



INTERNAL AUDIT OFFICE

FISCAL YEAR 2016
ANNUAL REPORT

(July 1, 2015 – June 30, 2016)



“Oversight that inspires stakeholder confidence . . . ALWAYS.”

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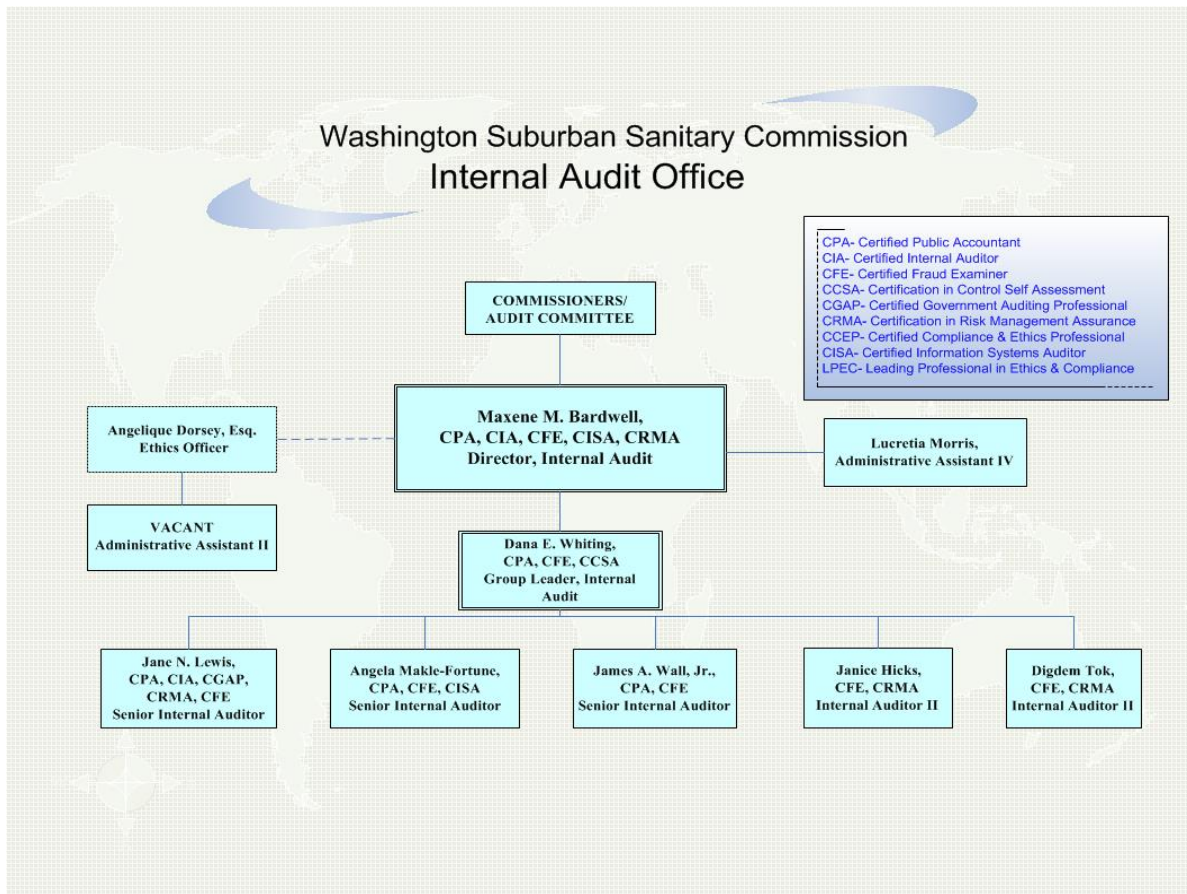
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OUR HISTORY

Established in 1972 by the Washington Suburban Sanitary Commission (WSSC), the Internal Audit Office (IAO) has been in existence for more than 40 years. The IAO was established to provide independent, objective assurance, and advisory services. Together, these services evaluate and improve the Commission’s risk management, control, and governance operations, which are essential to achieving organizational goals and objectives efficiently, effectively, economically, and ethically.

