089 was used, with the task code description "Prop O"; however, this is not descriptive of particular tasks relative to phases.
- A sample of 5 LASAN optimization expenditures were selected for testing to determine if they were charged in accordance with established criteria for optimization expenditures. LASAN has work orders specific to optimization; however, the task code descriptions were not sufficiently detailed for all 5 expenditures to clearly understand the optimization work that was conducted. For example, the description for task code 369 is "gardening", which was used to describe work related to re-planting at Echo Park Lake, but is not clearly descriptive of the actual activity.

The use of generic tasks codes does not facilitate charging labor hours to the proper phase of the project. Without specific and consistent use of descriptive coding, the Bureaus may not be accurately tracking City labor expenditures against budgeted amounts, which lessens oversight by the governing bodies. In addition, without better definitions of activities to categorize the optimization charges, LASAN is at risk for non-compliance with the California Constitution and Prop O related to bond funds, as the charges could be unallowable.

Recommendation:

LASAN and BCA should:

- 10.1 Develop a more comprehensive and integrated system of labor task codes that are detailed and useful for the Prop O projects and can be utilized for all Bureaus and the Office of Accounting.**

Finding 11: The BOE did not perform periodic audits of its consultants and sub-consultants billings and rates on selected projects. As a result, the BOE cannot verify that consultant billings, associated rates, and hours billed are not being overstated.

BOE does not currently exercise its audit rights to confirm that consultants and sub-consultants are complying with contractual terms and that billings and associated rates are not being overstated. BOE does mathematically check invoices each month and agrees rates on consultant invoices against those approved as described in BOE's General Guidelines for Consultant Services Invoices (July 11, 2014).

BOE did not consider exercising its contractual rights to audit consultants and sub-consultants billings to be necessary. In addition, BOE did not have procedures in place to periodically perform project risk assessments to determine whether audits would help address project risks and ensure proper billing and rates. Furthermore, BOE does not have dedicated staffing to perform such audits, nor does it currently outsource or co-source these audits.

Strong internal controls include evaluating risks relating to consultant and sub-consultant billings and rates, and implementing procedures to audit consultants and sub-consultants billing rates per hour, multipliers and hours billed (from timecard support) and hours paid (certified payrolls or actual payroll records). This condition applies beyond Prop O projects to other Department of Public Works construction projects that utilize pre-qualified contracts for consultants and sub-consultants.

Consultant billing audits may include testing for the following (testing may be performed on a sample basis):

- Agree time billed to original timecard details by employee;
- Determine if employee qualifies as a "Consultant Office" or "City Office" to ensure the correct overhead multiplier is being used
- Review the actual hourly billing rate against the employee pay per the maintenance file to ensure it has been properly computed;
- Ensure that hours billed for overtime are actually paid hours;
- Test the components of the overhead rate on a selective basis, including the burden and fringe rates;

- Test application of the overhead multiplier in cases of overtime pay to ensure that it is applied only on the straight-time (not premium time) portion of actual overtime pay.

BOE should perform periodic audits of consultants and sub-consultants billings to test the source data of billings, confirm that consultants and sub-consultants are complying with contractual terms and that billings, associated rates, and hours billed are not being overstated. This finding applies beyond Prop O projects to other Department of Public Works construction projects that utilize pre-qualified contracts for consultants and sub-consultants.

Recommendation:

BOE should:

- 11.1 Consider establishing procedures to periodically verify consultant and sub-consultant billing rates on a sample basis to ensure accuracy.**

Section III. Project Oversight and Monitoring

Project oversight and monitoring encompasses both control measures and performance measures. Control measures ensure that Prop O funds are being properly accounted for and that expenditures incurred are properly supported. Performance measures determine the extent to which Prop O projects are meeting the goals of the bond measure to protect public health, improve water quality, conserve water, and reduce flooding.

Through interviews with City management and review of program documentation, we determined that generally Prop O's governance and control structures adequately support project oversight. However, we identified one significant issue related to unit price contracting.

In addition, in seeking to determine whether Prop O's governance structure supported achievement of "high quality project outcomes", we analyzed existing Prop O performance metrics and measurement. The results of our testing indicated that the LASAN, until recently, had no process in place to define, measure, monitor, and report Prop O project performance.

Finding 12: BOE did not utilize an independent surveyor to verify payments for a unit price contract, resulting in a conflict of interest which could lead to BOE's overpayment of the contractor.

For unit price contracts, strong internal controls require independence between parties to ensure an independent evaluation of quantities for which a prime contractor is paid. For the Lake Machado project and other similar projects where there is a unit price arrangement, the surveyor hired to confirm quantities of dredging for billing purposes should be an independent prime contractor, rather than a sub-contractor to the dredging contractor.

For the Lake Machado project, a professional bathymetric surveyor was hired to verify quantities of dredging to validate a unit price contract; but the surveyor was not independent of the contractor performing work. Instead, the BOE contract specified "A bathymetric survey of Machado Lake shall be conducted before and after completion of the dredging work. The survey shall be conducted by a registered land surveyor in the State of California whose work is procured and paid for by the CONTRACTOR." In accordance with the contract, the prime contractor procured and paid for a professional registered land surveyor. In addition, a change order (Change Order No. 007, executed on August 26, 2014), provided for monthly progress payments based on

monthly measured dredge quantities measured by the surveyor (not to exceed the pre- and post-bathymetric surveys, as required by the contract).

During our audit of selected Prop O projects, we discussed with the City's BCA project management team the Lake Machado project relative to the billing arrangements in place and verification of quantities for the dredging operations being carried out. The dredging contractor is being paid on a unit price basis based on actual quantities removed through its dredging operations. The quantities removed are verified based on a pre- and post-bathymetric survey completed, which measures the pre- and post-project dredged materials.

As specified in contract, the procured relationship was between the prime dredging contractor and a bathymetric surveyor who is a sub-contractor hired by them. This arrangement would not be considered independent because the dredging contractor is paid by the unit of sludge removed from the lake, and the bathymetric surveyor as a sub-contractor to the prime contractor hired to verify the units removed from the lake presents a potential conflict of interest. For projects requiring the expertise of a surveyor or other professionally designated party for unit price, quantity and payment purposes, all arrangements for the procurement of the firm should be made directly with BOE through a separate contract from that of the dredging work.

Measuring and verifying units of production, in this case dredging quantities, should be a service procured of a professional surveyor independent of the prime dredging contractor performing the work under the contract. Failure to separate the surveyor's work from the contractor's work creates a conflict of interest. In this case, the surveyor as a sub-contractor is being paid for the services of establishing quantities that are the basis for BOE's payment to the prime contractor. Such a conflict of interest may lead to BOE's overpayment of the contractor due to inaccurate measurements, quantities and results.

Recommendation:

BOE should:

- 12.1 Make all arrangements for the procurement of an independent firm, separate from the Contractor, for projects requiring the expertise of a surveyor or other professionally designated party for unit price, quantity, and payment purposes.**

Finding 13: LASAN has been slow to report on interim or final project outcomes, making it difficult to measure project effectiveness and compliance with bond requirements.

The Prop O bond measure states the bond proceeds will be used to build improvements designed to “protect public health by cleaning up polluted storm water; keeping pollution, trash, toxic chemicals, dangerous bacteria from rivers, beaches; preserving clean drinking water by protecting groundwater quality; reducing flooding; increasing water conservation; protecting bays, rivers, and lakes from storm water contamination.” While water quality measures are the primary indicators of success for Prop O projects, the Proposition included broader goals. Based on the Proposition language and intent, factors to evaluate each project’s performance should include:

- Improving water quality
 - Meeting TMDL requirements (reductions in pollutants into the City’s waterbodies)
 - Reducing the number of beach closures
- Providing multi-use benefits
 - Reducing use of municipal water
 - Improving communities
 - Improving natural habitats
 - Reducing flooding
- Achieving successful project outcomes
 - Meeting the objectives and targets contained in initial project proposals
 - Designing and building to technical standards
 - Executing effective project management
 - Effective transitioning to ongoing operations and maintenance

The LASAN did not have a structured approach and formal procedures to measure, monitor, and report Prop O project performance and outcomes to demonstrate whether benefits have been achieved on projects funded. Rather than provide substantive reports on progress-to-date, LASAN has appeared to be waiting to determine full project results. However, because of

project complexity and the drought, it may be difficult to determine “final” project outcomes.

The projects funded by Prop O make a positive impact on the City by directly supporting compliance with Clean Water Act requirements, improving water quality and conservation, reducing flooding, protecting public health, and providing educational, recreational, and community benefits. While the audit was not intended to evaluate the extent to which Prop O projects have met the overall goals of the bond measure, our objectives and related procedures did consider high quality project outcomes.

The intent of Prop O projects is to *“build improvements designed to address the regulatory requirements of the Federal Clean Water Act, improve water quality and protect public health and the environment. The improvements will clean-up polluted storm water and bacteria in the City’s rivers, lakes, beaches, and ocean.”* As such, a primary performance metric of Prop O is improvement in Total Maximum Daily Loads (TMDL) of pollutants deposited into the City’s rivers, lakes, and beaches as well as the ocean. TMDL is a calculation of the maximum amount of a pollutant a waterbody can receive while still meeting water quality standards. TMDL requirements are established by the Los Angeles Regional Water Quality Control Board, which is responsible for enforcing the Federal Clean Water Act within the Los Angeles region. Meeting TMDL requirements is intended to increase the benefits and recreational uses of a waterbody.

A Senior Environmental Scientist with the Los Angeles Regional Water Quality Control Board (LARWQCB) was interviewed on May 15, 2015. The scientist interviewed oversees the MS4 (Municipal separate storm sewer system) program for the region, supporting Clean Water Act (CWA) compliance. As a CWA regulator, his perspective on Prop O projects is a good indicator of the program’s performance. In general, his perspective was that the projects were well thought out, reasonable, and should provide benefits. As far as compliance with TMDL limits, LARWQCB sees Prop O projects as falling into two categories: 1) those that directly met TMDL requirements; and 2) those that could be seen as a component of an overall strategy to comply with TMDL effluent limits for dry weather flows, wet weather flows, or both.

