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**FINANCE, BUDGET AND AUDIT COMMITTEE  
JUNE 18, 2014**

**SUBJECT: MANAGEMENT AUDIT SERVICES FY 2014 THIRD QUARTER  
REPORT**

**ACTION: RECEIVE AND FILE**

**RECOMMENDATION**

Receive and file the third quarter report of Management Audit Services (Management Audit) for the period ending March 31, 2014.

**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 on its audit activities. In July 2011, the audit responsibilities were transferred to the Finance, Budget and Audit Committee. This report fulfills the requirement for the third quarter of FY 2014.

**DISCUSSION**

Management Audit provides audit support to the Chief Executive Officer (CEO) and his executive management. The audits we perform are categorized as either internal or external. Internal audits evaluate the processes and controls within the agency. External audits analyze contractors, cities or non-profit organizations that we conduct business with or disperse funds to.

There are four groups in Management Audit: Performance Audit, Contract Audit, Financial and Compliance Audit and Audit Support and Research Services. Performance Audit is primarily responsible for all audits for Operations, Finance and Administration, Engineering and Construction, Information Technology, Communications and Executive Office. Contract and Financial and Compliance Audit are responsible for all audits in Planning and Development and Vendor/Contract Management. All of these units provide assurance to the public that internal processes are efficiently, economically, effectively, ethically, and equitably performed by conducting audits of program effectiveness and results, economy and efficiency, internal controls, and compliance.

Audit Support and Research Services is responsible for administration, financial management, budget coordination, and audit follow-up and resolution tracking.

The summary of Management Audit activity for the quarter ending March 31, 2014 is as follows:

Internal Audits: two internal audits were completed; 24 internal audits were in process.

External Audits: four contract audits with a total value of \$33 million and eight grant audits with a total value of \$18.3 million were completed; 20 contract audits and 39 grant audits were in process.

Audit Follow-up and Resolution: three recommendations were added and eight recommendations were closed during the third quarter. At the end of the quarter, there were 26 open audit recommendations.

Management Audit's FY 2014 third quarter report is included as Attachment A.

### **NEXT STEPS**

Management Audit will provide the FY 2014 year end summary of audit activity to the Board at the October 2014 Finance, Budget and Audit Committee meeting.

### **ATTACHMENT**

- A. Management Audit Services Quarterly Report to the Board for the period ending March 31, 2014

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Ruthe Holden  
Chief Auditor

  
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Arthur T. Leahy  
Chief Executive Officer

**MANAGEMENT AUDIT SERVICES  
QUARTERLY REPORT TO THE BOARD**

**Los Angeles County Metropolitan  
Transportation Authority**

***Third Quarter  
FY 2014***



**Metro**

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# *EXECUTIVE SUMMARY*

## Summary of Audit Activity

During the third quarter of FY 2014, fourteen projects were completed. These include:

### Internal Audits

- Maintenance and Material Management System Timekeeping Module;
- Subsidiary Ledger Accuracy and Completeness;

### Contract Audits

- Independent Auditor's Report on Agreed-Upon Procedures for the Cost Proposal for Contracted Transportation Services;
- Independent Auditor's Report on Agreed-Upon Procedures for the Cost Proposal for Project Management and Quality Assurance/Control Support Services;
- Independent Auditor's Report on Agreed-Upon Procedures for the Cost Proposal for Digital Microwave Radio Equipment;
- Independent Auditor's Report on Agreed-Upon Procedures for the Incurred Cost for the I-710 Corridor Project;