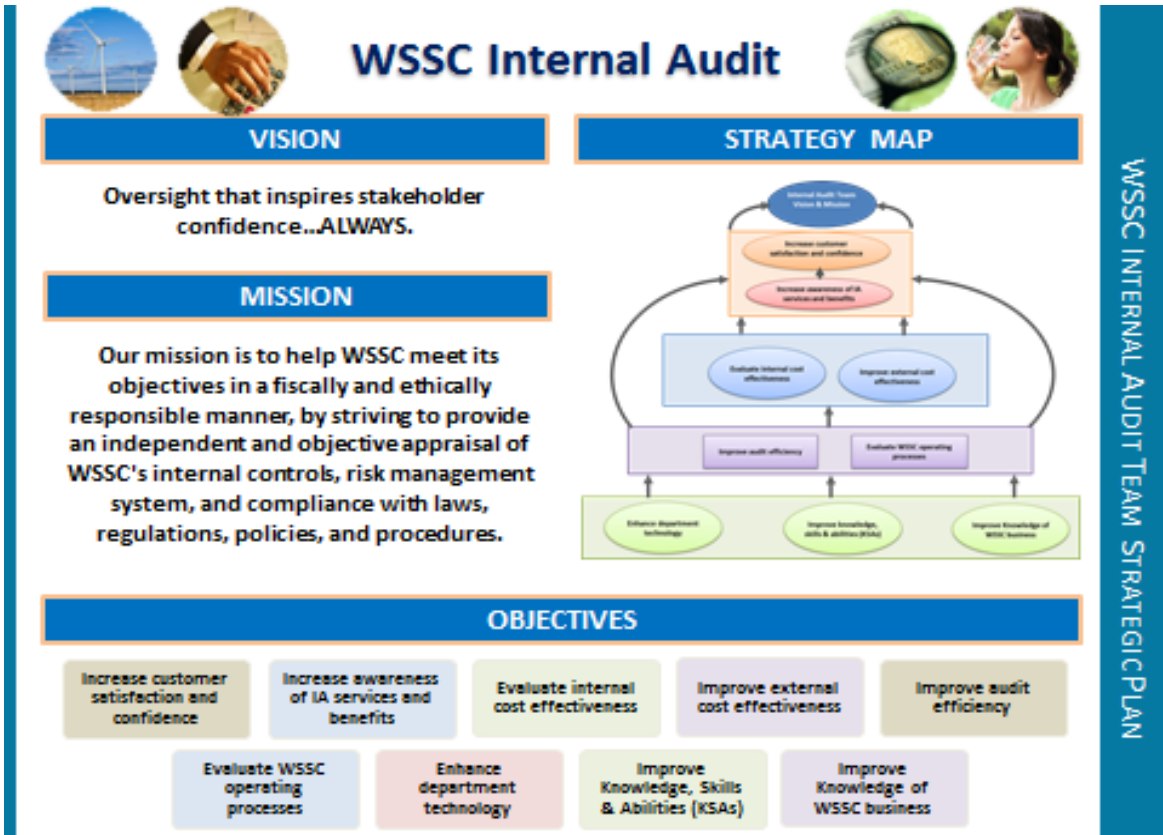
In 2010, the Commission established the Ethics Office to provide day-to-day direction to WSSC’s Ethics Program and execute the Code of Ethics. The Ethics Officer reports administratively to the Internal Audit Director.

To ensure independence, IAO personnel report to the six-member body of Commissioners (also known as the Audit Committee). The Audit Committee was established by the Commission in 2014 “to monitor WSSC’s: audit processes; financial reporting processes; system of internal controls; and compliance with laws, regulations, and the WSSC Code of Ethics.” This reporting relationship fortifies independence, promotes comprehensive audit coverage, and assures adequate consideration of audit recommendations.



OUR PURPOSE/ROLE

The authority and responsibilities of the IAO are detailed in Standard Procedure NR-GOV-IA 2015-001 (also known as the Audit Charter). The Internal Audit Office is recognized as an independent function that has no direct responsibility or authority over any activities audited or reviewed. Our vision, mission, strategy, and nine (9) objectives are disclosed in the snapshot below:



EXECUTIVE SUMMARY

This fiscal year marks the first time in our 44 year history that the internal audit function has officially been recognized as providing world-class services! After undergoing an independent external quality assessment, we earned the internationally recognized distinction of adhering to the Institute of Internal Auditors' *"International Standards for the Professional Practice of Internal Auditing."*

The Internal Audit Office continues to provide value-adding assurance and consulting services for the Commission's internal and external stakeholders. This is accomplished through our dedicated effort to bring a systematic, disciplined approach to evaluate and improve the effectiveness of WSSC's risk management, control, and governance processes.

Over the course of FY 2016 we completed or initiated several audit projects, which resulted in risk-mitigating operational process changes and/or enhancements. However, financial savings from System Development Charges (SDC) audits were substantially lower than prior fiscal years.

We continue to use available resources from the Hotline Response Team consisting of individuals from the WSSC Police Department and the Offices of Equal Employment Opportunity, Ethics, Human Resources, and Internal Audit to successfully conduct fraud, waste and abuse hotline investigations.

We also strive to educate our audit clients about the world-class services we provide and actively demonstrate our care for the environment by volunteering for several outreach activities throughout each fiscal year.

INDEPENDENT EXTERNAL QUALITY ASSESSMENT

BACKGROUND

Established in 1941, The Institute of Internal Auditors (IIA) is an international professional association. It is also the internal audit profession's global voice, recognized authority, acknowledged leader, chief advocate, and principal educator. Its members work in internal auditing, risk management, governance, internal control, information technology audit, education, and security. The IIA's *International Standards for the Professional Practice of Internal Auditing (Standards)* is essential in meeting the responsibilities of internal auditors and the internal audit activity.

