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INDEPENDENT ACCOUNTANTS' REPORT ON APPLYING AGREED-UPON PROCEDURES

Jim Fisher, Assistant Director
Public Utilities Department, Water Operations
2797 Caminito Chollas
San Diego, CA 92105

We have performed the procedures enumerated below, which were agreed to by the City of San Diego, solely to assist you with respect to the Public Utilities Department, Water Operations (Water Ops) Bid to Goal Program for the year ended June 30, 2009. Water Ops is responsible for the procedures performed on Water Ops' Bid to Goal Program. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of those parties specified in the report. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

We were not engaged to, and did not conduct an audit, the objective of which would be the expression of an opinion, on the Bid to Goal Program. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

Our findings and recommendations related to the Water Ops Bid to Goal Program for the year ended June 30, 2009 are included below. Additional items and areas for improvement that did not impact goal achievement, gainsharing savings, eligibility, or the Assurance Fund have been issued as a separate memorandum and provided to Water Ops.

The purpose and scope of the agreed-upon procedures are as follows:

Savings Calculation

- To perform a comprehensive review of Water Ops' budgetary savings calculation.

Division Performance Goals (Pay for Performance Program)

- To verify adequate documentation supports reported percentages of goals "met" or "partially met."
- To identify practices and procedures to assist Water Ops in improving future Pay for Performance program reporting.

Assurance Fund/Employee Efficiency Incentive Reserve (EEIR)

- To verify the activity in the Assurance Fund is accurate.

Gainsharing and Pay for Performance Payments

- To verify the calculation of employee payouts for the FY09 Bid to Goal Program (net of payroll taxes and other deductions) is accurate.

We performed the following procedures:

Savings Calculation

- Compared total expenditures and encumbrances presented in the Water Ops Bid to Goal FY2009 Annual Report (Annual Report) to the total expenditures and encumbrances reported in the City of San Diego Simpler reports.
- Performed testwork and analysis related to expenditures presented as out-of-scope.
- Performed testwork and analysis related to released encumbrances.

- Recalculated supporting schedules and documentation.
- Recalculated savings based upon results of testwork.
- Reviewed pass-through documentation and calculations.
- Reviewed budgetary documentation and calculations.
- Identified practices and procedures to assist Water Ops in improving future Gainsharing program reporting.

Division Performance Goals (Pay for Performance Program)

- Selected only goals that were reported as met or partially met by Water Ops.
- Reviewed the goals provided by Water Ops and compared them to the goals presented in the goal summaries at the beginning of the fiscal year.
- Judgmentally selected a sample of goals for testing based on the following criteria:
 - Complexity of the goal
 - Coverage of all functional areas
 - Emphasis on goals barely met
 - Emphasis on new goals
 - Emphasis on goals not met in prior year
 - Emphasis on goals with findings in prior year
 - Prior experience with other Pay for Performance programs
 - Results of previous Water Ops Pay for Performance programs
 - Coverage – test at least 50% of goals reported as achieved
- Interviewed goal contacts to gain an understanding of the goal and how it was tracked and measured.
- Reviewed reports and supporting documentation provided by Water Ops to determine the most effective approach for testwork.
- Performed testwork on 9 of the 18 goals provided to us by Water Ops, that were reported as met, and reviewed the supporting documentation to verify goal achievement.
- Performed additional procedures to verify the completeness of the population provided to us by Water Ops.
- Calculated the 2 shared goals that were based upon goals achieved by supported programs.
- Calculated the percentage of goals met, per our testwork, and verified that they agreed with the percentages reported by Water Ops.
- Identified practices and procedures to assist Water Ops in improving future Pay for Performance Program reporting.

Assurance Fund/Employee Efficiency Incentive Reserve

- Reviewed all supporting documentation for the Assurance Fund activity in FY09.
- Reviewed all management approvals for Assurance Fund expenditures.
- Recalculated Assurance Fund activity schedule to ensure accuracy.