Prop O projects that directly met TMDL requirements include the Catch Basin Screen Covers (Phases I through IV), and the Santa Monica Bay Low Flow Diversion Upgrades (Packages 1 through 4). Machado Lake will also provide direct TMDL compliance through the removal of contaminated sediments. Prop O projects that are components of broader compliance strategy, from the LARWQCB perspective, include Echo Park Lake Rehabilitation, Penmar Water Quality Improvements, South Los Angeles Wetlands, and Westside Park Rainwater Irrigation.

Prop O projects, overall, will make significant improvements to water quality in the City. The City would not have been able to meet TMDL requirements had it not been for Prop O projects. **Exhibit 13**, below, identifies 17 Prop O projects that have been (and will be) critical to directly or indirectly meeting TMDL requirements for trash, bacteria, and other pollutants. The funding for these projects represents 67 percent of total bond funds.

EXHIBIT 13: KEY PROP O PROJECTS FOR TMDL COMPLIANCE

Project	Council/Mayor Approved Budget (December 2014)	Status (as of July 2015)
Catch Basin Inserts and Coverings Phase I	\$14,702,886	Completed
Catch Basin Inserts and Coverings Phase II	\$9,360,788	Completed
Catch Basin Inserts and Coverings Phase III	\$44,500,000	Completed
Catch Basin Inserts and Coverings Phase IV	\$6,160,000	Construction
Santa Monica Bay Low Flow Diversions Pkg 1	\$4,613,087	Completed
Santa Monica Bay Low Flow Diversions Pkg 2	\$2,032,341	Completed
Santa Monica Bay Low Flow Diversions Pkg 3	\$12,079,108	Completed
Santa Monica Bay Low Flow Diversions Pkg 3 Phase 2	\$14,194,469	Construction
Santa Monica Bay Low Flow Diversions Pkg 4	\$3,891,062	Completed
Echo Park Lake Rehabilitation	\$45,296,789	Completed
Machado Lake Wilmington Drain	\$21,049,911	Construction
Machado Lake Ecosystem Restoration	\$110,457,563	Construction
Penmar Water Quality Improvements Phase I	\$17,754,800	Completed
Penmar Water Quality Improvements Phase II	\$5,830,200	Bid & Award
Temescal Canyon Park Stormwater Phase I	\$14,947,435	Post-Construction
Temescal Canyon Park Stormwater Phase II	\$4,398,565	Bid & Award
Westchester Stormwater BMP (now ARGO) ^a	\$2,574,787	Pre-Design
Total	\$333,843,791	
Percent of Bond Funds	67%	

^a Westchester/ARGO budget as of July 2015, after project restart.

It is still too early to determine the full success of Prop O. Furthermore, in many cases it is difficult to quantify the extent to which improvements in water quality are due specifically, or wholly, to Prop O projects, as compared to other initiatives in the City's broader strategic planning framework, the Water Quality Compliance Master Plan for Urban Runoff (WQCMPUR), weather patterns, and/or activities outside of the City's jurisdiction. LASAN conducts water quality monitoring

throughout the City, including Prop O project sites, to determine compliance with TMDL requirements. LASAN prepared a Monitoring Plan and Prop O Projects Optimization report (January 2015) that outlines the approach to water quality monitoring at eleven completed project sites. As described in this report, this monitoring and “optimization” is intended to provide time to measure, evaluate, and modify project elements so they achieve the intended goals. The benefits of individual projects, as well as the overall Prop O program, will be clearer as LASAN completes optimization and conducts additional water quality monitoring.

LASAN prepares “Project Information” sheets for completed projects to summarize project purpose, location, design features, ancillary benefits, operations and maintenance, and water quality monitoring. These summary sheets, along with the results of the Monitoring Plan completed in December 2015, will help measure performance of Prop O projects.

Overview of Prop O Performance

While LASAN is gathering data from Prop O project sites, the City has not yet implemented a formal performance measurement reporting framework for Prop O projects. However, with 22 projects completed, and several others near completion, there are a number of performance indicators that generally demonstrate high quality project outcomes have been achieved. It should be noted that the reported performance measures cited in the following examples were not independently verified by this audit:

- As reported by LASAN at the April 2013 COAC meeting, the City is at 100 percent compliance with the trash TMDLs for the Los Angeles River and Ballona Creek watersheds, three years ahead of the deadline. The trash TMDLs are technology-based.⁷ Thus, the City achieved compliance by installing catch basin screens and inserts under Prop O. The table below, based on Los Angeles Regional Water Quality Control Board (LARWQCB) and LASAN reports, illustrate TMDL compliance:

Watershed	2012/2013 Target	2012/2013 Actual	2013/2014 Target	2013/2014 Actual
LA River ⁸	80% Reduction	91.5%	90 %	91.5%

⁷ A technology based TMDL is one that can be met by installing a specific technology – in this case catch screens for trash. By comparison, for a metric-based TMDL the City must achieve a specific concentration of a pollutant, for example a chemical or nutrient.

⁸ Los Angeles Regional Water Quality Control Board, Staff Report: Reconsideration of Certain Technical Matters of the Trash TMDLs for the Los Angeles River Watershed and the Ballona Creek Watershed, April 2015; and RB4 Staff Report Trash LAR & BC April 2015.pdf

Ballona Creek ⁹	90% Reduction	98%	97%	98%
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- The Number of bacteria TMDL exceedances in Santa Monica Bay has declined significantly, as documented in an LASAN report.¹⁰ According to a LASAN evaluation, there was a measurable decline in exceedances following the completion of the Prop O funded Santa Monica Bay Low Flow Diversion Upgrades, completed in 2010. These upgrades improved existing low flow diversions (LFD), put in place between 2001 and 2007. The number of summer exceedances per year dropped from a high of almost 350 in 2005, to 160 in 2006 after six new LFD installations, to 60 in 2010 after completion of the Prop O LFD upgrades.
- In January 2013, LASAN reported to the COAC that the Westside Stormwater Best Management Practices project has reduced bacteria counts by 90 percent for both dry and wet weather. LASAN also noted that most projects at that point in time were not as effective as they will be once the optimization phase is complete.

Based upon interviews performed and documentation reviewed for Prop O project performance metrics, the following was noted:

- A primary metric of project performance for Prop O was achieving Total Maximum Daily Load (TMDL) requirements, a regulatory term in the U.S. Clean Water Act that describes a value of the maximum amount of a pollutant a body of water can receive while still meeting water quality standards. Certain Prop O projects, including Catch Basin Opening Screen Covers, Santa Monica Bay Low Flow Diversion (SMBLFD) Upgrades, Echo Park Lake, Machado Lake, Temescal Canyon Park Stormwater Penmar Water Quality Improvements, and Westchester Stormwater BMP, were deemed necessary to help meet TMDL requirements for trash, bacteria, and/or other pollutants.
- For those projects with technology-based TMDLs, such as the Catch Basin Inserts, and for projects with dry weather TMDLs, such as bacteria levels (SMBLFD), LASAN has realized improvements in TMDL compliance, documented by the LARWQCB, and/or in LASAN published reports¹¹.

⁹ Los Angeles Regional Water Quality Control Board, Staff Report: Reconsideration of Certain Technical Matters of the Trash TMDLs for the Los Angeles River Watershed and the Ballona Creek Watershed, April 2015; and RB4 Staff Report Trash LAR & BC April 2015.pdf

¹⁰ BOS, Santa Monica Bay Dry-Weather Exceedances LFD Correlation Summary in LA SAN_SMB Dry-Weather Exceedances_LFD Correlation Summary.2015.04.17.pdf

¹¹ See footnotes 9, 10, and 11.

- For other projects, it was difficult to determine success in meeting TMDLs due to factors such as the time required for projects to mature and lack of rain.
- No formal policies and procedures were developed for the monitoring of overall Prop O performance metrics and progress beyond TMDLs.
- The “Project Information” documents that the LASAN and the BOE prepared for completed projects provided an overview of each project; however, no formalized, defined metrics were developed to measure each Prop O project beyond TMDLs.
- As no metrics were defined, LASAN was not monitoring the projects against a set definition.
- There was no follow-through or comparison of the initial project score with project outcomes for completed projects.
- The LASAN presented general information on project performance to the COAC at monthly meetings; however, it was not until December 2014 that LASAN presented a water quality Monitoring Plan to the COAC. This plan, while an important step, is focused on water quality, and not the broader program benefits.

Formal, defined performance metrics, including interim metrics, along with the mechanisms to measure, monitor and present these metrics for individual projects along with the overall program should be developed and reported during monthly reporting to the Mayor’s Office, CAO, Board of Public Works, AOC and the COAC.

Failure to monitor and report on project performance metrics lessens the effectiveness of oversight controls and makes it difficult to determine whether bond funds were spent effectively and for the intended purpose. LASAN is currently working with the COAC to measure, monitor, and report on project performance metrics, but until recently has not prioritized the development of procedures to measure, monitor and report on performance metrics.

Example Project Performance Summary

There is currently no overall summary or “report card” of project performance that provides a straightforward evaluation of project progress and success, including how projects are performing as compared to expectations. In order to assess project performance, the audit team compiled information from a number of sources. **Exhibit 14**, on the next page, provides an example

performance summary of the seven selected projects based on information obtained during the audit.

