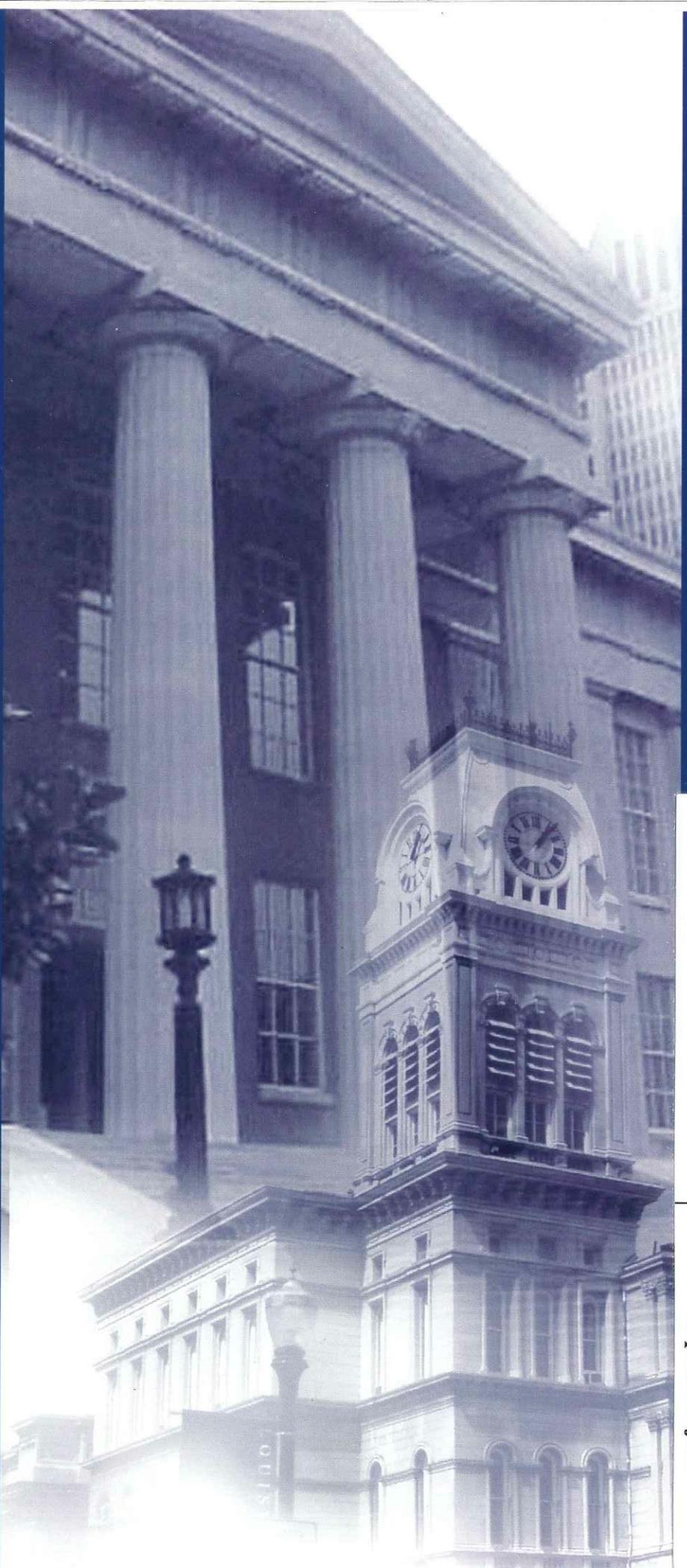




Jerry E. Abramson  
Mayor  
Louisville Metro Council

The Office of Internal Audit provides independent, objective assurance and consulting services that adds value to and improves Louisville Metro Government.