Gainsharing and Pay for Performance Payment

- Verified that Water Ops employees listed as eligible met eligibility criteria as listed in Water Ops Division Standard Operations Policy and Procedures Pay for Performance Eligibility and Rules, effective July 1, 2004 (Pay for Performance SOPP) and Water Ops Division Standard Operations Policy and Procedures Gainsharing Eligibility and Rules, effective July 1, 2008 (Gainsharing SOPP).
- Verified that Water Ops employees' eligible hours were accurate.
- Verified that Water Ops employees listed as ineligible were ineligible according to the criteria in the Pay for Performance SOPP and Gainsharing SOPP.
- Verified Water Ops' payout calculation of the net Gainsharing and Pay for Performance Program for all eligible employees was accurate.
- Identified practices and procedures to assist Water Ops in improving determining eligibility in future years.

SAVINGS CALCULATION

SUMMARY:

Water Ops reported savings of \$7,260,583 in the Bid to Goal (Bid) FY 2009 Annual Report (Annual Report). Per the Employee Bid agreement, 50% of the savings reported will be placed in an Assurance Fund for employee payouts. Based upon our comprehensive review, \$7,014,243 should be reported as savings and \$3,507,122 should be eligible to be placed in the Assurance Fund for employee payouts. Adjustments to the savings are included below in Exhibit A.

EXHIBIT A:

Functional Area	Savings per Annual Report	Savings per AKT	Increase (Decrease) in Savings
Treatment Plants	1,181,882	1,181,882	\$0
System Operations	(1,357,930)	(1,357,913)	\$17
Construction	976,061	1,021,142	\$45,081
Administration Support	1,681,155	1,681,155	\$0
Water Quality Laboratory	1,061,531	1,061,368	(\$163)
Engineering	2,973,798	2,744,217	(\$229,581)
Reservoirs and Recreation	955,566	955,566	\$0
Safety	519,244	519,244	\$0
Inflation	362,814	301,120	(\$61,694)
Electrical Consumption Credit	186,924	186,924	\$0
Revenue Credit	67,925	67,925	\$0
FY09 CIP Adjustment	(202,083)	(202,083)	\$0
FY05 thru FY08 CIP Adjustment	(1,146,304)	(1,146,304)	\$0
TOTAL	\$7,260,583	\$7,014,243	(\$246,340)

FINDINGS AND RECOMMENDATIONS:

Finding 1:

Encumbrances set during the fiscal year that are closed subsequent to year-end are allowed to be removed from the total expenditures and encumbrances used in the savings calculation. During our testwork, we identified purchase orders that were opened during fiscal year 2009 and closed subsequent to year-end however were not removed from the total expenditures. We also identified encumbrances opened in fiscal year 2009 and expended subsequent to the fiscal year-end that were inadvertently claimed as released encumbrances. The net difference between the two findings resulted in an increase to the savings.

As a result of these encumbrance errors, the functional areas (over)understated savings by the following amounts:

Functional Area	Understatement (Overstatement) of Budget Savings
System Operations	\$ 17
Construction	46,302
Water Quality Laboratory	(163)
	<u>\$ 46,155</u>

Recommendation:

We recommend that Water Ops carefully review all encumbrances and expenditures that are included in the released encumbrance portion of the budget savings calculation.

Finding 2:

Per the Employee Bid agreement, fringe benefits expenses above 40% of direct labor costs are considered out-of-scope. In our recalculation of the total out-of-scope portion for Construction we identified an overstatement of \$1,221 to fringe benefits.

Recommendation:

We recommend that Water Ops carefully review calculation of fringe benefit expenses to accurately report the out-of-scope portion.

Finding 3:

Management recorded a cost of treated water credit for \$729,365. During our testing, however, we identified an improper calculation for the credit. The Bid price of treated water was understated by \$229,581. This was caused by using the incorrect dollar values documented in the Bid for the calculation. As a result, by subtracting the actual price from the Bid price, the credit was overstated by \$229,581.