Due to WSSC's nature of business, we have adopted the IIA's *Standards* in lieu of others as our benchmark for providing world-class service to our audit clients. The *Standards*, specifically Standard 1312 – External Assessments, states that an external assessment must be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organization to ascertain the degree of conformance with the IIA's *Standards* and professional Code of Ethics. The external quality assessment was conducted by an independent team of reviewers from PBMares, LLP, a leading accounting and business consulting firm serving U.S. and international clients.

SCOPE AND METHODOLOGY

PBMares assessed data obtained from reviewing the internal audit activity's risk assessment and audit planning process, audit tools and methodologies, engagement and staff management processes, workpaper samples and reports. It also surveyed IAO staff, a representative sample of WSSC executives, and conducted extensive interviews throughout the organization.

KEY OBJECTIVES

The principal objectives of the quality assessment were to:

- Assess the internal audit activity's conformance to the IIA's *Standards*;
- Evaluate the internal audit activity's effectiveness in carrying out its mission (as set forth in its charter and expressed in the expectations of WSSC's management); and
- Identify opportunities to enhance its management and work processes as well as its value to WSSC.

The IIA suggests a scale of three ratings, "Generally Conforms," "Partially Conforms," and "Does Not Conform." Generally Conforms means that an internal audit activity has a charter, policies, and processes that are judged to be in conformance with the *Standards*. Partially Conforms means deficiencies in practice are noted that are judged to deviate from the *Standards*, but these deficiencies did not preclude the internal audit activity from performing its responsibilities in an acceptable manner. Does Not Conform means deficiencies in practice are judged to be so significant as to seriously impair or preclude the internal audit activity from performing adequately in all or in significant areas of its responsibilities.










KEY FINDINGS

The independent review team identified one issue concerning our lack of access to records located in the Commission Office. Overall, the independent team of reviewers observed that the WSSC internal audit activity Generally Conforms with the *Standards* or elements of the Code of Ethics (both Principles and Rules of Conduct) in all material respects. Therefore, the WSSC internal audit activity is permitted to state in its audit reports that it conforms with the *International Standards for the Professional Practice of Internal Auditing*.

PBMares also commended the internal audit activity for its audit workpapers, efficiencies gained via audit management software usage, key performance indicators and monitoring process. It recognized the internal audit activity’s clearly defined objectives, employee training, and audit follow-up. The results of the external quality assessment were shared with the Commissioners, executive leaders, and the public during the September 21, 2016, Commission Meeting.

FY 2016 PERFORMANCE RESULTS

The table below provides a two-year qualitative and quantitative review of our key performance indicators (KPIs), which are categorized into four strategic pillars: 1) customer, 2) financial, 3) people, and 4) process.

	Key Performance Indicators	Target	FY' 15 Actual	FY' 16 Actual	FY +/- Variance	Target <, >, or =	Indicator Meter
CUSTOMER	Avg. Percent of Satisfied Clients	90%	N/A	97%	N/A	>7%	
	% of Audit Recommendations Accepted	80%	100%	87.5%	-12.5%	>	
	Average # of Days from Management Implementation to Audit Verification	60 Days	63 Days	123 Days	+63 Days	>3 Days	
	Key Performance Indicators	Target	FY' 15 Actual	FY' 16 Actual	FY +/- Variance	Target +/- or =	Indicator Meter
FINANCIAL	SDC Reimbursements Requests Actual Fiscal Year Cost Savings	Savings	\$102,454	\$29,522	-\$72,932	=	
	Blue Plains O&M Billings Actual Adjustments Credits*	Credits	\$1,318,207	N/A	N/A	N/A	N/A
	Key Performance Indicators	Target	FY' 15 Actual	FY' 16 Actual	FY +/- Variance	Target <, >, or =	Indicator Meter
PEOPLE	Number of Auditors with Required Professional Certifications**	100%	100%	183%	83%	>	
	Annual Completion of 40 Continuing Professional Education (CPE) Hrs.	100%	100%	102.5%	2.5%	>	
	Key Performance Indicators	Target	FY' 15 Actual	FY' 16 Actual	FY +/- Variance	Target <, >, or =	Indicator Meter
PROCESS	% of Carryover Assurance Projects	75%	50%	83%	+33%	>8%	
	% of Assurance Projects Completed ≤ Budgeted Hrs. and/or within Fiscal Year	25%	50%	17%	-33%	<8%	
	% of Continuous Audits Completed within the Fiscal Year	50%	N/A	50%	N/A	=	

*Audit is historically performed on a biennial-basis

** = All internal auditors are required to be certified fraud examiners

Legend:  = Met target,  = Exceeded target,  = Did not meet target

CUSTOMER (STRATEGY FOR CREATING VALUE FOR OUR CUSTOMERS):

Client Satisfaction -- The results of our client surveys distributed during FY '16 indicate 97% satisfaction with IAO services. The 97% satisfaction rate exceeded our target goal of 90% by 7%.

Audit Recommendations – Eighty-seven and one-half percent (87.5%) of Internal Audit recommendations were accepted by management for implementation during FY '16. Therefore, we exceeded our KPI target goal of 80% by 7%. We are also happy to report that we did not experience any delinquent management action plans for accepted recommendations this fiscal year.

