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Metro

EXECUTIVE MANAGEMENT AND AUDIT COMMITTEE
MAY 15, 2008

SUBJECT: MANAGEMENT AUDIT SERVICES FY 2008 THIRD QUARTER REPORT

ACTION: RECEIVE AND FILE

RECOMMENDATION

Receive and file the third quarter report of Management Audit Services for the period ending March 31, 2008.

ISSUE

At its January 2005 meeting, the Board designated the Executive Management and Audit Committee (EMAC) as their audit committee. The EMAC requested a quarterly report from Management Audit Services on its audit activities. This report fulfills the requirement for the third quarter of FY 2008.

DISCUSSION

Management Audit Services (MAS) provides audit support to the Chief Executive Officer (CEO) and his executive management. MAS provides audit services both internally reviewing agency processes, functions and systems, as well as externally reviewing compliance to contracts and memorandums of understanding (MOUs).

There are five audit groups in MAS, contract audit, grant audit, financial audit, information technology audit, and operational audit. Contract Audit audits vendor's proposals and contractor's claims to support the Office of Procurement and Material Management. Grant Audit audits compliance to MOUs for projects funded by Countywide Planning and Development. Financial Audit specializes in financial transaction reviews, Information Technology Audit audits the information technology (IT) systems, infrastructure, IT programs and activities, and Operational Audit focuses on agency operations and processes.

The summary of MAS audit activity for the quarter ending March 31, 2008 is as follows:

Contract Audit – eight audits were completed, and 58 audits were in process with a total value of $5.5 million.

Grant Audit – nine audits were completed, and 50 audits were in process with a total value of $189.4 million.

Financial Audit, Information Technology Audit, and Operational Audit – three audits were completed, and 23 audits, six control self assessments, and three consulting engagements were in process.

Contractor Pre-Qualification – 206 applications and validations were processed and 140 were approved.

Audit Follow-up and Resolution – nine, or 18%, of all outstanding audit recommendations were completed and closed. Twelve new audit recommendations were added.

MAS' FY 2008 third quarter report is included as Attachment A.

NEXT STEPS

Management Audit Services will provide the year-end summary of FY 2008 audit activity to the Board at the August 2008 Executive Management and Audit Committee meeting.

ATTACHMENT

A.   Quarterly Report on Management Audit Services activity for period ending March 31, 2008.

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Ruthe Holden

Ruthe Holden
Chief Auditor, Management Audit Services

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Chief Executive Officer

Los Angeles County Metropolitan Transportation Authority

MANAGEMENT AUDIT SERVICES QUARTERLY REPORT TO THE BOARD

THIRD QUARTER
FY 2008

Metro

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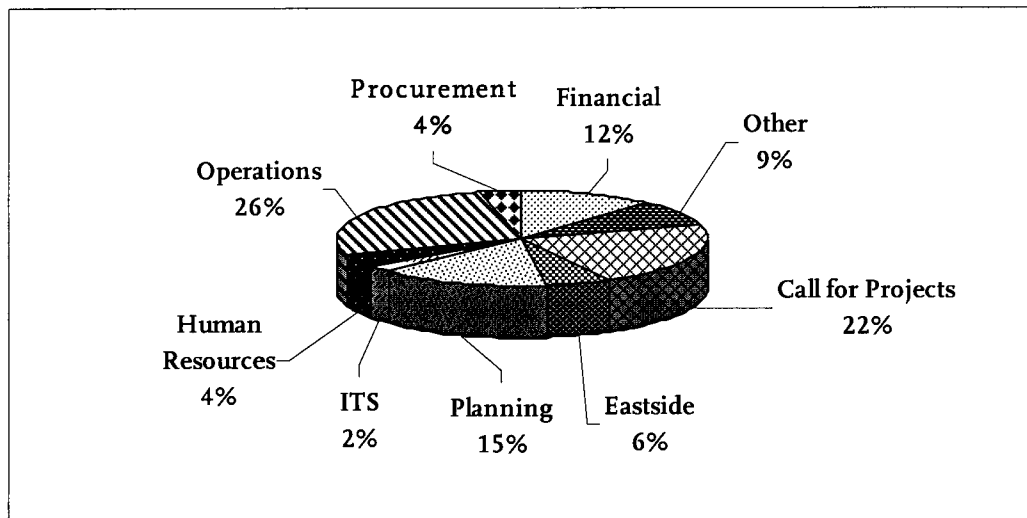
EXECUTIVE SUMMARY

Overview

During the third quarter of FY 2008, 20 audits were completed. In addition, an audit memo was issued for an audit project that was stopped after the preliminary survey was completed because risk to the agency was deemed to be low.