Recommendation:

We recommend that Water Ops carefully review the cost of treated water calculation to ensure its accuracy.

Finding 4:

Inflation rates are used City-wide and are adjusted to actual at year-end. We identified in our recalculation that inflation was overstated by \$61,694 creating a decrease of \$61,694 in budget savings.

Recommendation:

We recommend that Water Ops carefully review the inflation calculation to ensure its accuracy.

Finding 5:

Previously, in order to be included in the budgetary savings calculation, encumbrances were required to be released within the three month period following year end. Encumbrances that were released after the three month period were allowed as deductions in the current year due to the late timing of our review.

Recommendation:

We recommend including only those encumbrances released within 3 months following year end to be consistent with prior year reporting.

PAY FOR PERFORMANCE PROGRAM

SUMMARY:

Water Ops instituted a total of 24 goals, 2 of which had sub-components, for the fiscal year 2009 Pay for Performance Program. Of the 24 goals, Water Ops indicated 18 of the 24 goals that comprise the fiscal year 2009 Pay for Performance Program were met or partially met, and the 2 shared goals' percentages were to be determined based upon the results of our review. The 2 shared goals are calculated based upon goal achievement of functional areas that were supported. We calculated the 2 shared goals based upon the results of our testwork. We tested 9 of the remaining 18 goals that were met (50%) to determine if adequate supporting documentation exists to substantiate the status of those goals. Of the 9 goals we tested, we agree with the status reported for 6 goals as met, with exceptions on the other 3 goals. Payouts should be based on the following percentages:

Functional Area	% Met per Water Ops	% Met per AKT	Difference
Administration Support (AS) AS – Shared Goal	100.00% TBD	100.00% ⁽¹⁾ 72.37% ⁽¹⁾	0.00% -
Construction	93.75%	100.00%	6.25%
Production Engineering	100.00%	100.00%	0.00%
Facility Information Management Sections (FIMS) FIMS – Shared Goal	87.50% TBD	50.00% ⁽²⁾ 60.00% ⁽²⁾	(37.50)% -
Systems Operations / Optimization	25.00%	25.00%	0.00%
Reservoirs and Recreation (Lakes)	100.00%	100.00%	0.00%
Safety	58.33%	58.33%	0.00%
Water Treatment Plants/Laboratory	100.00%	66.67%	(33.33)%

(1) Total percentage met for AS is 86.19%

(2) Total percentage met for FIMS is 53.33%

FINDINGS AND RECOMMENDATIONS:

Finding 1:

Facility Information Management Sections' (FIMS) goal number one was reported as partially met with 75% goal achievement. The results of our review did not agree with the status of the goal achievement.

Goal number one states the criteria for goal achievement as "Map Operational and as-built drawings into GIS within 60 days of receipt and notification 95% of the time." Goal number one also states, "Only drawings received from July 1, 2008 through April 30, 2009 will be included." FIMS reported 193 Operational and/or As-built drawings due during the period and 181 mapped within the 60 day criteria, resulting in a 93.8% completion rate (75% payout). Prior to performing testwork, we refined the population FIMS provided to us to exclude Operational and/or As-built drawings (OP/AB) received before July 1, 2008 or after April 30, 2009 to identify a total population of OP/AB drawings received of 198. We then re-calculated achievement based upon the number of days to complete the OP/AB drawings. Of the 198 due, we calculated 186 as completed within 60 days, resulting in a 93.94% achievement.

Once the population within scope was identified, we stratified the population and selected 60 drawings for testwork. During test work we noted instances where drafters posted their drawings (as completed) on the drawing tracking sheet (which agreed to the report used to measure the goal), but made further updates for several days after the post date. Even though this did not affect goal achievement, it undermined the validity of the completion date.

Of those tested, we identified 8 drawings that were either not mapped within 60 days or were missing supporting documentation. When projecting this error across the stratified population, the achievement decreases to 82.3%, resulting in a failure to achieve the goal.