EXHIBIT 14: EXAMPLE PERFORMANCE EXPECTATIONS FOR SEVEN SELECTED PROP O PROJECTS

Project Name and Status	Original Scoring (maximum = 100)	Purpose (In Project Information)	Ancillary Benefits	Water Quality (WQ) Monitoring	Outstanding Issues	Overall Success
South Los Angeles Wetlands Park (Completed)	87	Meet TMDL requirements for metals, nutrients, bacteria; increase beneficial uses	Green space, recreation and education	Samples in 2013 and early 2014 showed high dry weather reductions for metals; bacteria variable; December 2014 storm monitoring had lower concentrations of contaminants	Improved water quality and stabilization of bacteria levels	WQ benefits mixed; Good education, community use, habitat components
Santa Monica Bay Low Flow Diversion (Pkgs 1 and 3) (Completed)	91	Meet bacteria TMDLs by reducing polluted stormwater runoff	Improved aesthetics of Santa Monica Bay Beaches and reduced closures	Significant reduction in bacterial TMDL exceedences		Excellent WQ benefits
Westside Park Rainwater Irrigation (Completed)	None (replaced La Cienega/Fairfax project)	Meet TMDL requirements for trash, metals, bacteria, and sediment in the Ballona Creek Watershed	Community recreational park with numerous improvements	Single sample December 2014 indicates flow challenges; detectable contaminants in influent and effluent	Need to evaluate operation of EPIC system	Moderate WQ benefits; good community use benefits
Machado Lake – Phase 1 (Wilmington Drain) (In Progress)	91	Meet TMDL requirements for chemicals, odors, nutrients, trash and remove contaminated sediment	Provide recreational and education activities and improved wildlife habitat	NA – in construction	NA – in construction	Incomplete
Echo Park Lake Rehabilitation (Completed)	90	Improve WQ in the lake and contribute to improved WQ in the LA River Watershed; reduce use of municipal water required to maintain water level; meet numeric TMDL	Numerous park amenities Project has won several awards	Samples in October and December 2013 were good; no pesticides or PCBs, low nutrients	Wet weather TMDL compliance	Good WQ benefits; excellent community use benefits
Penmar Water Quality Improvements (Phase 1) (Completed)	91	Meet wet weather TMDLs for bacteria at Santa Monica Bay Beaches; prevents 3 million gallons of stormwater from entering Bay	Protects and enhances community uses in the park to address water supply, water quality, flood reduction, storm water reuse, recreation	Monitoring dry and wet weather flows and capture; reduction of bacteria levels	Additional monitoring of wet weather flow	Good diversion of dry weather flows; excellent regional example of stormwater capture

Recommendation:

LASAN should:

13.1 Develop and regularly report project-specific and overall Prop O performance metrics.

Section IV. Contract Conditions

BOE could improve consistency and clarity by updating the Master General Conditions and Project Delivery Manual to reflect current policies and procedures. These revisions apply beyond Prop O. The following are presented as observations regarding documentation.

Finding 14: BOE Master General Conditions agreement for contractors did not reflect current City insurance requirements and procedures.

The Master General Conditions of the BOE agreement for Contractors related to Contract Article 00317 Insurance could be improved with certain revisions to terminology. These recommended changes to the Master General Conditions will reflect consistency between what the City already requires in its "*Track4LA*" Insurance & Bonds Compliance System (the City's on-line submission portal for Certificates of Insurance (COI) and compliance) and the CAO Risk Management "*Procedure Manual for City Departments*", both of which already provide for some of these leading practices in the industry. In addition, these improvements, if incorporated into the standard agreement, could, in some cases, more effectively protect the City from risk and reflect leading practices adopted by similar project owners.

We reviewed the Master General Conditions of the BOE agreement related to Article 00317 Insurance and noted the following:

- A) Section A (5) General – Priority of Coverage – This section notes that the Contractor's insurance shall not call on the City's program for contributions in the event of claims. This requirement is usually stated or noted in the contract that the Contractor's policy "shall be primary and non-contributory as regards additional insured coverage" with such wording required to be included in the "Descriptions" section of the Contractor's COI.

The priority of coverage should state the following in the contract: "The Contractor's policies shall be primary and non-contributory as regards additional insured coverage". As well, the contract should require that such wording be included in the "Descriptions" section of the Contractor's COI.

These requirements are already validated and required on the City's *Track4LA* site.

- B) Section (B) Aggregate Limits/Reduction of Coverage – This section addresses the concern associated with insurance aggregate limits being reduced by claims of the Contractor on other projects and the requirement to notify the City of same and restore coverage to the required limits.

The current requirements/terminology in the contract could be improved to reflect that aggregate insurance limits shall apply independently on each BOE project. It is common to now see insurance requirements reflect the following in the contract:

- 1) Require the Contractor to provide policy coverage whereby the General Liability aggregate limits required for insurance coverage will be applied on projects as follows: "General Aggregate Limit Applies per Project". This typically requires an endorsement to the policy by the Contractor and their Carrier(s). The BOE should require the COI to document "General Aggregate Limit Applies Per Project" and that this box be checked on the ISO Accord COI form.
- 2) For Section (J) Typical Limits of Liability of the agreement, modify the contract to require a form and limit of "Umbrella Coverage" since there are currently no umbrella coverage requirements spelled out in the BOE's Master General Conditions. When added, the aggregate umbrella amount can be set depending on the nature of the project and the dollar amount of the contract. This ensures that there is umbrella coverage over and above the other insurance aggregates, in many cases something the City already requires.

- C) Section (K) Contract Bonds covers requirements associated with the surety bonds provided by the Contractor to BOE for "payment" (Payment Bond) and "performance" (Performance Bond). While the requirements state the bonds shall be no less than 100% of the contract amount, the "Payment Bond" paragraph does not appear to specifically include subcontractors, *regardless of tier*. CAO Risk Management stated that there have been no past instances of where this has been an issue.

The CAO could consider utilizing bonding requirement terminology to include subcontractors (regardless of tier). The contract should be modified to reflect: "The "Payment Bond" (Material and Labor Bond) shall be for not less than one hundred percent (100%) of the Contract Price, to satisfy claims of material suppliers, **subcontractors**

(regardless of tier), and mechanics and laborers employed by it on the Work.”

Including proper insurance requirements noted above within the contract documents will make the City’s contract consistent with what the *Track4LA* and the CAO’s “Risk Management Procedure Manual for City Departments” already reflect and require, and reflect best practices for similar owners.

Recommendation:

BOE should:

14.1 Review and update insurance and indemnification provisions in the Master General Specifications to reflect current City practices.

Finding 15: BOE's Project Delivery Manual does not reflect City Risk Management and Board of Public Works policies and procedures for review and approval of bonds and insurance for contracts. As a result, it is not clear which entity is responsible for ensuring requirements are met.

The Master Specification "General Conditions", Section 00317 "Insurance" states the insurance requirements for contractors that perform work on BOE projects. Coverage is evidenced by the Contractor's submission of a Certificate of Insurance (COI) via the City's CAO *Track4LA* portal showing types of insurance coverage afforded, limits of coverage, carriers, cancellation notification requirements, additional insured coverage, and other contractual requirements. The City's *Track4LA* internet-based insurance compliance system is available 24 hours a day, 7 days a week.

The City's Risk Management Procedure Manual for City Departments states that it is the responsibility of the assigned Risk Management Official within the Department (of Public Works) to verify that each department contract incorporates appropriate indemnity and insurance requirements or has been referred to CAP Risk Management for Review. BOE's Project Delivery Manual states that the CAO Risk Management Section reviews and approves bonds and insurance. In practice, the Board of Public Works Contracts, Bonds & Insurance Section reviews contractor submissions to *Track4LA* on an ongoing basis to ensure that contractor insurance matches the requirements as defined on the form 146IR that is specific to each project.

The Board of Public Work's current procedure is to conduct ongoing audits of insurance requirements and expiration dates for contractors. The information is tracked and maintained in a Board database. The Bonds & Insurance Section works with the Project Manager if there are any deficiencies in insurance. The Project Manager and contractor are notified two to three weeks in advance of policy expiration in order to provide time for the contractor to submit renewal information to *Track4LA*.

Recommendation:

BOE should:

- 15.1 Update the Project Delivery Manual to more accurately reflect the current roles and responsibilities of the City Risk Management Section, Board of Public Works, and Project Manager, as relates to review and approval of contractor insurance and bonds.**

GLOSSARY OF KEY TERMS

Administrative Oversight Committee (AOC) was specified in Proposition O, and is composed of the City Administrative Officer (Chair), the Chief Legislative Analyst, a representative of the Mayor's Office, a Board of Public Works Commissioner and the General Manager from the Department of Water and Power. The AOC is responsible for developing and reviewing project criteria and overseeing and directing the program and the projects in order to comply with approved schedules and budgets.

Bureau of Engineering (BOE) is responsible for the City's vast network of infrastructure within the public right of way, and includes the planning, design, and construction of public facilities, and the management and delivery of voter-approved public bond funds. The BOE's Proposition O Project Implementation Program Manager has primary responsibility for keeping approved projects in scope, on time, and on budget.

Bureau of Sanitation (LASAN) controls the discharge of sewage, industrial wastes and storm waters into sewers, storm drains, open channel and navigable waters; inspects and maintains open storm water channels, and operates and maintains all structures related to sewage and stormwater, including wastewater treatment plants. LASAN's Proposition O Project Planning Program Manager leads in the planning, development, and review of project proposals

Citizen Oversight Advisory Committee (COAC) is a nine-member committee appointment by the Mayor and Council to develop and recommend Proposition O projects, work with the AOC in review and assessment of project proposals, monitor the program, and advise and report to the Mayor and Council on program status.

City Administrative Officer (CAO) is the chief financial advisor to the Mayor and the Council and reports directly to both. The CAO's responsibilities including managing the City's debt program. The CAO is the chair of the Administrative Oversight Committee.

Clean Water Act (CWA), passed in 1972, establishes the basic structure for regulating discharges of pollutants into the waters of the United States and regulating quality standards for surface waters. In California, the CWA is implemented by the State Water Quality Control Board, and in Los Angeles by the Los Angeles Regional Water Quality Control Board (LARWQCB).

Dry Weather Flow refers to the water flow in a sewer during periods of dry weather with minimum infiltration.