### Financial and Compliance Audits

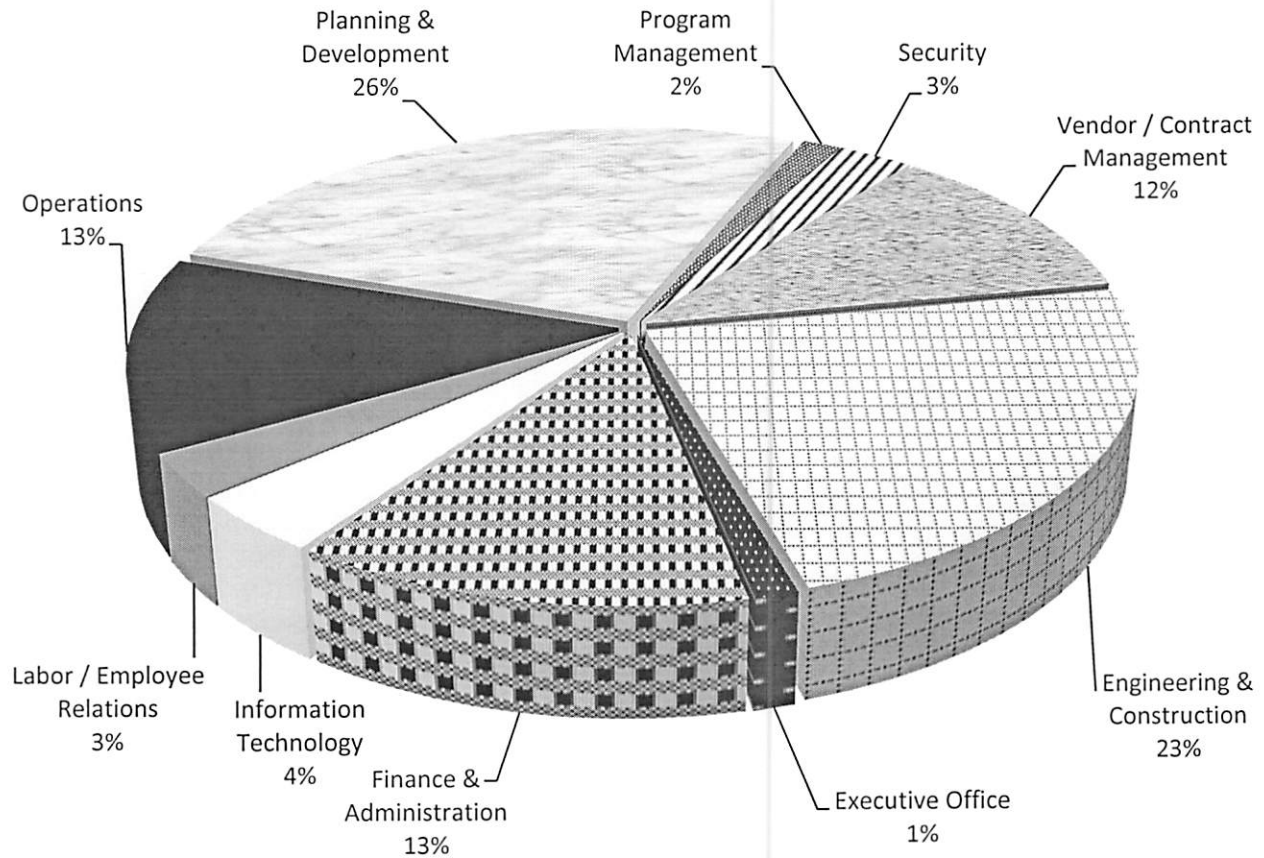
- Independent Auditor's Report on Agreed-Upon Procedures of the Close-out Review of City of South Pasadena's Business District Pedestrian Improvement Project;
- Independent Auditor's Report on Agreed-Upon Procedures of the Close-out Review of City of Alhambra's Valley Boulevard Capacity Improvement Project;
- Independent Auditor's Report on Agreed-Upon Procedures of the Close-out Review of City of Hawthorne's Rosecrans Avenue Arterial Improvements;
- Independent Auditor's Report on Agreed-Upon Procedures of the Close-out Review of City of Torrance's Del Amo Boulevard Extension/Grade Separation Project;
- Independent Auditor's Report on Agreed-Upon Procedures of the Close-out Review of City of Bellflower's Surface Transportation Program – Local Exchange Agreement;
- Independent Auditor's Report on Agreed-Upon Procedures of the Close-out Review of City of Los Angeles' Sawtelle Boulevard Widening at Venice Boulevard Project;
- Independent Auditor's Report on Agreed-Upon Procedures of the Close-out Review of City of Torrance's Maple Avenue at Sepulveda Boulevard Intersection Improvements Project;
- Independent Auditor's Report on Agreed-Upon Procedures of the Close-out Review of City of Glendale's Verdugo Road Signal Upgrade Project.

The completed external audits are discussed on page 4. Summaries of the internal audits begin on page 5.

# EXECUTIVE SUMMARY

Eighty-one projects were in process as of March 31, 2014; these include 22 internal audits, 20 contract audits, and 39 financial and compliance audits.