The completed audits for third quarter include three internal audits, eight contract audits and nine grant audits. The completed contract and grant audits are summarized on page two. Summaries of the internal audits begin on page three.

One hundred thirty-one audit projects, six CSA reports and three consulting engagements were in process as of March 31, 2008.

The following chart identifies the functional areas where Management Audit Services (MAS) focused staff time and efforts during third quarter FY 2008:

Procurement 4%   Financial 12%   Other 9%   Operations 26%   Call for Projects 22%   Human Resources 4%   ITS 2%   Planning 15%   Eastside 6%

"Other" includes hours spent on communications and environmental projects, risk assessment and quality assurance.

Audit Follow-up and Resolution continues to work with management to resolve open recommendations. Nine or 18% of the recommendations were completed and closed during the quarter out of a total universe of 51. Twelve audit recommendations were added during the third quarter.

The pre-qualification group processed 206 applications and validations during the third quarter FY 2008.

We completed the agency-wide risk assessment and prepared MAS' annual business and audit plan for FY 2009 which went to the April Board.

EXECUTIVE SUMMARY

Auditing and Accounting Standards Update

Government Accounting Standards Board Statement (GASB) No. 49, *Accounting and Financial Reporting for Pollution Obligations* (issued 11/06) applies to audits beginning after December 1, 2007 and addresses the accounting and financial reporting requirements for the obligation to address the current or potential detrimental effects of existing pollution, including contamination.

Once one of five obligating events occurs, a government is required to estimate the components of expected pollution remediation outlays and determine whether outlays for those components should be accrued as a liability or if appropriate, capitalized when goods and services are acquired. The five obligating events for GASB No. 49 are:
1) The government is compelled to take pollution remediation action because of an imminent endangerment;
2) The government violates a pollution prevention-related permit or license;
3) The government is named, or evidence indicates that it will be named, by a regulator as a responsible party or potentially responsible party for remediation, or as a government responsible for sharing costs;
4) The government is named, or evidence indicates that it will be named, in a lawsuit to compel participation in pollution remediation; and
5) The government commences or legally obligates itself to commence pollution remediation.

Prior to GASB No. 49, governments had discretion, consistent with Generally Accepted Accounting Principles (GAAP), to determine which cleanup costs should be capitalized, and which should be expensed. Statement of Financial Accounting Standards (SFAS) No. 5, *Accounting for Contingencies*, did not require that pollution sites with less than 50% probability of liability be recognized and reported. For example, SFAS No. 4, *Accounting and Financial Reporting Principles for Claims and Judgments and Compensated Absences* and SFAS No. 5, *Accounting for Contingencies*, did not require recognition of pollution remediation liabilities until after they were judged to be probable of occurrence.

GASB No. 49 requires government entities to estimate pollution and remediation liabilities and expenses using an expected cash flows measurement technique. The expected cash flow measurement technique is more complex than other methods used and involves subjectively assigning probabilities to the various possible remediation cost-at-completion outcomes. It also requires fairly detailed disclosures concerning specific liabilities. In addition, GASB No 49 permits government entities to recognize anticipated recoveries from responsible third parties and insurers as assets.

GASB No.49 will require government entities and their auditors to capture potential environmental liabilities and their impact on financial statements. In addition, audit procedures will need to be performed to capture the extent of environmental compliance and its impact to operational costs.

CONTRACTORS & OTHER AGENCY AUDITS

Contract Audit

Contract Audit provides support to the Office of Procurement and Material Management for a wide range of large-dollar procurements and projects. This support is provided throughout the procurement cycle in the form of pre-award, interim, change order, closeout audits, and assistance with contract negotiations.