Green Infrastructure or Natural Solution Projects refers to an approach to water management that protects, restores, or mimics the natural water cycle; projects that use natural solutions, for example, plant life and oxygen to remove pollutants from storm water runoff.

Optimization refers to an establishment and stabilization period for Prop O projects to allow for natural processes to be optimized by establishing the optimal balance between plant life, the amount of runoff and the amount of oxygen, and a mechanical system to deliver the runoff at the optimal time and amount.

Proposition O (Prop O), Clean Water, Ocean, River, Beach, Bay Storm Water Cleanup Measure General Obligation Bond was passed by the citizens of Los Angeles in November 2004. Prop O provides \$500 million to be expended on projects that provide water quality benefits and have as their primary purpose the reduction of pollutant loads to the impaired waters of the City to meet water quality standards.

Total Maximum Daily Load (TMDL) is an estimate of how much of a pollutant, or group of pollutants, a water body can absorb without becoming polluted (i.e. not meeting water quality standards). TMDLs are developed for a pollutant or group of pollutants in water bodies that are listed in each state's list of impaired waters. A key objective of Prop O is compliance with TMDL requirements in Los Angeles waters.

Water Quality Monitoring is a fundamental tool in the management of freshwater resources, and includes a protocol for design and implementation of monitoring surface and groundwater; details of sampling and analytical methods; and guidance on data analysis and presentation.

Wet Weather Flow refers to water entering storm drains during rainstorms/wet weather events.

APPENDIX I: ACTION PLAN

Finding	Page	Recommendation	Page	Entity Responsible for Implementation	Priority
Project Management					
1. The program has maintained a large balance of unexpended bond funds over time. As a result, since FY 2010, the City has incurred an average of \$1.36 million per year in net interest costs on idle funds.	#	<p>1.1 The CAO should work with the Controller-Operations Division, City Attorney and BOE to develop improved processes that would prevent the accumulation of excess, idle cash within the City's bond Funds. These could include developing procedures to:</p> <p>a. Better estimate the amount and timing of cash flow needs and periodically reassess the cash needs and the proposed bond issuances after taking into account project delays, cost savings and availability of other sources of funds, such as grants and accumulated interest.</p> <p>b. Periodically monitor available cash balances and consider the use of unexpended bond funds from prior issuances for eligible future projects before issuing additional bonds.</p> <p>The City should also:</p>		CAO, Controller, City Attorney, BOE	A

APPENDIX I: ACTION PLAN

Finding	Page	Recommendation	Page	Entity Responsible for Implementation	Priority
		<p>c. Consider, where feasible, adding an appropriations clause to eliminate the need for having cash for the full amount of the contract at the time of execution of contracts.</p> <p>d. Explore the use of short term financing, such as commercial paper, to provide cash for the early phases of approved projects and subsequently retire those instruments with the proceeds from bond sales.</p>			
2 The CAO did not timely submit the annual SB 165 report to the Mayor and City Council as required by State Statute, lessening the relevance of this oversight control.	#	2.1 Implement procedures to ensure the CAO timely submits SB 165 reports in accordance with statute to the governing bodies to strengthen oversight controls.	#	CAO	A
	#	2.2 Prepare a single annual Prop O report that clearly summarizes activities, project expenditures, and performance for an entire fiscal year.	#	CAO	A

APPENDIX I: ACTION PLAN

Finding	Page	Recommendation	Page	Entity Responsible for Implementation	Priority
3 The Monthly Status Reports of Prop O projects submitted to various City offices and committees contained inaccurate project expenditure data, lessening the effectiveness of oversight controls.	#	3.1 Perform a monthly reconciliation of the reports, and automate the monthly reporting process, including programming the Merlin system to apply CAP rates to increase the accuracy of the monthly reports.	#	BOE	A
4 Project scoring criteria were not fully developed at the start of the program, and evolved over time. However, LASAN did not provide consistent documentation of the changes, making it difficult to determine whether eligibility criteria were followed for some projects.	#	4.1 Always evaluate projects, and document the evaluation process, based upon a single set of established criteria to ensure all projects provide the highest benefit to water quality and meet the intent of the bond language.	#	LASAN	B
5 It will be important for LASAN and CAO to develop a more comprehensive tracking and reporting system as projects move from optimization to operations and maintenance to ensure compliance with Prop O bond funding requirements.	#	5.1 Ensure that there is adequate funding to support Prop O project operations and maintenance as projects transition out of the optimization phase.	#	LASAN and CAO	B
	#	5.2 Carefully track the timing and conclusion of optimization and the transition to operations and maintenance.	#	LASAN	B

APPENDIX I: ACTION PLAN

Finding	Page	Recommendation	Page	Entity Responsible for Implementation	Priority
6 Prop O expenditure files were not maintained in a consistent and organized manner by the Office of Accounting resulting in delays in obtaining information necessary for auditing procedures.	#	6.1 Implement a methodology to concisely organize hardcopy expenditure files to allow files to be properly identified and tracked.	#	Department of Public Works, Office of Accounting	C
Project Costs					
7 BOE did not have a system in place to validate consultant hours and rates. As a result, BOE paid selected consultants for hours worked that consultants did not, in turn, pay to employees.		7.1 Work with the City Attorney to revise the contract language to ensure that consultants compensate their employees for actual hours worked.	#	BOE	A
8 The BOE did not adjust the amounts calculated for indirect costs for Prop O expenditures as reported in monthly reporting when new cost allocation plan rates for the correct fiscal year were released by the Controller's Office, leading to inaccurate reporting of program and project expenditures.	#	8.1 Perform a "true-up" of all indirect costs calculated through each fiscal year with the updated, approved rates provided by the Controller's Office, and include these updated amounts in monthly reporting to the governing bodies.	#	BOE	A

APPENDIX I: ACTION PLAN

Finding	Page	Recommendation	Page	Entity Responsible for Implementation	Priority
9 The BOE did not review or potentially adjust consultant and sub-consultant employee hourly rates and support for labor multipliers after the Master Services Agreement was approved. As a result, rates and multipliers were not evaluated over time, potentially resulting in overbillings to BOE.	#	9.1 Develop and implement a policy to review and approve submitted multiplier information for consultants and sub-consultants at the beginning of the contract and then again after three years for those firms who are issued new task orders, and revise the Project Delivery Manual accordingly.	#	BOE	B
10 The LASAN, BCA, and DPW Office of Accounting did not utilize clear timesheet task and subtask codes, making it difficult to determine if internal labor project costs were categorized to the proper Prop O project phase.	#	10.1 Develop a more comprehensive and integrated system of codes that are detailed and useful for the Prop O projects and can be utilized for all Bureaus and the Office of Accounting.	#	LASAN and BCA	B
11 The BOE did not perform periodic audits of its consultants and sub-consultants billings and rates on selected projects to provide better oversight of project costs. As a result, the BOE cannot verify that consultant billings, associated rates, and hours billed are not being overstated.	#	11.1 Consider establishing procedures to periodically verify consultant and sub-consultant billing rates on a sample basis to ensure accuracy.	#	BOE	B

APPENDIX I: ACTION PLAN

Finding	Page	Recommendation	Page	Entity Responsible for Implementation	Priority
Project Oversight and Monitoring					
12 BOE did not utilize an independent surveyor to verify payments for a unit price contract, resulting in a conflict of interest which could lead to BOE's overpayment of the contractor.	#	12.1 Make all arrangements for the procurement of an independent firm, separate from the Contractor, for projects requiring the expertise of a surveyor or other professionally designated party for unit price, quantity, and payment purposes.	#	BOE	A
13 LASAN has been slow to report on interim or final project outcomes, making it difficult to measure project effectiveness and compliance with bond requirements.	#	13.1 Develop and regularly report project-specific and overall Prop O performance metrics.	#	LASAN	B
Contract Conditions					
14 BOE Master General Conditions agreement for contractors did not reflect current City insurance requirements and procedures.	#	14.1 Review and update insurance and indemnification provisions in the Master General Conditions to reflect current City practices.	#	BOE	C
15 BOE's Project Delivery Manual does not reflect City Risk Management and Board of Public Works policies and procedures for review and approval of bonds	##	15.1 Update the Project Delivery Manual to more accurately reflect the current roles and responsibilities of the City Risk Management Section, Board of Public Works, and Project Manager, as relates	##	BOE	C

APPENDIX I: ACTION PLAN

Finding	Page	Recommendation	Page	Entity Responsible for Implementation	Priority
and insurance for contracts. As a result, it is not clear which entity is responsible for ensuring requirements are met.		to review and approval of insurance and bonds.			

A –High Priority – The recommendation pertains to a significant audit finding or control weakness within the context of the audit objectives. Due to the significance of the matter, immediate management attention and appropriate corrective action is warranted.

B –Medium Priority – The recommendation is not significant to the objectives of the audit but warrants the attention of those charged with governance. Reasonably prompt corrective action should be taken by management to address the matter. Recommendation should be implemented no later than six months.

C –Low Priority – The recommendation is a deficiency or best practice that does not warrant the attention of those charged with governance but is worth noting. The timing of any corrective action is left to management's discretion.

APPENDIX II – FINANCIAL SCORECARD

Finding	Page	Category	Financial Impacts
1 The program has maintained a large balance of unexpended bond funds over time. As a result, since FY 2010, the City has incurred an average of \$1.36 million per year in net interest costs on idle funds.	#	Cost Avoidance	Reducing the balance of unexpended bond funds to an amount that is reasonable and takes into account program and project uncertainties could result in annual interest expense savings. Reducing the unexpended cash balance from the current average of \$171 million to \$100 million would have resulted in savings of approximately \$1.36 million per year, and \$6.8 million over the last five years.
7 BOE did not have a system in place to validate consultant hours and rates. As a result, BOE paid selected consultants for hours worked that consultants did not, in turn, pay to employees.	#	Cost Recovery	From a sample of invoices for the seven selected projects, the audit team reviewed 287 total pay period records from the ten consultants and found eight employee pay periods (2.5%) with costs that should have been disallowed totaling \$11,873.