The following chart identifies the functional areas where Management Audit focused audit staff time and efforts during third quarter FY 2014:



## Audit follow-up:

- three recommendations were added and eight recommendations were closed during the third quarter. At the end of the quarter, there were 26 open audit recommendations.

# *EXTERNAL AUDITS*

## Contract Audit

Contract Audit provides support to the Vendor/Contract Management Department 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, and closeout audits, as well as assistance with contract negotiations.

During third quarter FY 2014, four audits were completed, reviewing a net value of \$33 million. Auditors questioned \$6.5 million or 20% of the proposed costs. The four audits supported procurements in the following areas:

- Contracted Transportation Services procurement;
- Project Management and Quality Assurance procurement;
- Communications Technology procurement;
- I-710 Corridor Project procurement.

Twenty contract audits were in process as of March 31, 2014.

Details on Contract Audits completed during third quarter FY 2014 are in Appendix A.

## Financial and Compliance Audit

Financial and Compliance Audit conducts audits for Planning and Development's Call-for-Projects program, Engineering and Construction's highway projects, federally funded transportation programs, and various other transportation related projects, including 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.

Financial and Compliance Audit completed eight audits during third quarter FY 2014. We reviewed \$18.3 million of funds and identified \$13 thousand of unused funds that may be reprogrammed by Planning and Development for other projects. Thirty-nine grant audits were in process as of March 31, 2014.

Details on Grant Audits completed during third quarter FY 2014 are in Appendix B.



# INTERNAL AUDITS

For the third quarter of FY 2014, two internal audits were completed.

Twenty-two internal audits were in process as of March 31, 2014. The internal audits in process are listed in Appendix C.

The following internal audits were issued in the third quarter FY 2014. The completed reports are listed in order of the magnitude of risks that their findings represent to the agency.

## Performance Audit of Maintenance and Material Management System (M3) Timekeeping Module

The audit objective was to evaluate the efficiency and effectiveness of the timekeeping module to ensure timesheets are processed accurately, timely and completely.

We found that application controls over the M3 Timekeeping module were generally adequate to maintain the integrity and validity of data throughout the processing cycle. However, we found three significant issues:

- 1) inadequate controls over payroll adjustments;
- 2) inadequate information provided for reviewing access rights; and
- 3) inefficient use of M3 Timekeeping resources.

Management agreed with the findings and has already taken steps to resolve these issues.

## Performance Audit Subsidiary Ledger Accuracy and Completeness

The audit objectives were to evaluate subsidiary ledger controls over posting of transactions to the general ledger to ensure completeness and accuracy of financial transactions and to determine whether the agency complies with FTA requirements to conduct equipment physical inventory every two years.

We found that controls over posting transactions from subsidiary ledger to the general ledger are adequately designed and operating effectively. However, we found that since 2001 there were 18 buses that did not get depreciated as required by Financial Accounting Standards Board. This resulted in understatement of accumulated depreciation by \$6.7 million and a related net book value overstatement for fixed assets. During the audit, the Accounting Department corrected the accumulated depreciation and net book value of the fixed assets.

## *OTHER AUDITS*

Other audits completed during third Quarter FY14 by external CPA firms include:

### PTSC - MTA Risk Management Authority Basic Financial Statements – Issued March 2014

In October 1998, the Public Transportation Services Corporation (PTSC) and the Los Angeles County Metropolitan Transportation Authority (LACMTA) entered into a joint powers agreement to create the PTSC-MTA Risk Management Authority (PRMA) for the purpose of establishing and operating a program of cooperative self-insurance and risk management. PRMA receives all of its funding from LACMTA and PTSC. As PTSC also receives its funding from LACMTA, PRMA is a component unit of the LACMTA and is included in LACMTA's financial statements as a blended component unit.

An audit of PRMA's financial statements by an independent CPA firm is required annually. We retained Bazilio Cobb Associates (BCA) to conduct the audit for the fiscal year ended June 30, 2013. BCA found that PRMA's financial statements present fairly, in all material respects. However, BCA issued a management letter with comments in connection with the audit report. Management has addressed the comments and will rectify the issue.

### Audited Financial Statements of Metro ExpressLanes – Issued March 2014

Metro ExpressLanes is a one-year demonstration program that will test innovations to improve existing transportation systems in three sub-regions: the San Gabriel Valley, Central Los Angeles, and the South Bay. The first Metro ExpressLanes commenced revenue operations in November 2012 on the I-110 Harbor Freeway, between Adams Blvd. and the 91 freeway. The second Metro ExpressLanes began revenue operations in February 2013 on the I-10 El Monte Freeway between Alameda St. and the 605 Freeway.