Recommendations:

We recommend that FIMS safeguard original drawings and document when drawings are moved or updated so they can be easily tracked and protected.

AB drawings are date stamped upon receipt by FIMS. However, OP drawings had no such stamp. Therefore, there was often no way to validate the Notify Date for the OP drawings. We recommend that all incoming drawings be date stamped by someone outside the FIMS group. This will establish an objective start date to measure the goal.

We recommend that all drawings be finalized by the drafter before being posted to the SPLASH software as completed.

We recommend that FIMS designate a person who is knowledgeable of SPLASH, Drawing Application Log, and corresponding reports to review all reports that are related to Pay for Performance goals. This person should determine if the report is calculating achievement according to the goal definition. In addition, this person should document the filters and parameters used in measuring goal achievement, including dates within the scope of the goal criteria.

Finding 2:

Water Treatment Plants' (Treatment Plants) goal number three was reported as met. The results of our review did not agree with the status of the goal achievement.

Goal number three states "Complete an inventory of treatment plant facilities requiring maintenance." It further states "Listing of the required facilities will be taken from the construction drawings. A count of the listed facilities will be used to determine the percentage of completion. Inventory will be inputted into spreadsheets, one per plant." Although the goal was reported as 100% achieved, Treatment Plants could not provide a count of the listed facilities that defines the total population. Therefore, we were unable to perform testwork to verify goal achievement. This resulted in a failure to achieve the goal.

Recommendations:

We recommend that Treatment Plants assign responsibility for recordkeeping to one individual at each plant to ensure that supporting documentation is maintained and the goal can be verified.

We also recommend that Treatment Plants create a baseline of facilities to be maintained at each plant from As-Built drawings.

Finding 3:

Construction's goal number two was reported as partially met with 75% goal achievement. The results of our review did not agree with the status of the goal achievement.

Goal number two states "Repair reported distribution service leaks within 7 work days after referral 97.5% of the time." The goal further specifies, "includes work codes 'RPR' (Repair), 'Renew'...'RPL' (Replace), [and] 'RPPOL' (Poly Svc)" and that "only leaks referred from July 1, 2007 through June 19, 2009 will be included." Prior to performing testwork, Construction verified that the goal had a typographical error and the beginning date should have been July 1, 2008.

Construction reported 559 distribution service leaks during the period and 542 were repaired within 7 working days, for a completion rate of 97.0% (75% payout). The report provided to us for testwork included specifications that did not agree with the goal criteria and contained extraneous data such as leaks reported after June 19, 2009, and work codes other than those specified in the goal. Before commencing testwork we sorted and refined the data on the report and calculated 544 reported distribution service leaks as completed during the period and 532 as repaired within 7 working days, for a completion rate of 97.8% (100% payout).

We stratified the population of 532 distribution leaks reported as repaired within 7 work days and selected 60 water Work Orders for testwork. Of the 60 tested, we noted the following data entry errors that did not affect goal achievement:

- a. The Work Order generation date on the Work Order did not agree to the SWIM database (SWIM) on 5 Work Orders.
- b. The Work Order end date on the Work Order did not agree to SWIM on 2 Work Orders.
- c. The work code on the Work Order was different than the work code in SWIM on 2 Work Orders.
- d. The action code on the Work Order was different than the action code in SWIM on 3 Work Orders.
- e. The wrong year was recorded on the Work Order and in SWIM for 1 Work Order.

Recommendations:

We recommend that the goal wording be reviewed to ensure that it accurately defines the goal and is free of typographical errors.

We recommend that IT personnel and those responsible for writing the goal meet before reports are generated to ensure that only data included in the scope of the goal is included in the report and that the report specifications match the goal criteria.

We recommend that the SWIM (Excel) report be reviewed to identify and correct any obvious data entry errors.

We recommend that the Data Management group adhere to its policy to correct Work Orders with typographical errors during the data entry process. This will maintain the integrity of the data used to measure goal achievement and it will prevent confusion about the nature of the work performed.