We strive to identify and recommend actions that will result in real financial impact, whereby the City can achieve significantly more through cost savings and/or increased revenue than the cost of the audit function. The above dollar estimates are dependent upon various factors, such as full implementation of audit recommendations and should not be used as guaranteed amounts.

APPENDIX III – SCOPE & METHODOLOGY

Scope

The audit scope included the Proposition O program as a whole from November 2004 (inception) through December 31, 2014, though the transaction review focused only on the seven specific projects selected through a risk assessment performed by the Controller's Office. As noted in the task order from the City, the audit focused on these seven projects (Objectives 1 through 8), except for assessing program governance and oversight (Objective 1), bond transactions and expenditures (Objective 7), the reasons for inactive and canceled projects (Objective 10) and for evaluating processes to capture and report costs (Objective 9), including general program costs not charged to specific projects.

The audit pertained to the following Departments:

Department
Department of Public Works – Office of Accounting
Bureau of Contract Administration
Bureau of Engineering
Bureau of Sanitation
City Administrator's Office

Methodology

We conducted the 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. The audit involved a two-phase approach as follows:

PHASE I

- March 2015
- Data Gathering/Planning

Phase I, through interviews, walkthroughs, and review of pertinent laws, regulations and policies, consisted of obtaining a thorough understanding of the Prop O program, project oversight and accounting. During this phase, we assessed risk and significance, and identified preliminary issues and areas for

[Audit of Proposition O Projects](#)

APPENDIX III – SCOPE & METHODOLOGY

detailed test work. Upon completion of Phase I, a planning report summary was submitted to the Controller's Auditing Division for review and approval prior to commencing Phase II of the audit.

PHASE II

- April 2015 through September 2015
- Internal Control Testing
- Substantive Testing

Phase II included additional audit work to develop the issues identified in Phase I, as refined through discussion and approval by the Controller's Auditing Division management. The Controller's Auditing Division performed an analysis of the large cash balances as well as the interest rates related to bond proceeds.

The following individuals were interviewed during the course of the audit:

Name	Title	Department
Ching Ilagan	Assistant Director	Department of Public Works – Office of Accounting
Dina Colorado	Section Supervisor	Department of Public Works – Office of Accounting
Yolanda Antonio	Division Manager	Department of Public Works – Office of Accounting
Chris Smith	Chief Construction Inspector	Bureau of Contract Administration
Marc Wright	Principal Construction Inspector	Bureau of Contract Administration
Walter Bradley	Assistant Director	Bureau of Contract Administration
Iftekhar Ahmed	Project Manager I	Bureau of Engineering
James Zabala	Senior Manager II	Bureau of Engineering
Ken Redd	Deputy Chief Engineer	Bureau of Engineering
Kendrick Okuda	Project Implementation Program Manager	Bureau of Engineering
Kendrick Okuda	Project Implementation Program Manager	Bureau of Engineering
Monique Parker	Senior Management Analyst	Bureau of Engineering
Shahram Kharaghani	Program Planning Manager	Bureau of Sanitation
Wing Tam	Assistant Division Manager	Bureau of Sanitation
Alma Gibson	Physical Plant Analyst	City Administrator's Office
David Hirano	Chief Administrative Analyst	City Administrator's Office

APPENDIX III – SCOPE & METHODOLOGY

Ha To	Debt Management Analyst	City Administrator's Office
Patty Huber	Assistant City Administrative Officer	City Administrator's Office

Fieldwork was conducted from March 2015 through September 2015. During fieldwork, procedures were performed to address the audit objectives and support the findings and conclusions.

Procedures were performed to address the objectives, with sub-bulleted clarification of the numbered objectives, as follows:

1. Is the governance structure and oversight effective in achieving high quality project outcomes?

Approach: We conducted interviews with City management and reviewed the Proposition O Governance Structure (see Background section of report, #1. Program Structure and Governance, General Governance Structure) to obtain an understanding of the City's governance structure over Prop O as well as the City's process for defining high quality project outcomes. We identified and evaluated for accuracy Prop O performance metrics and the City's policies/procedures to monitor Prop O activities against the performance metrics. For the seven projects selected for testing by the Controller's Office based upon a risk assessment, we determined whether performance metrics were identified, evaluated, and met. We also determined whether the projects were managed per project guidelines. In addition, we evaluated whether high quality project outcomes were achieved for the seven projects based upon research performed on the projects, discussions with specialists and achievements made by the projects.

For additional testing of the governance structure, we selected a sample including one monthly, two quarterly, and 10 annual reports to City Council and obtained support for the date the reports were submitted. Our sample for the reports was based upon a population that included each monthly, quarterly and annual report submitted during the scope of the audit as noted above. We then tested the sample of reports to determine the reports were submitted timely. For two of the annual reports selected we obtained materials and documentation supporting the amounts reported and agreed key data and information to the support.

Conclusion: Overall, the Proposition O governance structure and the City's implementation of that governance structure has resulted in an effective program that meets the intent of the bond measure.

APPENDIX III – SCOPE & METHODOLOGY

2. Are there adequate systems in place to capture project costs?

Approach: We conducted interviews with City management to obtain an understanding of systems in place to capture project costs. We then selected a sample of 60 labor expenditure transactions totaling \$6,536 and 60 non-labor expenditure transactions totaling \$8,420,866 from the population of all labor (\$8,650,454) and non-labor (\$99,716,355) expenditures for the seven projects selected by the Controller's Office. For the sample selected we performed control testing and substantive testing. Control testing included testing of management reviews of the transactions and the documentation of the review in the systems. Substantive testing included vouching supporting documentation, including the voucher, vendor invoice and detailed billing documents, for each transaction to transaction detail reported in the systems to determine if the project costs were accurately reported in the systems.

Control and substantive testing was also performed related to indirect costs charged to the projects. Control testing included testing of the management review of the indirect cost calculations and the system used for calculating the costs. Substantive testing included a recalculation of the indirect costs charged to the projects. The December 2014 monthly report and the underlying records were selected for testing. The population included all monthly reports for the scope of the audit. Due to issues noted (see conclusion section below), it was determined not to select additional reports to test due to a lack of controls.

Conclusion: The results of interviews performed indicated the City utilized Financial Management Information System (FMIS) and Financial Management System (FMS) to capture project costs.

The results of our testing of 60 non-labor transactions supported that the systems listed above adequately captured project costs; however it does not appear project cost information is being pulled out of the systems accurately for monthly reporting. This issue was classified as a significant finding, See Finding 3. In addition, during testing of 60 labor transactions, a significant finding was noted related to the inaccuracy of the system in place to determine indirect costs, see Finding 8. During labor testing, it also could not be determined if all internal labor project costs were categorized to the proper Prop O phase code utilized during the budgeting process, see Finding 10 (classified as a medium priority finding). Lastly, a best practice was noted regarding the maintenance of project expenditure files. See Finding 6.

APPENDIX III – SCOPE & METHODOLOGY

3. Are costs accurately reported in Monthly reports to City Council?

Approach: We conducted interviews with key program and City personnel to gain an understanding of the City's Prop O monthly reporting process. We selected one Monthly report, December 2014, from the population of all monthly reports submitted during the scope of the audit and obtained materials and documentation supporting the sampled report. For the seven projects selected by the Controller's Office based upon a risk assessment, we compared project costs per reports (Merlin reports) from the FMS/FMIS systems to costs reported in the sampled Monthly report. In order to verify the FMS/FMIS project cost report data, we used the same Merlin reports generated from the FMS/FMIS systems to select a sample of 60 labor and 60 non-labor transactions (see details regarding amount of sample and population in Objective 2) from the population of all labor and non-labor expenditures for the seven selected projects and agreed supporting documentation, including the voucher amount, vendor invoice amount and detailed billing documents, for each transaction to transaction detail reported in the Merlin reports (see Objective 2 and 7 for additional details on this testing). As issues were identified (see conclusion), it was not deemed necessary to test an additional sample of Monthly reports as the issues identified would be consistent in all months. See also objective 2 related to indirect cost testing.

Conclusion: Costs were not accurately reported in Monthly reports as the Merlin reports did not agree or reconcile to the amounts reported. This issue was classified as a significant finding, see Finding 3. In addition, a significant finding was noted regarding the amounts calculated for indirect costs for Prop O expenditures as reported in monthly reporting when new cost allocation plan rates were released. See Finding 8.

4. Are contracts awarded based on established eligibility criteria?

Approach: We obtained the City's Prop O contract award eligibility criteria, two different sets of project selection criteria were used, and conducted interviews with key program and City personnel to gain an understanding of the criteria and the timing of criteria development. For the seven projects selected by the Controller's Office based upon a risk assessment, we obtained supporting documentation, including Board of Public Works minutes for approval to advertise the bid package and the approval of the bid package, the concept report for the project, the project evaluation score sheet for the project, City Council action for approval of the budget, and the application submitted to

APPENDIX III – SCOPE & METHODOLOGY

Board of Public Works, for all construction contracts related to the projects. We reviewed documentation to determine whether the City incorporated eligibility criteria into the contract awarding process during the project identification and selection process. We also compared documentation to the established eligibility criteria to determine contractors met the eligibility criteria.

Conclusion: The results of our testing indicated there were no significant findings and contracts were awarded based on established eligibility criteria. Issues were noted regarding documentation of project selection criteria for three projects which were identified as a deficiency that is not significant to the objectives of the audit. See Finding 4.

5. Are adequate processes in place to ensure contracts are awarded for reasonable amounts? Are the amounts reasonable in comparison with similar contracts for other jurisdictions and market conditions?