An audit of the financial statements of Metro ExpressLanes, an enterprise fund of the LACMTA, was performed by Vasquez & Company, LLP (Vasquez) for the period November 10, 2012 to June 30, 2013. Vasquez found that the financial statements present fairly, in all material respects.

### Agreed Upon Procedures Report of Xerox – Issued March 2014

Xerox is responsible for the tracking and reporting of Transit Access Pass (TAP) program revenues. We retained Mayer Hoffman McCann P.C. (MHM) to perform the audit to assist us in determining if the TAP program general and application controls are adequate and can be relied upon for the period July 1, 2013 through November 30, 2013.

MHM identified three findings relating to 1) a minor discrepancy in the distribution of revenues; 2) Oracle password settings not in compliance with company policies; and 3) limited segregation of duties in Oracle. Xerox agreed with all of the findings and committed to correct the issues noted.

# AUDIT SUPPORT SERVICES

## Audit Follow-Up and Resolution

During the third quarter, three new audit recommendations were added to the outstanding audit recommendations list and eight recommendations were completed and closed. At the end of this quarter, there were 26 outstanding audit recommendations. The table below summarizes the third quarter activity.

### Summary of MAS and External Audit Recommendations As of March 31, 2014

Executive Area	Closed or Completed in Jan.	Closed or Completed in Feb.	Closed or Completed in Mar.	Late	Extended	Not Yet Due/Under Review	Total Open Recom.
Engineering and Construction			4	2		0	2
Finance and Budget	1					1	1
Information Technology		1				3	3
Operations						15	15
Planning and Development						3	3
Vendor/Contract Management			2			2	2
<b>Totals</b>	<b>1</b>	<b>1</b>	<b>6</b>	<b>2</b>	<b>0</b>	<b>24</b>	<b>26</b>

## Appendix A

<b>Contract Audit FY 2014 - Audits Completed During Third Quarter</b>				
<b>Area</b>	<b>Audit Number &amp; Type</b>	<b>Contractor</b>	<b>Requirement</b>	<b>Date Completed</b>
Operations	14-OPS-A06 - Attestation Agreed-upon Procedures	MV Transportation, Inc.	Contractual	2/2014
Engineering & Construction	14-PLN-A05J - Attestation Agreed-upon Procedures	AFSHA Consulting, Inc.	Contractual	2/2014
Security	14-ITS-A01 - Attestation Agreed-upon Procedures	Aviat Networks, Inc.	Contractual	3/2014
Planning & Development	11-PLN-C15A - Attestation Agreed-upon Procedures	URS Corporation	Contractual	3/2014

## Appendix B

<b>Financial and Compliance Audit FY 2014 - Audits Completed During Third Quarter</b>				
<b>Area</b>	<b>Audit Number &amp; Type</b>	<b>Grantee</b>	<b>Requirement</b>	<b>Date Completed</b>
Engineering & Construction	12-PLN-A08 - Closeout	City of South Pasadena	Contractual	1/2014
Engineering & Construction	13-PLN-A25 - Closeout	City of Alhambra	Contractual	1/2014
Planning & Development	13-PLN-A17 - Closeout	City of Hawthorne	Contractual	2/2014
Planning & Development	14-PLN-A01 - Closeout	City of Torrance	Contractual	2/2014
Planning & Development	14-PLN-A06 - Closeout	City of Bellflower	Contractual	3/2014
Planning & Development	14-PLN-A12 - Closeout	City of Los Angeles	Contractual	3/2014
Planning & Development	14-PLN-A11 - Closeout	City of Torrance	Contractual	3/2014
Engineering & Construction	13-PLN-A16 - Closeout	City of Glendale	Contractual	3/2014