During third quarter FY 2008, eight audits were completed, reviewing a net value of $4.5 million. Seven of these completed audits were for Planning projects, and one was for an Operations project. As of March 31, 2008, 58 audits were in process with a total dollar value of $5.5 million.

During the quarter, approximately 43% of Contract Audit efforts supported Planning completing pre-award audits in support of congestion pricing and corridor projects. The rest of the audit effort for this group was split between Eastside and Operations.

Details on Contract Audits completed during third quarter FY 2008 are in Appendix A.

Grant Audit

Grant Audit conducts audits for Countywide Planning's Call-for-Projects program, federally funded transportation programs, and various other transportation related projects, including Alameda Corridor East and CalTrans projects. The purpose of the audits is to ensure that grantees spend funds in accordance with the terms of the grants and federal cost principles.

Grant Audit completed nine audits during third quarter FY 2008, reviewing $37.6 million. $2.2 million of unused funds was identified that may be reprogrammed by Countywide Planning for other projects. Fifty audits with a total value of $189.4 million were in process as of March 31, 2008.

Details on Grant Audits completed during third quarter FY 2008 are in Appendix B.

INTERNAL AUDITS

Financial Audit

For the third quarter of FY 2008, one memo was issued discontinuing the audit of Capital Project Expenditures. After completing the preliminary survey and risk assessment, the issues were designated as low residual risk and the audit was stopped.

Four financial audit projects and one consulting engagement were in process as of March 31, 2008. The audits in process are: SAS 70 Reporting Requirements, Environmental Estimating Methodology, the Human Resources/TAP Interface, and Real Estate Rental Income. The audits in process are listed in Appendix C.

Operational Audit

For the third quarter of FY 2008, three audit projects were completed, Bus Operations Accident Management Process, Rail Service Interruption Communication, and School Tripper Program.

Six operational audit projects were in process at of March 31, 2008. One from the prior year's audit plan, Scheduled Bus Performance, and five projects from the FY 2008 audit plan: Preventative Training for High Risk Occupations, Key Metrics, M3-Inventory, Operations Safety Training, and Fare Media Stock Room. There are also six control self assessments (CSA) in process on Grievance Tracking, Fuel Management, Work Order Management, Equipment Maintenance, Inventory, and Driver Safety Training. The six operational audits and six CSA's in process are listed in Appendix E.

Audit of Bus Operations Accident Management Process
The audit objective was to verify that Vehicle Accident Monitoring System (VAMS)/TransitSafe information is accurate and complete and this information is being used in the Bus Operator accident review process. VAMS/TransitSafe is the central repository database for bus, rail and non-revenue vehicle accident information.

We found the information in VAMS/TransitSafe is not complete. For a variety of reasons, 25% of the accidents in the Maintenance and Material Management System (M3) could not be reconciled to the information in VAMS/TransitSafe. In addition, we found that internal controls need to be strengthened over accident reporting, file documentation and procedures.

Bus Operations management agreed to revise the Standard Operating Procedures that require the Transit Operations Supervisor to log the accident into the VAMS/TransitSafe database as soon as the Operator reports the accident to Bus Operations Control. Bus Operations management has also tasked the new Accident Investigation Group to study, develop and report on procedures that will capture unrecorded accidents, as well as identify methods of using technology to detect unreported accidents.

INTERNAL AUDITS

Audit of Rail Service Interruption Communication

The audit objective was to determine whether rail operation service interruptions are communicated effectively to customers at rail stations. We found that non-emergency phones were not distinguishable or not clearly designated from emergency phones and there was not clear or consistent telephone signage at the rail stations.

Rail Operations management has agreed to work with Communications/Marketing to develop bigger, bolder signs that will go around or above the intercoms identifying them as passenger assistance phones. Communications/Marketing is also developing signs that will be visible on the platform that will lead customers to our emergency/information phones. In addition, the new Train Passenger Information System is coming online with the ability to inform our customers of current delay and schedule adjustments. In the long term, Rail Communications is looking into the possibility of adding more "information intercoms" around the ticket vending machines as a potential capital project.

Audit of School Tripper Program

This audit was co-sourced to Macias Consulting Group, Inc. (Macias). The audit objective was to determine whether Metro's School Tripper Program complies with the requirements of Title 49 of the Code of Federal Regulations Section 605 (49 CFR 605) that pertain to Federal Transit Administration (FTA) grants.