Audit Verification -- Based on auditor experience, the previous 30 day KPI verification goal was impractical. Therefore, the 30 day verification goal was changed from 30 days to 60 days for current and succeeding fiscal years. However, due to high client personnel turnover, system learning curve issues, and other matters outside of the control of Internal Audit, our average number of days for verifying the implementation of management action plans was 63 days greater than our new target goal of 60 days. Therefore, this new goal was not met.

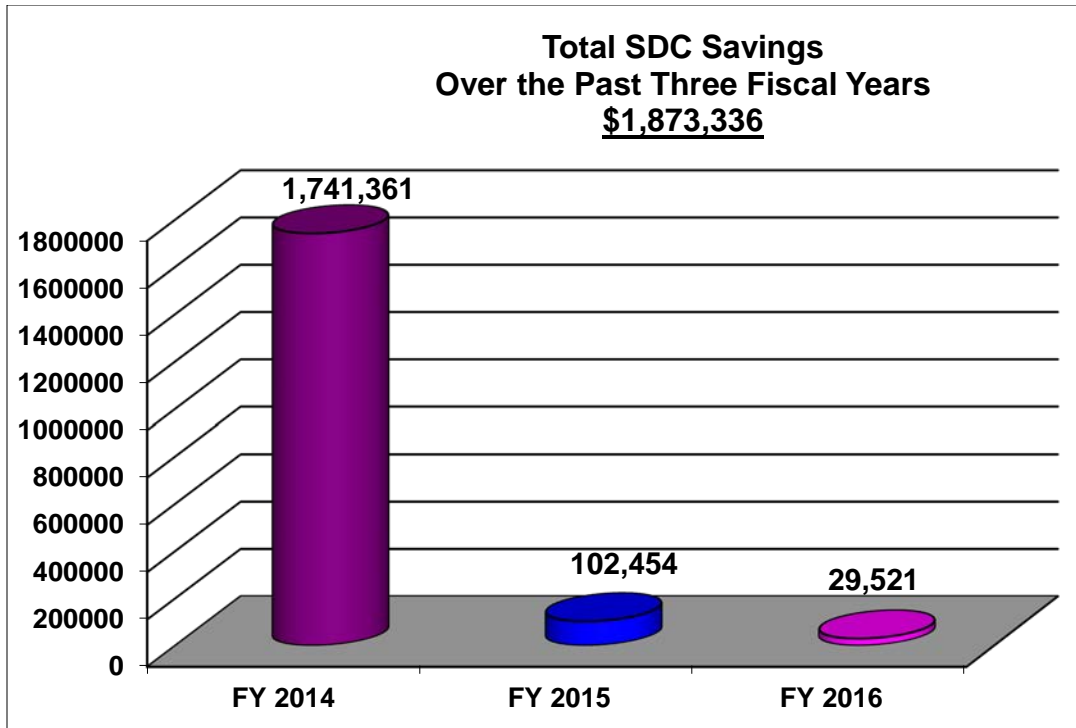
FINANCIAL (STRATEGY FOR FINANCIAL SAVINGS AS VIEWED BY OUR STAKEHOLDERS):

SYSTEM DEVELOPMENT CHARGES (SDC) AUDITS

Maryland Public Utility Article, §25-405(d), "Construction of Facilities," enables the Commission's Internal Audit function to review and approve System Development Charges (SDC), which are costs incurred by developers who design and construct certain facilities as defined by the Article.

Each fiscal year the Internal Audit Office routinely receives written requests to perform SDC audits. The number of SDC audit requests received varies from year to year. In order to complete SDC audits, developers must provide required documentation. Our audits of actual developer costs incurred have led to millions of dollars in adjustment savings over the years.

Currently, we are experiencing substantial lags in processing SDC audit requests due to delays in receiving supporting documentation. Based on these delays, financial savings have fluctuated considerably over the past three fiscal years. As depicted in the graphics below, the FY 2016 financial savings of \$29,522 was significantly less than fiscal years 2014 and 2015 (\$1,741,361 and \$102,453, respectively). The total savings for the last 3 fiscal years is over \$1.8 million.



We are in the process of reviewing viable solutions to address the delays. At the end of FY 2016 there were thirteen (13) SDC audit requests in our possession; however, three (3) were deemed inactive.

BLUE PLAINS WASTE WATER TREATMENT PLANT OPERATION & MAINTENANCE AUDITS

The Blue Plains Intermunicipal Agreement (Agreement) is a documented understanding between the District of Columbia, Fairfax County, Virginia, Montgomery County, Maryland, Prince George’s County, Maryland, and WSSC. In addition to other matters, the Agreement equitably allocates the operation and maintenance costs shared between these parties for the usage of the Blue Plains Waste Water Treatment Plant (Blue Plains). With an estimated usage of 170 million gallons per day (MGD), WSSC’s allocated purchased capacity is approximately 46%.