## Appendix C

<b>Internal Audit FY 2014 - Progress Toward Completing Audit Plan</b>				
<b>Area</b>	<b>Audit Number &amp; Title</b>	<b>Description</b>	<b>Risk</b>	<b>Estimated Date of Completion</b>
Operations	11-OPS-O01 - Drugs and Alcohol	Evaluate efficiency and effectiveness of drug and alcohol compliance program.	High	5/2014
Operations	11-OPS-O04 - Facilities Maintenance	Evaluate the efficiency and effectiveness of Facilities Maintenance meeting their stated objectives and goals.	High	5/2014
Vendor / Contract Management	13-CEO-P01 - Cost Estimating Process	Assess efficiency and effectiveness and timeliness of Procurement's cost estimating process.	High	6/2014
Vendor / Contract Management	14-ADM-P04 - Management and Movement of Parts and Supply	Evaluate the efficiency and effectiveness of the management and movement of parts and supplies.	High	6/2014
Finance & Administration	10-ACC-F04 - Chart of Accounts	Verify that Chart of Accounts adequately reflect the current business process and reporting needs.	High	6/2014
Engineering & Construction	12-CON-P03 - I-405 Follow-up	Verify if management's corrective actions from the Audit of I-405 Sepulveda Pass Improvement Project were implemented and resulting in improvements.	High	6/2014
Operations	13-OPS-P03 - Operations IT System Integrations (ATMS)	Evaluate the efficiency and effectiveness operation IT systems integration and utilization.	High	6/2014
Planning & Development	14-EDD-P01 - Real Estate Property Management Follow-up	Evaluate accuracy and completeness of tracking real estate properties in Real Property Management System.	High	6/2014
Other Funded Agencies	12-HCP-P01 - Metro Freeway Service Patrol	Evaluate project management and contract performance.	High	7/2014

## Appendix C

<b>Internal Audit FY 2014 - Progress Toward Completing Audit Plan</b>				
<b>Area</b>	<b>Audit Number &amp; Title</b>	<b>Description</b>	<b>Risk</b>	<b>Estimated Date of Completion</b>
Finance & Administration	10-ACC-F01 - Accounts Receivable	Validate adequacy of current policies and procedures.	High	7/2014
Engineering & Construction	10-CPC-K02 - Third Party Utility Relocation Agreement Efficiency	Assess the adequacy and effectiveness of the Third Party Utility Relocation.	High	7/2014
Operations	13-OPS-P06 - Contracted Bus Services	Evaluate the efficiency and effectiveness of contracted bus services contracts.	High	7/2014
Information Technology	14-ADM-P01 - Mobile Devices	Evaluate efficiency and effectiveness of mobile device security and controls for personal usage.	High	8/2014
Operations	12-OPS-P01 - Rail Overhead and Maintenance	Evaluate the efficiency and effectiveness of the Rail Overhaul and Refurbishment Program.	High	8/2014
Operations	12-OPS-P02 - Bus Operator Road Calls	Determine the adequacy and effectiveness of Bus Operator Road Calls.	High	8/2014
Operations	13-OPS-P02 - Non-Revenue Vehicle Usage (Agencywide)	Evaluate efficiency and effectiveness of bus division non-revenue vehicle usage.	High	8/2014
Operations	13-OPS-P04 - Operations KPI Audit	Evaluate the accuracy and completeness of Operations KPIs.	High	8/2014
Engineering & Construction	14-HCP-P01 - Caltrans Funding Agreement	Evaluate the accuracy, completeness and compliance of project cost to MOU requirements.	High	8/2014
Operations	12-ROP-O01 - Wayside System	Evaluate effectiveness of maintenance of the Rail signaling systems.	High	8/2014

## Appendix C

<b>Internal Audit FY 2014 - Progress Toward Completing Audit Plan</b>				
<b>Area</b>	<b>Audit Number &amp; Title</b>	<b>Description</b>	<b>Risk</b>	<b>Estimated Date of Completion</b>
Engineering & Construction	14-TPD-P01 - Construction Change Order Process	Evaluate the efficiency and effectiveness of the construction change order process including effectiveness of estimating process.	High	9/2014
Vendor / Contract Management	12-ADM-I01 - Contract Information Management System	Assess the system implementation process to acquire, design, test and implement the Contract Information Management System that meets specific functionalities required by the MTA business processes.	High	10/2014
Vendor / Contract Management	13-ADM-P01 - RFP Process	Assess efficiency and effectiveness and timeliness of Procurement's RFP processes.	High	10/2014
Other Funded Agencies	11-MET-F01 - Metrolink Use of TAP Funds	Validate costs claimed were allowable and allocable, adequately supported and met the objectives of grant terms and conditions.	High	10/2014
Vendor / Contract Management	13-ADM-O02 - Automated Storage and Retrieval System Phase I & II	Evaluate the adequacy of internal controls over the Automated Storage and Retrieval System (ASRS) Manager Computer System.	High	1/2015