The School Tripper Program is designed to add buses to the normal public bus routes, so that student customers do not seriously overload bus lines, causing delays and significant inconvenience to the general public. Federal grantees are prohibited under 49 CFR 605 regulations from providing transportation for students and school personnel if it excludes the general public or competes with private school bus operators. According to 49 CFR 605, school tripper service is permissible as a part of regularly scheduled transit service as long as it is open to the public and only stops at public bus stops. Four criteria were evaluated during the audit to determine school tripper compliance with 49 CFR 605: school trippers (1) should be communicated to the general public; (2) do not deviate from the published bus line routes to service a school; (3) do not stop at unmarked bus stops or locations that are not publicly accessible; and (4) do not start or end at schools, limiting public access.

The audit reviewed the Transit Service Policy revised in November 2007 to determine the extent it complied with 49 CFR 605. In addition, the audit sampled from the population of 713 school trippers between June 24, 2007 and December 15, 2007 to determine the extent they complied with the criteria set forth in 49 CFR 605.

Approximately 91.2% of all school trippers, out of a population of 713, were non-compliant with one or more of the 49 CFR 605 school tripper criteria. This represents between approximately $2,030,000 and $2,980,000 in annual operating costs. Failure to comply with federal regulations will put us in jeopardy of federal penalties.

INTERNAL AUDITS

Operations Management agreed to require Service Sector Development Managers to certify that all school trippers in their sector fully comply with established policies and procedures related to school tripper service. Each sector will submit a report prior to each major service change program that identifies all existing school trippers for review and approval. In addition, any existing trips that cannot be brought into compliance with 49 CFR 605 will be cancelled. Also, public timetables will be amended to reflect all regularly scheduled school operations, timetable maps will be amended to reflect route deviations, and bus stop placards will be placed at all stops included in the route deviations timetable maps. Lastly, Service Development will work with the Service Sectors to develop policies and procedures for (1) a public notification process when scheduled trips are modified on certain days; (2) requirements to log all requests for scheduled trippers and modifications to existing trippers, and (3) requests for new scheduled service or modifications to existing trippers will require enough prior notice to process the request in compliance with 49 CFR 605.

Information Technology Audit

During the third quarter FY 2008, 13 Information Technology (IT) audit projects and one consulting engagement were in process. Seven audits were in process from prior years' audit plans: Oracle Human Resources, Budget Information and Accounting System, Compliance to Software License Agreements, Oracle Change Management, Procurement Card, Vendor Master File, and Payroll E-Time. Four audits are in process from the FY 2008 audit plan: HR Central/Payroll System Controls, Transit Operator Activity Scheduling and Tracking (TOAST), Backup Recovery Management, and Information Privacy. Two new audits were started during third quarter, Materiel Maintenance & Management System (M3) General Controls, and M3 Timekeeping System. The 13 IT audits in process are listed in Appendix D.

AUDIT SUPPORT SERVICES

Contractor Pre-Qualification

California Public Utilities Code §130051.21 and Ordinance #4-05 of the Administrative Code require firms to be pre-qualified prior to doing business with the agency.

During third quarter FY 2008, 206 applications and validations were processed. Eighty-five applications and 38 validations were submitted and 79 applications and four validations were in process from the end of third quarter FY 2008. Of the 206 processed, 140 firms were approved to do business with Metro, four were closed as incomplete (applicant failed to respond to requests for information), and 62 applications and one validation were still in process as of March 31.

The applications processed during third quarter FY 2008 were in support of 34 different procurement actions, including contracts in construction, operations, and professional services.

Audit Follow-Up and Resolution

During the third quarter, 12 new audit recommendations were added to the outstanding audit recommendations list, and nine recommendations were completed and closed out of a total universe of 51 representing an 18% reduction in the total outstanding recommendations. The table below summarizes the third quarter activity.

