



- **Board of Directors**
Executive Committee

11/20/2024 Committee Meeting

7-1

Subject

Approve amendments to the Metropolitan Water District Administrative Code Section 6451 regarding the Audit Department Charter; the General Manager has determined that the proposed action is exempt or otherwise not subject to CEQA

Executive Summary

The proposed amendments will (1) add information technology to the Audit Department's scope of work; (2) delete the responsibility of the Audit Department for issuing an opinion on internal controls over financial reporting; and (3) delete Governmental Auditing Standards as a professional standards reference and make other minor, non-substantive changes.

Proposed Action(s)/Recommendation(s) and Options

Staff Recommendation: Option #1

Option #1

Approve amendments to the Metropolitan Water District Administrative Code Section 6451 regarding the Audit Department Charter.

Fiscal Impact: None

Business Analysis: This option will improve the Audit Department Charter by aligning this portion of the Administrative Code with current and permissible Audit Department practices.

Option #2

Do not approve amendments to the Metropolitan Water District Administrative Code.

Fiscal Impact: None

Business Analysis: The Administrative Code will not be amended to specifically define information technology as part of the Audit Department's scope of work, and department strategy and resource allocation will be modified to perform additional work required to issue opinions and comply with the additional standards.

Alternatives Considered

No alternatives were considered for the update of the Administrative Code.

Applicable Policy

Metropolitan Water District Administrative Code Section 6451: Audit Department Charter

Metropolitan Water District Administrative Code Section 11104: Delegation of Responsibilities

Related Board Action(s)/Future Action(s)

The Board approved amendments to the Audit Department Charter in April 2023. Administrative Code 6451(e) requires an annual review of the Audit Department Charter with amendments proposed to the Board accordingly.

California Environmental Quality Act (CEQA)

CEQA determination(s) for Option #1:

The proposed action is not defined as a project under CEQA because it involves organizational, maintenance, or administrative activities; personnel-related actions; and/or general policy and procedure making that will not result in direct or indirect physical changes in the environment. (Public Resources Code Section 21065; State CEQA Guidelines Section 15378(b)(2) and (5)).

CEQA determination for Option #2:

None required

Details and Background

Audit Department Charter


Professional internal auditing standards require that an internal audit activity's purpose, authority, and responsibility be formally defined in an internal audit charter. The internal audit charter establishes the internal audit activity's position within the organization; authorizes access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal audit activities. Standards require the charter to be reviewed periodically.

The District's Audit Department charter is contained within Metropolitan Water District Administrative Code Section 6451. Audit Department staff reviewed the charter and propose amending Section 6451 as follows:

1. Information technology is pervasive in District operations and support functions. Associated risks with cybersecurity and other information technology require Audit Department focus. Accordingly, this letter proposes amending subsection (a) to add information technology to the Audit Department's scope of work.
2. California Government Code Section 1236 requires that the District's Audit Department conduct audits under specified standards prescribed by the Institute of Internal Auditors (IIA) or the Comptroller General of the United States (GAO). Both entities are recognized as authoritative sources for providing frameworks for executing audits. Generally, the GAO's Governmental Auditing Standards (GAGAS) provides requirements for conducting performance and financial audits, while the IIA's standards focus on internal audit function management and principles for conducting audits. Federal government audit agencies more commonly follow standards issued by the GAO but may be adopted by others, and an agency can opt to follow both standards. Historically, the District's Audit Department has exclusively followed the IIA's standards and other public agency internal audit functions exclusively follow this standard as well (e.g., County of Los Angeles, County of Orange, California State University). Continuing to follow the IIA's standards sufficiently meets the District's internal auditing needs while complying with State law. Accordingly, this letter proposes amending subsection (c) to remove reference to the Government Auditing Standards (GAGAS).
3. The District hires an independent external audit firm to annually perform an audit of the District's financial statements. As part of this audit, the external auditor considers the District's internal control over financial reporting (ICFR) to design audit work for the purpose of expressing an opinion on the financial statements. While the work performed by the external auditor is not for the purpose of expressing an opinion on the effectiveness of the District's ICFR, it is sufficient and does not warrant the additional expense or use of internal resources to complete work that would result in an opinion on ICFR. Furthermore, only certain publicly traded companies are required to have an opinion on ICFR. Accordingly, this letter proposes amending subsection (d) to remove the responsibility for the Audit Department to issue an opinion on ICFR on an annual basis.

Project Milestone

Not applicable



Scott Suzuki
General Auditor

11/13/2024

Date



Deven Upadhyay
Interim General Manager

11/14/2024

Date

Attachment 1 – Redline Version, Proposed Administrative Code Amendment

Attachment 2 – Clean Version, Proposed Administrative Code Amendment

Ref# a12690756

Provisions updated to reflect the actions of the Board of Directors through its 3/12/2024 meeting.