Approach: We conducted interviews with key program and City personnel to gain an understanding of the City's procurement/contracting procedures over Prop O, including the bidding and awarding processes. For the seven projects selected by the Controller's Office based upon a risk assessment, we obtained supporting documentation related to the contract awarding process including bids received from other vendors and documentation of the City's initial estimate of project cost. We reviewed documentation to determine whether the City incorporated contracts for reasonable amounts in comparison with other bids received and the City's estimates (see detailed information below). Due to the unique nature of the Prop O projects, direct benchmarking project performance and budgets with other entities and jurisdictions was determined to not be applicable as the information was not available to compare.

In order to complete the objective related to a comparison with similar contracts for other jurisdictions, the audit team reviewed a variety of literature on related project costs. After evaluating the documents and projects, it was determined that a comparison of projects in other jurisdictions would not be effective in determining whether Prop O project contracts were reasonable as compared to other jurisdictions for three reasons: (1) the types of projects constructed under Prop O were customized and specific to the individual project, natural conditions within the project site, time period in which the project was constructed, and local market conditions; (2) "soft" project characteristics such as environmental permitting, community meetings, and Endangered Species Act compliance

APPENDIX III – SCOPE & METHODOLOGY

cannot reasonably be compared across projects; and (3) existing literature on “natural treatment” projects such as wetlands, infiltration basins, and subsurface infiltration systems are highly variable.¹²

Conclusion: The results of our testing of the seven selected projects award documentation indicate adequate processes were in place resulting in contracts being awarded for reasonable amounts in comparison with other bids received and the City’s estimates. Testing related to comparisons of contract amounts to similar contracts for other jurisdictions and market conditions was determined not applicable (see approach for detailed information).

6. Are contract amendments and change orders properly approved?

Approach: We obtained the City’s procedures for approval of contract amendments and change orders and conducted interviews with key program and City personnel to gain an understanding of the City’s procedures, including the approval process for contract amendments and change orders. For the seven projects selected by the Controller’s Office based upon a risk assessment, we obtained the population of all contract amendments and change orders. From the population of all contract amendments and change for the seven projects, we selected a sample of 38 change orders/contract amendments. We reviewed documentation of contract amendments and change orders to determine the amendments and change orders were properly submitted, categorized, approved and finalized. Testing was also performed on 10 change orders to determine the change order was adequately supported.

Conclusion: For the sample tested of the seven selected projects, contract amendment and change orders were properly approved. Based upon the change order documentation provided, a timeline was developed for each of the seven projects, see Background, Exhibit 12.

¹² For example, Boston Water and Sewer Commission’s Stormwater Best Management Practices: Guidance Document (January 2013) identifies construction-only cost ranges that vary fivefold for a “stormwater wetland” and no cost estimates for several types of infiltration systems. A 1994 United States Environmental Protection Agency report, “Making Sense of Wetland Restoration Costs” reviewed cost data available at that time and found a range of \$5 per acre to \$1.5 million per acre to restore wetlands. Cost estimates prepared in 2012 for the California Coastal Conservancy to restore wetlands in the Upper Klamath Basin to help meet TMDL requirements ranged from \$15 million to \$27.5 million. In the City of Ontario, California, the recently completed Mill Creek Wetlands Recreation and Restoration Demonstration Project cost \$16 million. The project includes a series of natural water quality treatment ponds, a de-silting basin, UV light treatment, and wetland vegetation. These data illustrate a wide range of costs.

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7. Are transactions being properly recorded, and are expenditures adequately supported by documentation, including proper approval for payment?

Approach: We conducted interviews with key program and other City personnel to gain an understanding of the City's Prop O expenditure processing and internal control procedures, including procedures related to allocation of staff and overhead costs to projects. In addition, we obtained the City's procedures for approval of expenditures. For the seven projects selected by the Controller's Office based upon a risk assessment, we selected a sample of 60 labor and 60 non-labor expenditure transactions (see details regarding amount of sample and population in Objective 2) from the population of all labor and non-labor transactions for the seven projects. We obtained supporting documentation for the sample of expenditures selected (i.e., payroll support and documentation of employee time spent on Prop O activities; invoices, purchase orders, bidding forms and related documents). We performed testing on the sample of expenditures to determine internal control processes were followed in processing the expenditure transactions. In addition, we performed testing on the sample of expenditures to determine proper documentation was maintained to support the transaction, the expenditure was properly recorded, properly approved for payment, reasonable, and made in accordance with City policies and contract terms. Procedures were also performed on indirect costs (see Objective 2).

Based upon the interviews, we also obtained an understanding of the City's procedures for bond proceed transactions. Bond documentation, including the official statements, resolutions, and arbitrage reports, were obtained and reviewed. For all bond issuances, bond proceeds were traced from documentation supporting amounts received to the City's bank accounts and to the recording of the amounts in special funds used solely for the purpose of the Prop O program.

The Controller's Audit Division staff conducted additional analyses of Prop O bond balances, interest earnings, and interest expenditures for 2006 to 2015. The rates as calculated by the CAO's debt management staff indicated an average effective yield for each issuance, and a weighted average rate each year, which ranged from 3.622% in 2010 to 3.333% in 2015, for an overall rate of 3.398% over the five year period.

To derive an incremental cost rate, we considered the monthly interest yield on the City's reserve funds, as reported by the Office of Finance (formerly

APPENDIX III – SCOPE & METHODOLOGY

Treasurer), which ranged from a high of 2.7% to a low of 1.1%, for an overall average yield of 1.483% over the five year period.

Therefore, the difference between the interest expense and interest earnings noted an incremental interest expense rate of 1.915%. When applied to the excess or idle funds of \$71 million, equates to \$1,359,534 per year, or approximately \$6.8 million over five years.

Conclusion: The results of our testing determined expenditure transactions were supported by proper approval for payment and bond proceed transactions were properly recorded. However, the Controller's analysis of the large cash balances as well as the interest rates related to bond proceeds found a significant deficiency. See Finding 1.

During testing of 60 non-labor transactions and 60 labor transactions, it could not be determined if all internal labor project costs were categorized to the proper Prop O phase code utilized during the budgeting process, which was identified as a deficiency that is not significant to the objectives of the audit. See Finding 10. In addition, the calculation of indirect costs was not accurate, which was classified as a significant finding. See Finding 8.

8. Are payments to contractors in accordance with contract terms? Are costs billed allowable and reimbursable per contract and bond requirements, including costs related to change orders?

Approach: For the seven projects, we selected a sample of 60 labor and 60 non-labor expenditure transactions (see details regarding amount of sample and population in Objective 2) from the population of all transactions for the seven projects. We obtained supporting documentation for the sample of expenditures selected (i.e., payroll support and documentation of employee time spent on Prop O activities; invoices, purchase orders, bidding forms and related documents). We performed testing on the sample of expenditures to determine the expenditures were made in accordance with contract terms and were allowable and reimbursable per contract and bond requirements, including costs related to change orders. We also performed testing of consultant billings and rates. Lastly, contract documents were reviewed.

Conclusion: The results of our testing noted various issues regarding consultant billings and contract documents. A finding was identified related to consultants billing and being reimbursed for hours worked over 40 hours per week by employees who were not compensated for the hours over 40. See

APPENDIX III – SCOPE & METHODOLOGY

Finding 7. Additional information related to this finding is also included in the Financial Scorecard (Appendix II). A significant deficiency was also identified related to a lack of an independent verification of unit pricing. See Finding 12. Deficiencies were also detected that are not significant to the audit objectives but warrant the attention of those charged with governance. These deficiencies include a lack of periodic review of consultant direct labor multiplier rates (Finding 9), lack of performance of periodic audits of consultant and sub-consultant billings and rates (Finding 11). A documentation update issue was also identified related to the Master General Conditions agreement for contractors (Finding 14).

9. Are project costs appropriately categorized by phase? For completed projects, this will include assessing costs charged to “optimization” as capital project costs, rather than as operations or maintenance costs.

Approach: For the seven projects, we selected a sample of 60 labor and 60 non-labor expenditure transactions (see details regarding amount of sample and population in Objective 2) from the population of all expenditure transactions for the seven projects. We obtained supporting documentation for the sample of expenditures selected. The supporting documentation included timesheets and MERLIN reports (contained phase/task information for the sample) for labor expenditures and invoices and MERLIN reports (contained phase/task information for the sample) for the non-labor expenditures. We also obtained the MERLIN Task Code Description Report, the BOE Task Code Description Manual, and the LASAN Task Code Description Manual. We performed testing on the sample of expenditures to determine the expenditures were appropriately categorized by project phase. In addition, for the seven selected projects, we determined whether the projects were completed during the scope of our audit. If a project was completed, we determined if any optimization costs were charged to the project. If optimization costs were charged to a selected project, we evaluated the costs to determine they were capital projects costs, rather than operations and maintenance costs. We also determined the costs were appropriate by evaluating them against established criteria for defining optimization. For the seven selected projects, six projects were completed during the scope of our audit. For the six completed projects, four projects had optimization costs charged to the project. From this population of optimization expenditures for the completed projects, we selected a sample of five optimization expenditure transactions and obtained support for

APPENDIX III – SCOPE & METHODOLOGY

the transactions. For each sampled transaction, we determined the project was completed prior to the optimization expenditure and evaluated the optimization cost against established criteria for defining optimization and capital improvement requirements. Lastly, a sample of 17 program management and planning/feasibility costs were selected for testing from the population of all general program costs for program management and planning/feasibility costs. Utilizing this sample, we tested to determine whether the general costs were properly coded or should have been charged to a specific project code.

Conclusion: The results of our testing indicated there were no significant findings as project costs were appropriately categorized by phase and costs charged to optimization were capital project costs, not operations or maintenance costs. During testing of the sample of 60 labor and 60 non-labor expenditure transactions, the 5 optimization expenditures, and the 17 general program costs, issues were noted regarding the transactions being categorized by phase and/or the information to support how the costs were charged. See Finding 10. This deficiency was not significant to the objective of the audit but does warrant the attention of those charged with governance.

For the sample of five optimization expenditure transactions, the project the transaction was associated with was completed prior to the optimization expenditure.