Summary of MAS and External Audit Recommendations
As of March 31, 2008

Executive Area	Closed or Completed in Jan.	Closed or Completed in Feb.	Closed or Completed in Mar.	Under Review	Extended	Not Yet Due	Total Open Recom.
Chief Financial Services Officer	1						
Chief Administrative Services Officer	3	1	3	4	7	1	12
Chief Real Property Management & Development						1	1
Chief Planning Officer				4	3	3	10
Chief Operating Officer			1		1	13	14
General Mgr. Rail Operations				1	3	1	5
Totals	4	1	4	9	14	19	42

Appendix A

Contract Audit FY 2008 - Audits Completed During Third Quarter

Area	Audit Number & Type	Contractor	Requirement	Date Completed
Planning	07-COR-CO7C S2 - Cost Proposal	Terry A. Hayes Associates	Contractual	1/2008
Bus Operations	08-NAB-CO1 - Buy America	Noth America Bus Industries (NABI)	Contractual	3/2008
Planning	08-PBA-CO1A - Cost Proposal	Cambridge Systematics, Inc.	Contractual	3/2008
Planning	08-PBA-CO1B - Cost Proposal	The Lee Andrews Group	Contractual	3/2008
Planning	08-PBA-CO1D - Cost Proposal	Redhill Group, Inc.	Contractual	3/2008
Planning	08-PBA-CO1G - Cost Proposal	ECO Northwest	Contractual	3/2008
Planning	08-PBA-CO1H - Cost Proposal	Pulsar Advertising	Contractual	3/2008
Planning	08-PBS-CO1A - Cost Proposal	PBS&J	Contractual	3/2008

Appendix B

Grant Audit FY 2008 - Audits Completed During Third Quarter

Area	Audit Number & Type	Grantee	Requirement	Date Completed
Planning	08-CLA-G01 - Closeout	Los Angeles Department of Transportation	Contractual	1/2008
Planning	07-CPF-G02 - Closeout	City of Pomona	Contractual	1/2008
Planning	07-CAL-G03 - Interim	Caltrans	Contractual	2/2008
Planning	07-COG-G02 - Closeout	City of Glendale	Contractual	2/2008
Planning	08-COT-G01 - Closeout	City of Torrance	Contractual	2/2008
Planning	07-COA-G01 - Closeout	City of Alhambra	Contractual	3/2008
Planning	07-CAL-G04 - Closeout	Caltrans	Contractual	3/2008
Planning	07-CAL-G08 - Closeout	Caltrans	Contractual	3/2008
Planning	07-CAL-G01 - Closeout	Caltrans	Contractual	3/2008

Appendix C

Financial Audit FY 2008 - Progress Toward Completing Audit Plan

Area	Audit Number & Title	Description	Risk	Estimated Date of Completion
Finance	08-ACC-F03 - Environmental Estimating Methodology	Evaluate methodology for estimating significant environmental information as required by GASB no. 49 for the Comprehensive Annual Financial Report (CAFR). This audit is co-sourced with Macias Consulting Group.	High	5/2008
Real Property Management & Development	08-REA-F01 - Real Estate Rental Income	Determine whether lease database is accurate and complete, evaluate whether rental revenue is tied to property leases, and whether Real Estate records reconcile with Accounting records.	High	5/2008
Human Resources/Real Property Management & Development	08-TAP-F01 - Human Resources/TAP Interface	Review Employee, Dependent & Retiree Badging Process, and Interface with Transit Access Pass (TAP).	High	6/2008
Finance	08-ACC-F02 - SAS 70	Evaluate Statement on Auditing Standards (SAS) 70 Contract Requirements.	High	5/2008

Appendix D

Information Technology Audit FY 2008 - Progress Toward Completing Audit Plan

Area	Audit Number & Title	Description	Risk	Estimated Date of Completion
Information Technology Services/Human Resources	06-ITS-004 Oracle Human Resources	Assess Oracle HR security controls.	High	5/2008
OMB/Information Technology Services	06-OMB-005 - Budget Input & Analysis System	Assess the adequacy of controls for processing budget information.	Medium	5/2008
Agency-wide	06-ITS-012 - Compliance to Software License Agreements	Assess compliance with vendor licensing agreements and copyright laws.	High	5/2008
Information Technology Services	07-ACC-I04 - Oracle Change Management	Validate the formal change management process and assess the adequacy of controls in managing changes to Oracle applications.	High	6/2008
Procurement/ Material Management	07-PMM-I10 - Procurement Card	Assess procurement card policies, procedures and controls and determine compliance with policies and procedures.	High	4/2008
Procurement/ Material Management	07-ACC-I08 - FIS - Vendor Master File	Validate internal controls of the vendor master file and that the data in the file are accurate, complete, and duplicate vendors do not exist.	High	5/2008