# Office of Internal Audit

Louisville Metro Government

Miscellaneous Building Repairs  
Capital Project

# Audit Report

Office of Internal Audit

## Louisville Metro Government

### Miscellaneous Building Repairs Capital Project

September 2009



Louisville Metro Government

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Miscellaneous Building Repairs  
Capital Project

## Table of Contents

<b>Transmittal Letter .....</b>	<b>2</b>
Introduction.....	2
Scope.....	3
Opinion .....	3
Corrective Action Plan.....	4
Internal Control Rating .....	5
Background.....	6
Summary of Audit Results.....	6
<b>Observations and Recommendations.....</b>	<b>8</b>
Scope and Methodology .....	8
#1 – General Administration.....	9
#2 – Appropriations .....	14



OFFICE OF INTERNAL AUDIT  
LOUISVILLE, KENTUCKY

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**Transmittal Letter**

September 22, 2009

The Honorable Jerry E. Abramson  
Mayor of Louisville Metro  
Louisville Metro Hall  
Louisville, KY 40202

**Subject: Audit of Miscellaneous Building Repairs Capital Project**

**Introduction**

An audit of the Miscellaneous Building Repairs and Minor Renovations capital project was performed. The objective was assessing compliance with the intended use of the appropriation and contractual terms with suppliers. The focus was expenditures for the life of the project. This was originally part of the Public Works and Assets capital projects audit. Due to the nature of the issues identified, and to ensure appropriate accountability, it was determined that the Miscellaneous Building Repairs and Minor Renovations capital project merited a separate review.

The audit was conducted in accordance with Government Auditing Standards issued by the Comptroller General of the United States and with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

As a part of the review, the internal control structure was evaluated. The objective of internal control is to provide reasonable, but not absolute, assurance regarding the achievement of objectives in the following categories:

- Achievement of business objectives and goals
- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations
- Safeguarding of assets

There are inherent limitations in any system of internal control. Errors may result from misunderstanding of instructions, mistakes of judgment, carelessness, or other personnel factors. Some controls may be circumvented by collusion. Similarly, management may circumvent control procedures by administrative oversight.

### Scope

The Miscellaneous Building Repairs and Minor Renovations capital project was reviewed. The objective was assessing compliance with the intended use of the appropriations, and with the terms of supplier contracts. Detailed policies and procedures were not considered within the scope of the review, nor was the bid and award process for supplier contracts. The review period covered project inception through January 31, 2009.

An understanding of the capital project was obtained through the examination of supporting documentation. This included obtaining an understanding of project objectives, goals and expenditure activity. Documentation reviewed included Louisville Metro Ordinances, capital budgets, financial system records, purchase orders, invoices, payment documents and other supporting documentation.

A sample of expenditures from the Miscellaneous Building Repairs and Minor Renovations capital project was reviewed. The activity was verified to the intended purpose of the appropriation and to the contractual terms for the supplier. Also, budget revisions were reviewed to determine the justification and appropriateness of the activity. The details of the scope and methodology of the review are addressed in the Observations and Recommendations section of this report. The audit would not identify all issues because it was based on selective review of activity.

### Opinion

It is our opinion that the internal control structure for the Miscellaneous Building Repairs and Minor Renovations capital project needs improvement. The internal control rating is on page 5 of this report. This rating quantifies the opinion regarding the internal controls. Specific results include the following.

- **General Administration.** There were issues noted with the general administration of the Miscellaneous Building Repairs and Minor Renovations capital project.
  - *Processing of Activity.* Beginning in Fiscal Year 2007, Finance and Administration personnel initiated, authorized, and processed activity in the capital project account even though this was a Public Works and Assets capital project account. Finance personnel should not have had the ability to charge activity to this account without Public Works and Assets involvement. Current Public Works and Assets Business Office personnel were unaware that Finance processed activity in the capital project account.
  - *Procurement Policy.* Metro policy was not followed in the procurement of goods exceeding \$10,000. Finance personnel created a purchase order for \$17,150 without going through Metro Purchasing. Thus, the goods were not procured using one of Metro's approved methods. It could not be determined if this occurred because of a financial system weakness, or if it was the result of the internal controls being overridden.