A best practice was identified related to the tracking and reporting mechanism for optimization expenditures. See Finding 5.

10. Was there a reasonable basis for cancelling projects? What is the reason for inactive projects?

Approach: We conducted interviews with key program personnel to identify and gain an understanding of cancelled and inactive projects, including the reason for the cancellation or inactivity and the process to cancel a project. We obtained a list of cancelled and/or inactive projects along with documentation supporting the cancelled/inactive status of each project. We determined there were two cancelled and no inactive projects during the scope of our audit. We reviewed the documentation to determine the documentation adequately supported the cancelled status of the project.

Conclusion: For each cancelled project, the City maintained adequate documentation to support the cancelled status of the project. No issues noted.

APPENDIX IV – DEPARTMENTS' RESPONSE and ACTION PLANS

As part of our audit protocol, we requested action plans from the three primary Departments involved in this audit, which are attached in the following pages.

CITY OF LOS ANGELES
INTERDEPARTMENTAL CORRESPONDENCE

Date: April 20, 2016

To: Farid Saffar, CPA, Director of Auditing
City Controller Office

Ken R Redd For
From: Gary Lee Moore, City Engineer
Bureau of Engineering

Subject: **FINAL DRAFT AUDIT OF PROPOSITION O PROJECTS**

Enclosed are the electronic files of the Final Draft Audit (dated March 31, 2016) with Bureau of Engineering's (BOE) edits, and the table of BOE's Initial Action Plan. Our edits are found on pages 6, 7, 8, 9, 10, 58, 59, 60, 61, 63, 64, 65, 70, 71, 72, 84, 90, 91, 92, 93, 95, 96, 98, and 100 of the word document.

If you any questions, please contact Ken Redd, Deputy City Engineer, of my staff, at (213) 485-4906.

GLM/KRR/KO:tlw

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Enclosure

Report Title:
 Department responsible for Implementation:

Audit of Proposition O Projects
PW Bureau of Engineering
 Initial Action Plan

Finding Number	Summary Description of Finding	Rec. No.	Recommendation	DEPARTMENT REPORTED INFORMATION		
				Current Status	Basis for Status	Target Date for Implementation
Section I Project Management						
3	The Monthly Status Reports of Prop O projects submitted to various City offices and committees contained inaccurate project expenditure data, lessening the effectiveness of oversight controls.	3.1	Perform a monthly reconciliation of the reports, and automate the monthly reporting process, including programming the Merlin system to apply CAP rates to increase the accuracy of the monthly reports.	Implemented	<i>The BOE implemented improvements to the preparation of the Monthly Report. The Monthly Report now includes a query of all expenditures from the project inception through the current reporting period. In addition, custom individual project expenditure queries have been created in the Merlin System. This improves the reliability and consistency of future expenditure queries. CAP rates are applied at the time they become valid, as instructed by the Controllers Office.</i>	<i>Implemented in Dec. 2015</i>
Section II Project Costs.						
7	BOE did not have a system in place to validate consultant hours and rates. As a result, BOE paid selected consultants for hours worked that consultants did not, in turn, pay to employees.	7.1	<i>In future contacts, the BOE will work with the City Attorney to revise the contract language to ensure that consultants compensate their employees for actual hours worked.</i>	In Progress	<i>Upon completion of the Final Audit, the BOE will draft the revised contract language and a submit the draft to the City Attorney for review.</i>	<i>Six months after the completion of the Final Audit</i>
8	The BOE did not adjust the amounts calculated for indirect costs for Prop O expenditures as reported in monthly reporting when new cost allocation plan rates for the correct fiscal year were released by the Controller's Office, leading to inaccurate reporting of program and project expenditures.	8.1	Perform a "true-up" of all indirect costs calculated through each fiscal year with the updated, approved rates provided by the Controller's Office, and include these updated amounts in monthly reporting to the governing bodies.	Implemented	<i>The BOE has implemented a procedure to "true-up" all indirect costs. New CAP rates are applied at the time they become valid, as instructed by the Controllers Office. The indirect costs are updated in the Monthly Report at the time the new CAP rates are applied.</i>	<i>Implemented in Dec. 2015</i>

Report Title:
 Department responsible for Implementation:

Audit of Proposition O Projects
PW Bureau of Engineering
 Initial Action Plan

Finding Number	Summary Description of Finding	Rec. No.	Recommendation	DEPARTMENT REPORTED INFORMATION		
				Current Status	Basis for Status	Target Date for Implementation
9	The BOE did not review or potentially adjust consultant and sub-consultant employee hourly rates and support for labor multipliers after the Master Services Agreement was approved. As a result, rates and multipliers were not evaluated over time, potentially resulting in overbillings to BOE.	9.1	<i>BOE will develop a policy to review and approve submitted multiplier and hourly rate information for consultants and sub-consultants at the beginning of the contract, and then again every three years for those firms who are issued new task orders, and revise the Project Delivery Manual accordingly.</i>	<i>In Progress</i>	<i>Upon completion of the Final Audit, the BOE will program the work effort to implement this recommendation into the Work Plan for Fiscal Year '16-'17.</i>	<i>Six months after the completion of the Final Audit.</i>
11	The BOE did not perform periodic audits of its consultants and sub-consultants billings and rates on selected projects to provide better oversight of project costs. As a result, the BOE cannot verify that consultant billings, associated rates, and hours billed are not being overstated.	11.1	<i>BOE will develop a policy to review and approve billings and rates for consultants and sub-consultants at the beginning of the contract, and then again after three years for those firms who are issued new task orders, and revised the Project Delivery Manual accordingly.</i>	<i>In Progress</i>	<i>Upon completion of the Final Audit, the BOE will program the work effort to implement this recommendation into the Work Plan for Fiscal Year '16-'17.</i>	<i>Six months after the completion of the Final Audit.</i>
Section III	Project Oversight and Monitoring					
12	BOE did not utilize an independent surveyor to verify payments for a unit price contract, resulting in a conflict of interest which could lead to BOE's overpayment of the contractor.	12.1	Make all arrangements for the procurement of an independent firm, separate from the Contractor, for projects requiring the expertise of a surveyor or other professionally designated party for unit price, quantity, and payment purposes.	<i>Disagree</i>	<i>Not Applicable</i>	<i>Not Applicable</i>

Report Title:
 Department responsible for Implementation:

Audit of Proposition O Projects
PW Bureau of Engineering
 Initial Action Plan

Finding Number	Summary Description of Finding	Rec. No.	Recommendation	DEPARTMENT REPORTED INFORMATION		
				Current Status	Basis for Status	Target Date for Implementation
Section IV	Contract Conditions					
14	BOE Master General Conditions agreement for contractors did reflect current City insurance requirements and procedures.	14.1	Review and update insurance and indemnification provisions in the Master General Conditions to reflect current City practices.	<i>In Progress</i>	<i>Upon completion of the Final Audit, the BOE will program the work effort of the BOE, CAO, and City Attorney to implement this recommendation, into the Work Plan for Fiscal Year '16-'17.</i>	<i>Six months after the completion of the Final Audit.</i>
15	BOE's Project Delivery Manual does not reflect City Risk Management and Board of Public Works policies and procedures for review and approval of bonds and insurance for contracts. As a result, it is not clear which entity is responsible for ensuring requirements are met.	15.1	Update the Project Delivery Manual to more accurately reflect the current roles and responsibilities of the City Risk Management Section, Board of Public Works, and Project Manager, as relates to review and approval of insurance and bonds.	<i>In Progress</i>	<i>Upon completion of the Final Audit, the BOE will program the work effort to implement this recommendation, into the Work Plan for Fiscal Year '16-'17.</i>	<i>Six months after the completion of the Final Audit.</i>

I - Implemented
 PI - Partially Implemented or In Progress
 NI - Not Implemented
 D - Disagree

BOLD italics are BOE comments

CITY OF LOS ANGELES
INTER-DEPARTMENTAL CORRESPONDENCE

DATE: April 13, 2016

To: Ron Galperin, City Controller
Office of the Controller

Attn: Farid Saffar, Director of Auditing
Office of the Controller

FROM: Enrique C. Zaldivar, Director
LA Sanitation

SUBJECT: **LASAN IMPLEMENTATION PLAN FOR PROPOSITION O AUDIT
REPORT RECOMMENDATIONS**

Thank you very much for an opportunity to review the final draft report of the "Audit of Proposition O Projects", hereafter called the "Audit Report." LASAN received a copy of the final draft report from your March 31, 2016 transmittal. As the owner, operator and planning lead for all Prop O, LASAN has reviewed the Audit Report and intends to implement the report's recommendations as it relates to LASAN's activities under the Prop O Program as reflected in the attached spreadsheet.

If you have any questions or comments, please contact me or Shahram Kharaghani at (213) 485-0587.

ECZ:SK
WPDCR9261

Enclosure

cc: Siri Khalsa, City Controller
Traci Minamide, LASAN
Adel Hagekhalil, LASAN
Lisa Mowery, LASAN
Eva Sung, LASAN
Shahram Kharaghani, LASAN
Wing Tam, LASAN

Report Title:
 Department responsible for Implementation:

Audit of Proposition O Projects
PW Bureau of Sanitation
 Initial Action Plan

Finding Number	Summary Description of Finding	Rec. No.	Recommendation	DEPARTMENT REPORTED INFORMATION		
				Current Status	Basis for Status	Target Date for Implementation
Section I Project Management						
4	Project scoring criteria were not fully developed at the start of the program, and evolved over time. However, LASAN did not provide consistent documentation of the changes, making it difficult to determine whether eligibility criteria were followed for some projects.	4.1	Always evaluate projects, and document the evaluation process, based upon a single set of established criteria to ensure all projects provide the highest benefit to water quality and meet the intent of the bond language.	I	LASAN will use the established project selection criteria in evaluating all Prop O projects from hereon and document the project scores.	1-Apr-16
5	It will be important for LASAN and CAO to develop a more comprehensive tracking and reporting system as projects move from optimization to operations and maintenance to ensure compliance with Prop O bond funding requirements.	5.1	Ensure that there is adequate funding to support Prop O project operations and maintenance as projects transition out of the optimization phase.	IP	The City of LA (Mayor's Office) is working very closely with the LA County Board of Supervisors for a Countywide fee to fund stormwater management programs. On April 5, 2016, the County Supervisors approved a "Drought Resiliency Work Plan" with instructions to their LA County Public Works staff report back on the fee in 45 days. The fee will go to the voters in the fall of 2017. Once adopted, this fee will enable the City to program its O&M needs for the storm water program and in particular for the Prop O projects. If this initiative fails, LASAN will work with CAO to budget O&M needs of the Prop O Program based upon the requirements of GO bonds.	1-Jul-17
		5.2	Carefully track the timing and conclusion of optimization and the transition to operations and maintenance.	IP	LASAN will use the FMIS system and all of its capabilities to better track optimization cost by tasks and subtasks.	1-Jul-16
Section II Project Costs.						

