



THE CITY OF SAN DIEGO

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## OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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# Independent Rates Oversight Committee (IROC) – Audit Responsibilities

## OVERVIEW

On October 3, 2011, the Audit Committee received a presentation of the audit of the Public Utilities Department Capital Improvement Program. In discussing audit findings made by the Office of the City Auditor, Committee Member Hebrank raised questions about the Independent Rates Oversight Committee (IROC) and their role in procuring performance audits. This report provides additional information about IROC responsibilities and related performance audits that IROC now requests from the Office of the City Auditor.

## FISCAL/POLICY DISCUSSION

### IROC Origin and Purpose

In February of 2007, the Mayor proposed the creation of IROC in advance of City Council consideration of proposed rate increases for the water and wastewater systems. IROC oversight was intended to instill public confidence in the City's water and wastewater systems and ensure that these systems would continue to improve their financial and management practices. The City Council approved Ordinance No. O-19607 to create IROC on April 10, 2007. IROC held its first meeting on November 5, 2007.

Sections 26.2001 - 26.2003 of the Municipal Code (attached) describe the purpose/intent and duties/functions of IROC. IROC was established to:

- 1) Serve as an official advisory body to the Mayor and City Council on policy issues relating to the oversight of the City of San Diego's public utilities department operations including, but not limited to, resource management, planned expenditures, service delivery methods, public awareness and outreach efforts, high quality and affordable utility services provided by the public utilities departments, including the Water and Metropolitan Wastewater Departments; and

2) Assist the City in tracking and reviewing the use of rate proceeds to advance the capital improvements related to the rate packages and work programs adopted by the City Council.

Sections 26.2003 (g) and (h) require that IROC assist in the selection and retention of an independent firm to conduct annual financial and performance audits for each public utility department. Sections 26.2003 (c) charges IROC with reviewing independent performance audits on Water and Wastewater systems. At the Audit Committee meeting on October 3rd, the director of the Public Utility Department indicated the Department will fund audit requests made by IROC.

#### Feedback from IROC regarding Performance of Audit Duties

In their Annual Report for FY 2010 (and in previous IROC Annual Reports), IROC notes their "role is not that of an auditor or list checker, but more broadly as an independent overseer of the City's water and wastewater services, on behalf of the ratepayers." As provided above, Section 26.2003 (h) charges IROC to assist in the selection of an independent performance auditor and Section 26.2003 (c) requires them to review the resulting performance audits.

The IBA briefly discussed IROC's delay in requesting performance audits with the current Chair Jim Peugh. Mr. Peugh indicated IROC was aware of the performance audit duties described in the Municipal Code, but suggested Committee members were not sure about available funding for audits and City processes for retaining independent auditors (the independent Office of the City Auditor was not established until 2009). When informed that funds would be available for audits, he indicated IROC put a significant effort into identifying appropriate audit areas. In retrospect, Mr. Peugh indicated that he wished IROC had been more aggressive in seeking information about performance audit resources and assistance earlier. In reviewing IROC's first Annual Report for FY 2008, the IBA notes the Committee understandably spent much of its initial year establishing bylaws/subcommittees, reviewing past/present/planned department activities and endeavoring to learn more about City and other public utility operations.

#### Office of the City Auditor Involvement

In making their FY 2011 budget recommendation for the Office of the City Auditor on April 12, 2010, the Audit Committee recommended Public Utility Department funds (\$100,000) for utility performance audits be transferred to the Office of the City Auditor. The Committee further directed the City Auditor to coordinate performance audits with IROC and serve as its audit resource going forward. The budget recommendation was adopted by the City Council which allowed the Office of the City Auditor to add 1.00 Performance Auditor to their budget.

The Office of the City Auditor subsequently met with IROC on July 12, 2010 to discuss performance audits. It was determined that the Office of the City Auditor should develop a risk assessment and survey to identify key issues and potential audits for the Public Utilities Department. On September 16, 2010, the Office of the City Auditor provided IROC with a risk assessment and a list of performance audit options to consider. IROC agreed with the City Auditor's recommendation that the initial performance audit should focus on the Public Utility Department's Capital Improvement Program. The Office of the City Auditor began the Public Utilities CIP audit in March 2011 and issued their audit report on September 27, 2011.

Plans for Future Public Utility Performance Audits

Utilizing the public utility risk assessment they developed in 2010, the Office of the City Auditor has informed the IBA that they plan to recommend IROC consider requesting a Water Distribution System performance audit with a focus on valve maintenance. Discussion of this recommendation and other future performance audit options is scheduled for IROC's November 21, 2011 meeting.

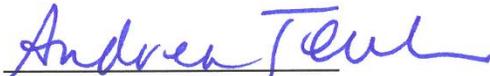
Additionally, the Public Utilities Department has issued a RFP for an Independent Accountant Financial Review of rate increases, sources and uses of debt proceeds and analysis of the Dedicated Reserve from Efficiencies and Savings (DRES). At IROC meetings early in 2011, Department management asked IROC to review/comment on the draft RFP Scope of Work and feedback was provided. IROC will be reviewing the resulting analysis. It is expected that an Independent Accountant contract will be awarded early in 2012. The Audit Committee may wish to request a presentation from the selected accountant and/or IROC once the analysis has been completed.

**CONCLUSION**

In response to IROC audit oversight questions raised by Committee Member Hebrank at the Audit Committee meeting on October 3, 2011, this report provides additional information about purpose/intent and duties/functions of IROC. We reviewed IROC Annual Reports and solicited feedback from the current IROC Chair with respect to their performance audit related duties. Additionally, we discuss the current interaction between the Office of the City Auditor and IROC to identify and request future performance audits related to public utility operations.



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Attachment: San Diego Municipal Code Sections 26.2001 - 26.2003