- *Contractual Compliance.* Issues were noted in verifying compliance of activity with contractual terms. There were cases in which the procurement was made using a State contract. The contract states the price of the goods or services will be a fixed percentage price reduction discounted from the manufacturer's price list at the time of purchase. The manufacturer's price list at the time of purchase was not documented; therefore compliance could not be verified. There was another transaction that could not be verified to contractual terms because the invoice did not contain enough information to determine the goods and services actually provided.
- **Appropriation.** Expenditure activity for the Miscellaneous Building Repairs and Minor Renovations capital project was in compliance with the intended use of the appropriation. There was one minor documentation issue noted.

**Corrective Action Plan**

Representatives from Finance and Administration were asked to provide a corrective action plan. The corrective action plan is included in this report in the Observations and Recommendations section. We will continue to work with Finance and Administration to ensure the actions taken are effective to address the issues noted.

Sincerely,

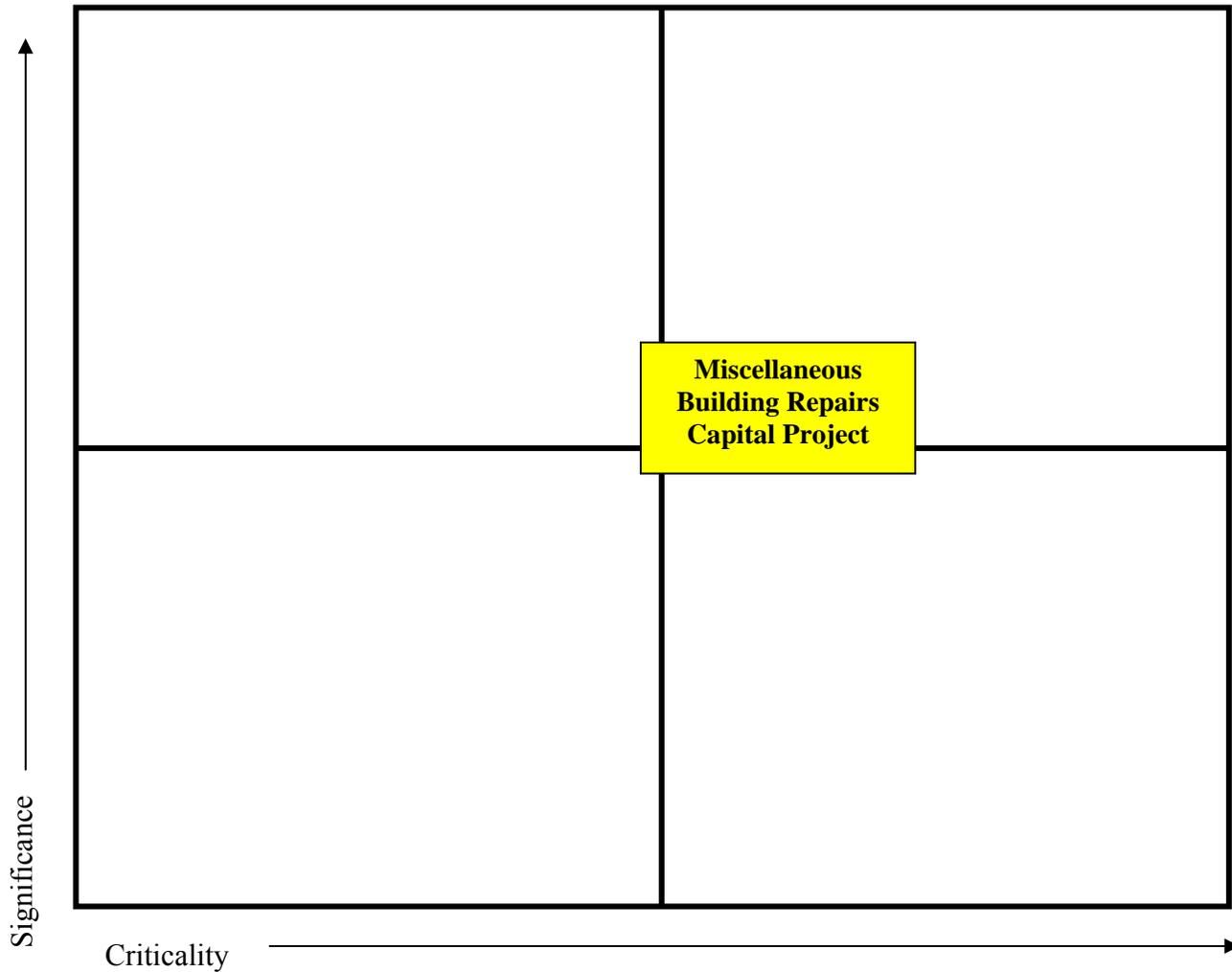


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Michael S. Norman, CIA, CFE, CGAP  
Chief Audit Executive

cc: Louisville Metro Council Government Accountability and Audit Committee  
Director of Finance and Administration  
Director of Public Works and Assets  
Louisville Metro External Auditors

**Internal Control Rating**



<u>Legend</u>			
<u>Criteria Issues</u>	<u>Satisfactory</u> Not likely to impact operations.	<u>Needs Improvement</u> Impact on operations likely contained.	<u>Inadequate</u> Impact on operations likely widespread or compounding.
<i>Controls</i>	Effective.	Opportunity exists to improve effectiveness.	Do not exist or are not reliable.
<i>Policy Compliance</i>	Non-compliance issues are minor.	Non-compliance issues may be systemic.	Non-compliance issues are pervasive, significant, or have severe consequences.
<i>Image</i>	No, or low, level of risk.	Potential for damage.	Severe risk of damage.
<i>Corrective Action</i>	May be necessary.	Prompt.	Immediate.

## **Background**

Capital projects are authorized by ordinances approved by the Louisville Metro Council. The projects involve activities related to acquiring, constructing, maintaining, repairing, or improving Louisville Metro's public works.