§ 6451. Audit Department Charter.

(a) Mission and Scope of Work - The mission of the Audit Department is to provide independent, professional, objective assurance and consulting services designed to add value and improve Metropolitan's operations. It helps the District accomplish its objectives by using a proactive, systematic approach to evaluate and improve the effectiveness of governance, risk management, and internal control. The scope of work of the Audit Department is to determine whether the District's network of governance, risk management, and internal control, as designed and represented by District management, is adequate and functioning in a manner to ensure:

- (1) Risks are appropriately identified, managed, and monitored;
- (2) Significant financial, managerial, and operating information is accurate, reliable, and timely;
- (3) Employees' actions are in compliance with policies, standards, procedures, and applicable laws and regulations;
- (4) Resources are acquired economically, used efficiently, and adequately protected;
- (5) Programs, plans, and objectives are achieved;
- (6) Quality and continuous improvement are fostered in the District's control process;
- (7) Significant legislative or regulatory issues impacting the District are recognized and addressed appropriately; and
- (8) Information technology is governed and systems and applications are securely deployed and monitored.

Opportunities for improving management internal control, efficiency and the District's image may be identified during audits. They will be communicated to the appropriate level of District management.

(b) Accountability - The General Auditor shall be accountable to the Board of Directors and the Executive Committee to:

- (1) Advise on the adequacy and effectiveness of the District's processes for controlling its activities and managing its risks;
- (2) Report significant issues related to the processes for controlling the activities of the District, including potential improvements to those processes, and provide information concerning such issues through to resolution; and

(3) Coordinate with other District control and monitoring functions (e.g., risk management, legal, finance, ethics, security, environmental).

(c) Professional Standards - The Audit Department shall govern itself by adherence to The Institute of Internal Auditors' mandatory guidance, including the Definition of Internal Auditing, the Code of Ethics, and the *International Standards for the Professional Practice of Internal Auditing (Standards)*. This mandatory guidance constitutes principles of the fundamental requirements for the professional practice of internal auditing and for evaluating the effectiveness of the Audit Department's performance. These documents constitute the operating procedures for the department and constitute an addendum to the charter. The Institute of Internal Auditors' Practice Advisories, Practice Guides, and Position Papers shall also be adhered to as applicable. In addition, Audit Department staff shall adhere to Metropolitan's policies and procedures, the California Government Code, and the Audit Department's Policies and Procedures Manual.

(d) Responsibilities - The Audit Department shall carry out the following responsibilities:

(1) Develop and present a flexible annual audit plan to the Executive Committee for review and approval. This plan should be developed utilizing a risk-based methodology and should include risks or internal control concerns identified by District management or the Board of Directors;

(2) Report periodically to the Executive Committee and District management the status of the current year's audit plan and the sufficiency of department resources;

(3) Submit audit reports to the Executive Committee and District management communicating the General Auditor's opinion regarding the internal control structure, identifying significant control issues, and providing related recommendations;

(4) Evaluate the adequacy and timeliness of District management's responses to, and the corrective action taken on, all recommendations noted in such reports. Conduct follow-up reviews as necessary and periodically report to the Executive Committee the status of District management's progress;

(5) Ensure the selection, development, and supervision of competent and professional audit staff;

(6) Perform a quality assurance program by which the General Auditor evaluates internal auditing activities against professional standards. Obtain an external quality assurance review as required by the Standards;

(7) Perform advisory services to assist District management in meeting its objectives. Examples may include facilitation, process design, training, and assessment services;

(8) Evaluate additions or changes in internal control processes coincident with their development and implementation;

(9) Keep the Executive Committee informed of significant emerging trends and best practices in internal auditing and governance;

(10) Assist in the investigation of significant suspected fraudulent activities within the District. Assure reporting to the Executive Committee on the results, as appropriate; and

(11) Coordinate with external auditors to minimize duplication of effort and ensure that issues raised as a result of their review are appropriately addressed.

(e) Authority - The General Auditor and Audit Department staff members are authorized to:

(1) Have unrestricted access to all functions, records, property, and personnel, subject to the requirements of safekeeping, confidentiality, and applicable process;

(2) Have full and free access to the Executive Committee, subject to applicable law;

(3) Allocate resources, set frequencies, select the subject, determine scopes of work, and apply the techniques required to accomplish audit objectives; and

(4) Obtain the necessary assistance of personnel within units of the District where they perform audits, as well as other specialized services from within or outside the District.

The General Auditor and Audit Department staff are not authorized to:

(1) Perform any operational duties for the District;

(2) Initiate or approve accounting transactions external to the Audit Department;
or

(3) Direct the activities of any District employee not employed by the Audit Department, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the internal auditors.