Appendix D

Information Technology Audit FY 2008 - Progress Toward Completing Audit Plan

Area	Audit Number & Title	Description	Risk	Estimated Date of Completion
Information Technology Services/Payroll	07-ACC-I05 - Audit of Payroll E-Time	Validate internal controls of new E-Time System.	High	5/2008
Information Technology Services	08-ACC-I03 - Audit of HR Central/Payroll System Controls	Validate whether Payroll Input Systems internal controls are working properly.	High	6/2008
Bus Operations	08-OPS-I02 - Audit of TOAST	Evaluate system design for internal controls for Transit Operator Activity Scheduling and Tracking (TOAST)	High	6/2008
Information Technology Services	08-ITS-I01 - Audit of Backup Recovery Management	Evaluate backup procedures and controls for critical information	High	6/2008
Agency-wide	08-CEO-I01- Audit of Information Privacy	Evaluate internal controls over systems, databases, and processes that collect data subject to privacy acts.	High	6/2008
Bus Operations	08-OPS-I03 - Audit of Materiel Maintenance & Management System	Evaluate IT general controls over M3 systems.	High	6/2008
Bus Operations	08-OPS-I04 - Audit of M3 Timekeeping System	Assess M3 Timekeeping System to ensure adequacy and completeness of application controls.	High	6/2008

Appendix E

Operational Audit FY 2008 - Progress Toward Completing Audit Plan

Area	Audit Number & Title	Description	Risk	Estimated Date of Completion
Bus Operations	08-OPS-O08 Preventative Training for High Risk Occupation	Validate preventative safety training for high-risk professions, analyze relationship between safety training and accidents, and determine adequacy of the process.	High	5/2008
Bus Operations	07-OPS-O11 - Scheduled Bus Performance	Validate that bus performance metrics are accurate, complete and timely.	High	5/2008
Agency-wide	08-OPS-O01 Key Metrics	Validate accuracy of metrics provided to managers for consistency with other metrics published. Compare GL reporting information to Balance Scorecard information. Determine whether Project Management metrics are accurate, consistent, complete, and timely.	Critical	5/2008
Procurement/ Material Management	08-OPS-O05 M3-Inventory	Validate that M3 impacted key business process security and controls are in place and working as designed. Recommend improvements as necessary.	Critical	6/2008

Appendix E

Operational Audit FY 2008 - Progress Toward Completing Audit Plan

Area	Audit Number & Title	Description	Risk	Estimated Date of Completion
Bus Operations	08-OPS-O07 Operations Safety Training	Validate bus operator safety training and safety training selection process. Analyze relationship between safety training and accidents. Determine adequacy of the process.	High	4/2008
Communications	08-OPS-O06 - Fare Media Stock Room	Validate Fare Media Stock Room controls. Determine adequacy of process.	High	5/2008
Bus Operations	07-CSA-O01B - Equipment Maintenance, RRC Power Plant	Control Self Assessment - Document business process objectives, risks and activities.	-	4/2008
Procurement/ Material Management	08-CSA-O01B - Inventory	Control Self Assessment - Document business process objectives, risks and activities.	-	6/2008
Bus Operations	08-CSA-O05 - Driver Safety Training	Control Self Assessment - Document business process objectives, risks and activities.	-	5/2008
Bus Operations	08-CSA-O02 - Grievance Tracking	Control Self Assessment - Document business process objectives, risks and activities.	-	6/2008
Bus Operations	08-CSA-O03 - Fuel Management	Control Self Assessment - Document business process objectives, risks and activities.	-	6/2008

Appendix E

Operational Audit FY 2008 - Progress Toward Completing Audit Plan

Area	Audit Number & Title	Description	Risk	Estimated Date of Completion
Bus Operations	08-CSA-O06 - Work Order Management	Control Self Assessment - Document business process objectives, risks and activities.	-	6/2008