The Agreement enables its parties to conduct examinations, inspections, or audits of books, accounts, records, documents, and other evidence associated with Blue Plains. We have historically conducted biennial audits of WSSC’s share of the operation and maintenance costs of Blue Plains, which has led to credits to the quarterly billings WSSC prepays in advance of the actual expenses incurred for its aforementioned share. However, an audit was not completed during this reporting period.

PEOPLE (STRATEGY THAT SUPPORTS CHANGE, INNOVATION, AND GROWTH):

Required Professional Certifications -- Internal auditors continuously met or exceeded in this category, which signifies the level of effort we put forth to keep current with trends in our profession and enhance our skill sets to provide world-class services to our audit clients. All internal auditors are now required to be Certified Fraud Examiners (CFEs). This certification enables auditors to perform confidential Fraud, Waste & Abuse Hotline

investigations individually. Additionally, all internal auditors ranked as Senior Internal Auditors or higher are required to be Certified Public Accountants (CPAs) in the State of Maryland. The CPA requirement distinguishes internal auditors from all other Commission positions required to possess accounting experience and knowledge. The CPA credential is highly sought after and not easily obtained, thereby enabling WSSC's internal auditors to tackle complex accounting matters often encountered during audit engagements.

During this fiscal year the Director of Internal Audit and Senior Internal Auditor Angela Makle-Fortune earned the credential of Certified Information System Auditor (CISA) on their first attempt. (The first-time pass rate for this professional certification is only 30%!) The CISA designation is a globally recognized certification for information system, audit, control, assurance and security professionals. In addition to showcasing audit experience, skills, and knowledge, individuals who possess this credential are able to demonstrate that they are capable of assessing vulnerabilities, report on compliance, and establish controls within organizations.

To date, internal auditors have earned one or more of the following professional certifications (as indicated in the IAO's organizational chart appearing on Page 3): Certified Public Accountant (CPA), Certified Internal Auditor (CIA), Certified Fraud Examiner (CFE), Certified Information Systems Auditor (CISA), Certified Government Auditing Professional (CGAP), Certification in Control Self-Assessment (CCSA), and Certification in Risk Management Assurance (CRMA). Overall, this goal was exceeded by 83%.

Continuing Professional Education (CPE) Hours – Each Internal Auditor obtained 40 or more CPE hours targeted for this goal, which helps them maintain active status for their respective professional certifications. In addition to obtaining training from on-line and external parties, each fiscal year we make a concerted effort to gain a better understanding of Commission operations and technologies. During this fiscal year we obtained training in-house from various Teams/Office regarding the following topics: HR Analytics, HR Analytics II, Contract Management, iSupplier, FWA Hotline Process, and Oracle Inventory. We are very thankful to all of the presenters and other involved parties who took time out of their busy schedules to keep us apprised of the Commission's latest technological and operational developments. Some employees of the Internal Audit Office also completed safety courses offered by the WSSC Police Department. This goal was exceeded by 2.5%.

PROCESS (STRATEGY FOR INTERNAL AUDIT PROCESSES THAT CREATES VALUE FOR STAKEHOLDERS):

COMMISSION-WIDE RISK-BASED AUDIT PLANS

Fiscal Year 2016 marks the eighth year that we have been conducting Commission-wide risk-based audits. Taking a Commission-wide approach to assessing risk has enabled Internal Audit to focus its limited resources on the highest risk areas of the Commission. Helping the Commission identify more efficient, effective, and economical ways to reach its objectives enables the IAO function to help the Commission achieve its mission.

The risk assessment is a systematic process for assessing and integrating professional judgments about the probability of adverse conditions and/or events. The process provides a means to organize these judgments so they may be used to assist in developing an audit schedule that helps the Commission obtain its objectives. A vital part of the process entails gathering information from the senior and mid-level managers of the Commission and assessing the relevant risk factors and weighting them through defined impact and probability calculations.

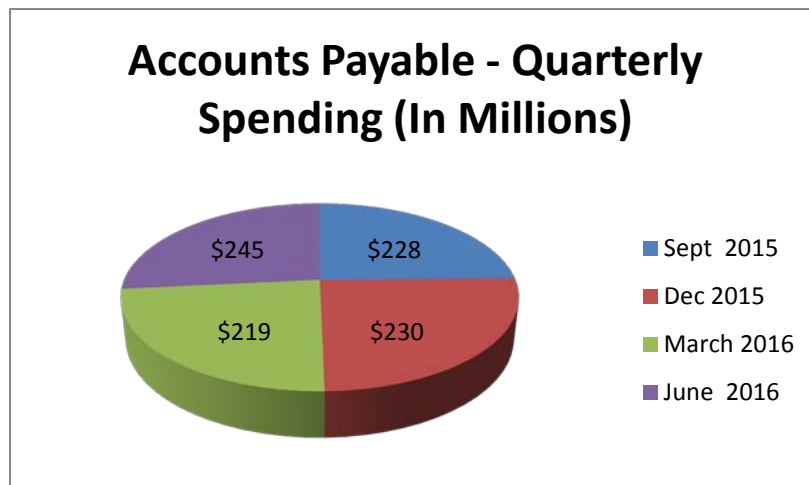
Carryover Assurance Audits – It is our goal to complete audits within our budgeted available audit hours and approved risk-based audit plans each fiscal year. It is customary, however, to experience timing challenges in the years when first-time and Blue Plains audits occur as well as when Hotline investigations take priority or significant client staffing changes arise.