ASSURANCE FUND

	Year 1 FY2005	Year 2 FY2006	Year 3 FY2007	Year 4 FY2008	Year 5 FY2009
Undesignated funds, beginning of year	\$ -	\$ 3,188,730	\$ 4,259,196	\$ 1,982,848	\$ 2,316,915
Allocation of savings to the Assurance Fund (AF)	<u>4,573,862</u>	<u>4,929,991</u>	<u>4,936,047</u>	<u>4,897,179</u>	<u>3,507,122</u>
AF balance available for payouts/ approved (exp. capped at \$5,600,000)	4,573,862	5,600,000	5,600,000	5,600,000	5,600,000
Gainshairng payout	(1,385,132)	(1,340,804)	(1,965,739)	(1,927,487)	(2,000,000) ⁽¹⁾
Pay for Performance payout	-	-	(624,225)	(428,458)	(575,000) ⁽¹⁾
Approved AF expenses	-	-	<u>(1,027,188)</u>	<u>(927,140)</u>	<u>(1,598,632)</u> ⁽²⁾
Undesignated funds, end of year	<u>\$ 3,188,730</u>	<u>\$ 4,259,196</u>	<u>\$ 1,982,848</u>	<u>\$ 2,316,915</u>	1,426,368
Final amount per testwork					<u>1,440,086</u>
Difference					<u>\$ (13,718)</u>

⁽¹⁾ Amounts are estimated based on anticipated payouts

⁽²⁾ Some expenses are estimated based on amounts that were approved. Actual final costs could differ and the undesignated funds at the end of FY2009 will be updated to reflect those costs.

Finding and Recommendation:

In FY2009, Water Ops included an expenditure that was greater than the amount approved. This caused the “approved AF expenses” line to be overstated by \$13,718.

We recommend that the assurance fund report be reviewed to ensure that only expenditures are only included in the schedule up to the amount that was approved.

GAINSHARING AND PAY FOR PERFORMANCE PAYMENTS

SUMMARY:

Water Ops provided us “Pay for Performance” and “Bid to Goal” Certification Reports (Cert Reports) by Division, employee, and time sheet level. The Cert Reports listed all employees deemed eligible for FY09 Gainsharing and Pay for Performance payments (payouts). These reports also included employees who worked in Water Department divisions that did not participate in the Program and who were ineligible, and did not provide a total number of eligible Water Ops employees. The Cert Reports did not include payout calculations based upon FY09 results. Water Ops also provided us a “Bid to Goal Award Employees Ineligible for Awards” (Ineligible Report). We randomly selected 55 employees deemed eligible, and 5 employees deemed ineligible for FY09 Gainsharing and Pay for Performance payments.

Water Ops provided us a separate payout calculation report after initial testwork described above was completed that included all employees deemed eligible for payouts. This report included 426 employees with a total net

payout of \$1,543,240.05. We traced the 55 employees previously tested for eligibility to the payout calculation report to verify that the information agreed to the Cert Reports. Of the 55 employees, 3 were listed in 2 sections on the payout calculation report and in only 1 section on the Cert Reports and 2 employees were listed in a different section than originally provided to us by Water Ops. Water Ops provided us memorandums signed by the Assistant Public Utilities Director to substantiate the adjustments. We re-calculated the net payout for all employees based upon their eligible hours and Division Performance Goal achievement percentage.

We performed the agreed-upon procedures set forth above to the sample selected. A summary of results is listed below:

Procedures	Number of Exceptions	Error %	Dollar	Error %
Verification of Eligibility	0	0%	N/A	N/A
Verification of Ineligibility	0	0%	N/A	N/A
Verification of payment calculation	0	0%	N/A	N/A

This report is intended solely for the information and use of the City of San Diego and the Public Utilities Department, Water Operations and is not intended to be and should not be used by anyone other than these specified parties.

AKT LLP

AKT LLP
 March 22, 2011