Report Title:
 Department responsible for Implementation:

Audit of Proposition O Projects
PW Bureau of Sanitation
 Initial Action Plan

Finding Number	Summary Description of Finding	Rec. No.	Recommendation	DEPARTMENT REPORTED INFORMATION		
				Current Status	Basis for Status	Target Date for Implementation
10	The LASAN, BCA, and DPW Office of Accounting did not utilize clear timesheet task and subtask codes, making it difficult to determine if internal labor project costs were categorized to the proper Prop O project phase.	10.1	Develop a more comprehensive and integrated system of codes that are detailed and useful for the Prop O projects and can be utilized for all Bureaus.	IP	LASAN will develop additional tasks and subtasks for project work orders to differentiate among the specific functions and activities that are conducted for each project under the individual project work orders.	1-Jul-16
Section III	Project Oversight and Monitoring					
13	LASAN has been slow to report on interim or final project outcomes, making it difficult to measure project effectiveness and compliance with bond requirements.	13.1	Develop and regularly report project-specific and overall Prop O performance metrics.	IP	LASAN will develop performance reports that describe project-specific and overall performance metrics twice a year at the end of the wet and dry weather seasons.	1-Jul-16

I - Implemented
 PI - Partially Implemented or In Progress
 NI - Not Implemented
 D - Disagree

CITY OF LOS ANGELES

CALIFORNIA



ERIC GARCETTI
MAYOR

MIGUEL A. SANTANA
CITY ADMINISTRATIVE OFFICER

ASSISTANT
CITY ADMINISTRATIVE OFFICERS

BEN CEJA
PATRICIA J. HUBER

April 25, 2016

Ron Galperin, City Controller
Attention: Farid Saffar, Director of Auditing
200 North Main Street, Room 300
Los Angeles, CA 90012

Dear Mr. Galperin:

Thank you for conducting and sharing the audit of the City Proposition O Program. We are grateful for all the hard work that your staff and the auditors have devoted to this effort. We know you share our goal of providing transparency and high quality services. As Chair of the Administrative Oversight Committee (AOC) and as staff to the Citizens Oversight Advisory Committee (COAC), we will advise both bodies to consider your recommendations thoughtfully.

We have reviewed the Draft Audit and, as you requested, have filled out the table of recommendations for findings relating to this Office (attached).

We are appreciative of the positive statements made about the role this Office, along with the Bureaus of Engineering and Sanitation, have had on the implementation of this unique and innovative Program. We accept your findings and are taking immediate steps to improve our support of the Proposition O Program.

While we accept your findings, we feel that important context is missing pertaining to your finding on SB165 and would like to make this part of the record. Therefore, we are including both the immediate steps we are taking to address the finding, as well as, information on our transparency efforts in this communication.

Regarding Audit Finding 2

Audit Finding 2 - The CAO did not timely submit the annual SB 165 report to the Mayor and City Council as required by State Statute, lessening the relevance of this oversight control.

- Audit Recommendation 2.1 - Implement procedures to ensure the CAO timely submits SB 165 reports in accordance with statute to the governing bodies to strengthen oversight controls.

We agree that SB165 reports were not submitted timely and are making immediate changes to our priorities and work procedures to allow for a timely submission beginning

with the current fiscal year, 2015-2016. We will begin working on the 2015-16 Year report on or near July 1, 2016. Our partners in producing this report are the Bureau of Engineering and the City Controller. They will be contacted early in July for their assistance.

Your assistance in clarifying, and achieve a new understanding of, the requirements for use of fully audited information produced when the Comprehensive Annual Financial Report (CAFR) is published has assisted us in establishing a new process. This will remove the SB165 report workload from our busiest season, allowing it to be produced during an alternate timeframe. This has been discussed with staff and a goal of producing this within 30 days of receipt of information from the Bureau of Engineering and City Controller has been established.

We believe that the intent of SB165 has been continually prioritized as critical and achieved by the management of this Program. The Audit says that SB165 “found that it was important for local agencies to demonstrate to voters that bond funds are expended on the intended facilities and services.” We believe that the goal of SB165 is important and that the intended level of transparency currently exists with the Prop O Program and is both constant and continual. Voters are both continually provided with information that shows that funds are expended on intended facilities and services and continually provided with opportunities to interact with Program management.

This Office has worked, and continues to work, diligently to keep the public, the Mayor and the Council informed of relevant issues with the oversight of the Prop O Program. Specifically, we respectfully ask that consideration be given to the following:

- This Office reported 29 times (other than the 10 SB165 reports), over a period of eight years, to the Mayor and Council on issues relating to oversight of Proposition O. These reports were subject to the Council hearing process and were available to the public in general;
- This Office organized 83 publicly held, Brown Act noticed, Administrative Oversight Committee meetings, keeping the Mayor and Council apprised of all relevant issues;
- This Office organized 105 publicly held, Brown Act noticed, Citizen Oversight Advisory Committee meetings, keeping the public apprised of all relevant issues;
- This Office communicated weekly with the Bureaus of Engineering and Sanitation to provide an opportunity for Program related issues to be raised on a timely basis; and,
- The Department of Public Works has continually provided Program information to the public by preparing and distributing Monthly Reports on the status of the Program and making information available through the use of two City websites:

<http://www.lastormwater.org/green-la/proposition-o/>
and
http://eng.lacity.org/projects/prop_o/index.htm

While the timeliness of the SB165 reports were not optimal, the efforts above demonstrate that this Office has a proven track record of keeping all stakeholders informed.

- Audit Recommendation 2.2 - Prepare a single annual Prop O report that clearly summarizes activities, project expenditures, and performance for an entire fiscal year.

We have discussed this with the Bureau of Engineering and determined that the July Monthly Report can, and will, include all the information from the Prior Fiscal Year. We have jointly determined that we will begin this during the summer of 2016.

Regarding Audit Finding 5

Audit Finding 5 – It will be important for LASAN and CAO to develop a more comprehensive tracking and reporting system as projects move from optimization to operations and maintenance to ensure compliance with Prop O bond funding requirements.

- Audit Recommendation 5.1 - Ensure that there is adequate funding to support Prop O project operations and maintenance as projects transition out of the optimization phase.

We agree that Operations and Maintenance (O&M) funding is important. Funding for O&M is most appropriately addressed during each budget cycle with the Mayor and Council. Within this process, the Bureau must identify and request resources, clearly and sufficiently explaining their needs.

Ultimate authority for funding decisions rest with the Mayor and Council. However, to assist them with making decisions to fund a well-defined Bureau request, we may also explore development of alternative funding sources to the General Fund.

Thank you for this opportunity to work together to improve how we provide service to the public.

Sincerely,



Miguel A. Santana,
City Administrative Officer

Report Title:
 Department responsible for Implementation:

Audit of Proposition O Projects
City Administrative Officer
 Initial Action Plan

Finding Number	Summary Description of Finding	Rec. No.	Recommendation	DEPARTMENT REPORTED INFORMATION		
				Current Status	Basis for Status	Target Date for Implementation
Section I	Project Management					
2	The CAO did not timely submit the annual SB 165 report to the Mayor and City Council as required by State Statute, lessening the relevance of this oversight control.	2.1	Implement procedures to ensure the CAO timely submits SB 165 reports in accordance with statute to the governing bodies to strengthen oversight controls.	PI	A new understanding of the requirements for the report were obtained from the Controller during this audit process. Instead of waiting until the CAFR is adopted, and thereby placing this workload within our busiest season, this report can be produced during an alternate timeframe that will work better for us. This has been discussed with staff and a goal of producing this each summer has been established. We will begin working on the 15-16 Year report on or near July 1, 2016. Our partners in producing this report are the Bureau of Engineering and the City Controller. They will be contacted early in July for their assistance.	Summer 2016
		2.2	Prepare a single annual Prop O report that clearly summarizes activities, project expenditures, and performance for an entire fiscal year.	PI	We have discussed this with the Bureau of Engineering and determined that the July Monthly Report will include all the information from the Prior Fiscal Year. We have jointly determined that we will begin this during the summer of 2016.	Summer 2016
5	It will be important for LASAN and CAO to develop a more comprehensive tracking and reporting system as projects move from optimization to operations and maintenance to ensure compliance with Prop O bond funding requirements.	5.1	Ensure that there is adequate funding to support Prop O project operations and maintenance as projects transition out of the optimization phase.	PI	We agree that O&M funding is important. Funding for O&M is most appropriately addressed during each budget cycle with the Mayor and Council. Within this process, the Bureau must identify and request resources, clearly and sufficiently explaining their needs. Ultimate authority for funding decisions rest with the Mayor and Council. However, to assist them with making decisions to fund a well-defined Bureau request, we may also explore development of alternative funding sources to the General Fund.	Spring 2016

I - Implemented
 PI - Partially Implemented or In Progress
 NI - Not Implemented
 D - Disagree