We completed the Customer Relations Group Operational Audit, which resulted in several value-adding recommendations to WSSC management. However, we carried over five out of six audits (83%) of our approved assurance audits from FY 2016 to the next fiscal year. This slightly exceeds our goal of no more than 75% carryover by 8%. Those carryover audits are as follows: Construction Contracts Change Orders, Cloud Computing Services, Payroll Operational Audit, Regulatory Services Group Operational Audit, and Blue Plains WWTP O&M and Capital Indirect Audit (for FY '14).

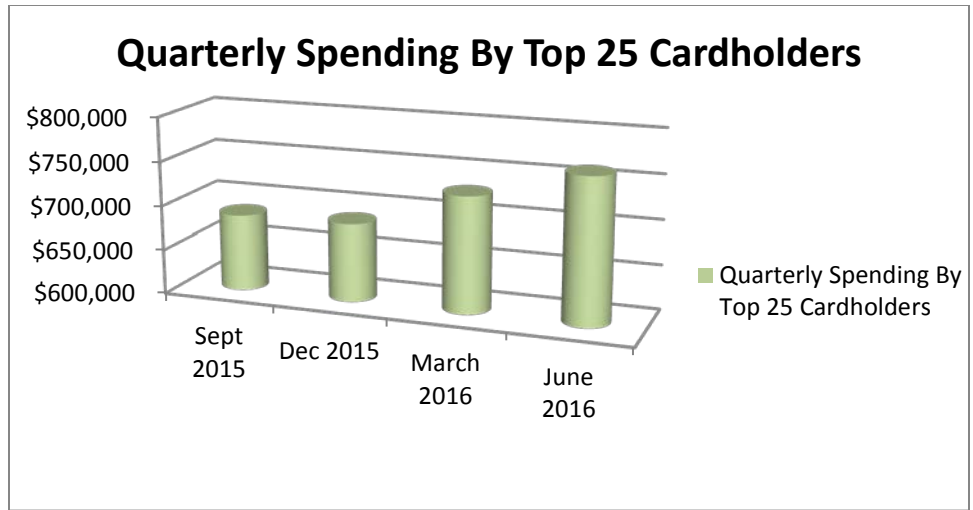
Assurance Projects Completed – The Customer Relations Group Operational Audit completed during FY '16 was completed within the budgeted hours. Yet, its completion only equated to a 17% of approved audit plan projects, which resulted in 8% less than our target goal of 25%.

Continuous Auditing – Due to their high susceptibility for fraudulent activities, continuous audits are conducted for certain areas (i.e., Accounts Payable, P-Cards, and Payroll). On a quarterly-basis the results of reports distributed to management regarding P-Card and Accounts Payable are shared with WSSC’s Audit Committee. Three out of six (50%) quarterly reports were issued timely within the fiscal year. This met the target goal of 50%. Continuous auditing trends are captured in the graphics appearing below.

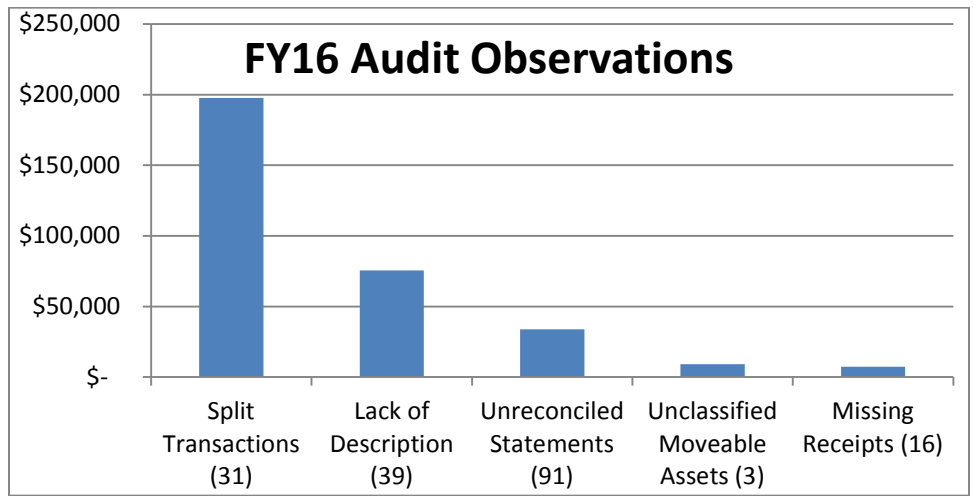
In FY '16, WSSC made approximately 60,000 remittances by check or electronic fund transfers totaling approximately \$230 million on average each quarter and over \$880 million by fiscal year end. There were no identifiable issues regarding WSSC accounts payable throughout the fiscal year.