This Charter shall be reviewed at least annually by the Executive Committee and Board of Directors.#

Provisions updated to reflect the actions of the Board of Directors through its 3/12/2024 meeting.

§ 6451. Audit Department Charter.

(a) Mission and Scope of Work - The mission of the Audit Department is to provide independent, professional, objective assurance and consulting services designed to add value and improve Metropolitan's operations. It helps the ~~organization-District~~ accomplish its objectives by using a proactive, systematic approach to evaluate and improve the effectiveness of ~~governance~~, risk management, ~~and internal control~~, ~~and governance processes~~. The scope of work of the Audit Department is to determine whether the ~~organization's-District's~~ network of ~~governance~~, risk management, ~~and internal control~~ ~~and governance~~, as designed and represented by ~~District~~ management, is adequate and functioning in a manner to ensure:

- (1) Risks are appropriately identified, managed, and monitored;
- (2) Significant financial, managerial, and operating information is accurate, reliable, and timely;
- (3) Employees' actions are in compliance with policies, standards, procedures, and applicable laws and regulations;
- (4) Resources are acquired economically, used efficiently, and adequately protected;
- (5) Programs, plans, and objectives are achieved;
- (6) Quality and continuous improvement are fostered in the ~~organization's-District's~~ control process;
- (7) Significant legislative or regulatory issues impacting the ~~organization-District~~ are recognized and addressed appropriately; ~~and~~
- (8) Information technology is governed and systems and applications are securely deployed and monitored.

Opportunities for improving management internal control, efficiency and the ~~organization's-District's~~ image may be identified during audits. They will be communicated to the appropriate level of ~~District~~ management.

(b) Accountability - The General Auditor shall be accountable to the Board of Directors and the Executive Committee to:

- (1) Advise on the adequacy and effectiveness of the ~~organization's-District's~~ processes for controlling its activities and managing its risks;

(2) Report significant issues related to the processes for controlling the activities of the ~~organization~~District, including potential improvements to those processes, and provide information concerning such issues through to resolution; and

(3) Coordinate with other Metropolitan District control and monitoring functions (e.g., risk management, legal, finance, ethics, security, ~~and~~ environmental);

(c) Professional Standards -- The Audit Department shall govern itself by adherence to The Institute of Internal Auditors' mandatory guidance, including the Definition of Internal Auditing, the Code of Ethics, and the *International Standards for the Professional Practice of Internal Auditing (Standards)*. This mandatory guidance constitutes principles of the fundamental requirements for the professional practice of internal auditing and for evaluating the effectiveness of the Audit Department's performance. These documents constitute the operating procedures for the department and constitute an addendum to the charter. The Institute of Internal Auditors' Practice Advisories, Practice Guides, and Position Papers shall also be adhered to as applicable. In addition, Audit Department staff shall adhere to Metropolitan's policies and procedures, the California Government Code, ~~Government Auditing Standards (GAGAS)~~; and the Audit Department's Policies and Procedures Manual.

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(1) Develop and present a flexible annual audit plan to the Executive Committee for review and approval. This plan should be developed utilizing a risk-based methodology and should include risks or internal control concerns identified by District Mmanagement or the Board of Directors;

(2) Report periodically to the Executive Committee and District Mmanagement the status of the current year's audit plan and the sufficiency of department resources;

~~(3) Issue an opinion on internal controls over financial reporting on an annual basis;~~

(4) Submit audit reports to the Executive Committee and District Mmanagement communicating the General Aauditor's opinion regarding the internal control structure, identifying significant control issues, and providing related recommendations;

(5) Evaluate the adequacy and timeliness of District Mmanagement's responses to, and the corrective action taken on, all ~~significant control issues recommendations~~ noted in such reports. Conduct follow-up reviews as necessary and periodically report to the Executive Committee the status of District Mmanagement's progress;

(6) Ensure the selection, development, and supervision of competent and professional audit staff;

(7) Perform a quality assurance program by which the General Auditor evaluates internal auditing activities against professional standards. Obtain an external quality assurance review as required by ~~GAGAS and~~ the Standards;

(87) Perform ~~consulting-advisory~~ services to assist District management in meeting its objectives. Examples may include facilitation, process design, training, and ~~advisory assessment~~ services;

(98) Evaluate additions or changes in internal control processes coincident with their development and implementation;

(109) Keep the Executive Committee informed of significant emerging trends and best practices in internal auditing and governance;

(140) Assist in the investigation of significant suspected fraudulent activities within the ~~District~~organization. Assure reporting to the Executive Committee on the results, as appropriate; and

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(3) Direct the activities of any ~~organization~~District employee not employed by the ~~internal-a~~Auditing ~~d~~Department, except to the extent such employees have been appropriately assigned to auditing teams or to otherwise assist the internal auditors.

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