Fiscal Year 2016 P-Card purchases by the top twenty-five (25) cardholder users occurred in the Laboratory Services Group (\$453,563), Potomac Group (\$159,383), IT Office II (\$124,040), Process Control Group (\$121,784), and Utility Services Group South (\$120,998). The highest purchases occurred in the month of June, which is common practice during the last month of the fiscal budget year.



P-Card observations include the identification of 31 split transactions, 39 instances of lack of description for card purchases, 91 unreconciled monthly statements, 16 purchases with missing receipts, and 3 purchases that were not classified as moveable assets. Information regarding these matters was timely shared with management and addressed accordingly.



We issued several bi-weekly payrolls reports during FY '16. Payroll trends we observed over the course of this and other fiscal years concern issues regarding: 1) prolonged lengths of employment for temporary WSSC employees (including interns); 2) untimely completion of performance appraisals; and 3) excess salaries paid due to grade changes or demotions to lower paying positions. Information regarding these matters was timely shared with management and addressed accordingly.

Additionally, we continue to provide consulting/advisory services by providing advice during various Commission projects from an internal control perspective, including advice on operational policies and procedures. Some projects that we served on as advisors this year include the Records Retention, Internal Security Task Force (ISTF), Capital Asset Management Implementation Plan, Oracle Accounts Payable, Oracle iSupplier, Oracle Inventory, P-Card Steering Committee, and Procurement Phase II & Intake Implementation.



FRAUD, WASTE AND ABUSE HOTLINE

The WSSC Fraud, Waste and Abuse Hotline is available to all internal and external stakeholders 24 hours a day, 7 days per week, and 365 days per year. Hotline investigations are handled by a group of individuals called the Hotline Response Team, which includes Certified Fraud Examiners from the IAO, WSSC Police Investigators, and other individuals who have obtained the experience or training necessary to conduct such examinations relative to their respective areas (for example, equal employment opportunities practice). These individuals also have access to requisite training throughout each fiscal year to ensure best practices for Hotline investigations are administered.

According to the Commission’s Hotline provider (The Network), during FY ‘16 its intake specialists received thirty-two (32) calls. Two (2) were caller callbacks. Fifteen (15) were client follow-up. Seven (7) calls were general inquiries that did not result in completed reports, such as hang ups, wrong numbers, etc. Eight (8) of those calls resulted in incident reports. Seven (7) of the incident reports were anonymous and one (1) was non-anonymous. The chart data below shows a slight decrease in the number of Hotline calls as compared to FY ‘15.

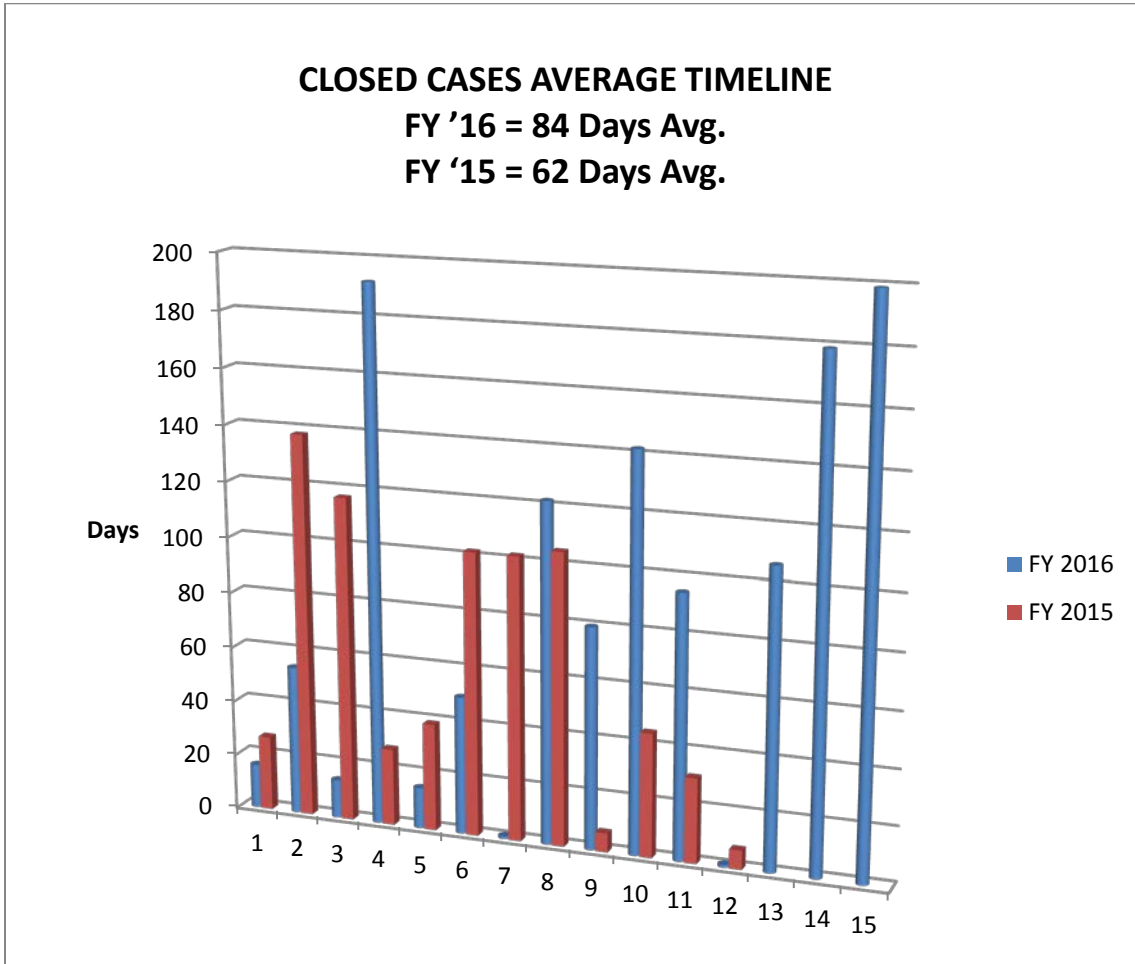
TOP 5 ALLEGATION CASE TYPES:			
FY 2016		FY 2015	
Policy Issues	2	Policy Issues	4
Customer Relations	2	Discrimination	3
Employee Relations	1	Employee Relations	2
Theft of Time	2	Theft of Goods/Services	2
Conflicts of Interest	1	Kickbacks	2

Top Five Case Types -- The top five case types for the past twenty-four months show a decrease by two (2) for alleged policy issues, while employee relations allegations decreased by one (1), and theft of time, goods, and/or service allegations remained constant at two (2).

Closed Cases Timeframe -- As of June 30, 2016, Hotline investigations are averaging 84 calendar days from commencement to closure. This is an increase of 22 calendar days when compared to FY ‘15 statistics of 62 days. Three (3) of the cases closed averaged more than 160 days to investigate.

During FY ‘16, fifteen (15) cases were closed. The closed case types consisted of: four (4) conflicts of interest; three (3) each for operational, compliance, and customer relations; and two (2) security and safety. Twelve (12) cases were closed during the preceding fiscal year. The closed case types during that period included: four (4) compliance; three (3) each for operational and safety issues & sanitation; and one (1) each for customer relations and conflicts of interest.

Six (6) of the fifteen (15) cases closed in FY '16 were substantiated; five (5) cases were unsubstantiated; one case was partially substantiated; and three (3) cases were found to be inconclusive. The substantiated and partially substantiated cases led to recommendations for corrective action.



INTERNATIONAL INTERNAL AUDIT AWARENESS MONTH

In recognition of International Internal Audit Awareness Month, members of the IAO hosted an open house event on May 11, 2016, to educate Commission employees about the services we offer. During the event we welcomed numerous employees including General Manager/Chief Executive Officer, Carla Reid, and Corporate Secretary, Sheila Finlayson.



More than 100 Commission employees visited our open house to meet IAO employees and learn about how we can better serve them. A special thank you goes out to all Commission employees as well as the Graphics Department, and other Communications Office team members for continuing to make this a successful event each fiscal year.

OUTREACH ACTIVITIES

Throughout each fiscal year we participate in various outreach events sponsored by the Commission, including events occurring on weekends. This is done in our effort to support WSSC's core values such as environmental stewardship and safety awareness. Specifically, Internal Audit Office staff volunteered in the Fall Watershed Stewardship opportunities at Tridelphia Recreation Area and Sweitzer Lane Adopt-A-Road Clean-Up as well as participated in the Annual Children's' Water Festival, WSSC Blood Drive, Principal for a Day, WSSC in the Classroom, WSSC's 6th Annual Women Business Owners' Expo, WSSC Mentoring Program, Salvation Army Angel Tree, and other activities offered by the Commission as we strive to give back to the Washington Suburban Sanitary District.

Salvation Army Angel Tree



Tridelphia Recreation Area Tree Mulching



Annual Women Business Owners' Expo



Adopt-A-Road Clean-Up



CONCLUSION

During FY 2016 we were officially recognized as providing world-class internal auditing services to our audit clients and the Commission as a whole. This accomplishment could not have been done without the combined effort of all of the Internal Audit & Ethics Office team members, the WSSC Audit Committee, Executive Leadership, and our audit clients who continue to support us.

This achievement is something we have strived for all along. As has been stated each fiscal year, everything we undertake cannot always be quantified, yet we continue to add value in numerous ways. We hope that by reading this report we have shown you how WSSC's Internal Audit Office helps support WSSC's vision. Our client surveys show we are surpassing their expectations and volunteering for various outreach events helps sustain the environment. In the end, we want all internal and external customers to be delighted with our world-class services.

We plan to continue to work together with our audit clients to help accomplish the Commission's strategic goals and support its mission to provide safe and reliable water, life's most precious resource, and return clean water to our environment, all in an ethical, sustainable, and financially responsible manner. Thank you for allowing us to serve you.