Capital projects may be authorized as part of the annual budget process or appropriated at any time during the fiscal year. Each capital project has a specific description that summarizes the scope of work to be performed. Overall project scope cannot be significantly changed without the approval of the Metro Council. Projects may also be funded through the issuance of bonds. Bond legislation details the intended use of funds and is approved by ordinance enacted by the Metro Council.

The Miscellaneous Building Repairs and Minor Renovations capital project provides funding for repairs and minor renovations to Metro owned buildings and other public facilities. These funds are used for both routine and emergency repairs to building systems (e.g., heating, air conditioning, plumbing, elevators) and structures. These funds are also used for minor renovations to office space to increase efficiencies and improve general working conditions.

As of January 31, 2009, the total amount of capital and carry forward funds appropriated for the Miscellaneous Building Repairs and Minor Renovations capital project was approximately \$878,980 and the total project expenditures were approximately \$649,460.

Initially, the Miscellaneous Building Repairs and Minor Renovations capital project was part of the Public Works and Assets capital projects review. Due to the nature of the issues identified, and to ensure appropriate accountability, it was determined that this capital project merited a separate review.

## **Summary of Audit Results**

### **I. Current Audit Results**

See Observations and Recommendations section of this report.

### **II. Prior Audit Issues**

The Office of Internal Audit has not performed any previous reviews of the Miscellaneous Building Repairs and Minor Renovations capital project.

### **III. Statement of Auditing Standards**

The audit was performed in accordance with Government Auditing Standards issued by the Comptroller General of the United States and with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

#### **IV. Statement of Internal Control**

An understanding of the internal control structure was obtained in order to support the final opinion.

#### **V. Statement of Irregularities, Illegal Acts, and Other Noncompliance**

The review did not disclose any instances of irregularities, any indications of illegal acts, and nothing was detected during the review that would indicate evidence of such. Any significant instances of noncompliance with laws and regulations are reported in the Observations and Recommendations section of this report.

#### **VI. Views of Responsible Officials / Action Plan**

Due to the nature of the issues noted, a draft report was issued to the Metro Department of Finance and Administration on May 19, 2009. An exit conference was held at Finance on June 22, 2009. Participating were Jane Driskell, Kevin Moore, and Daniel Frockt representing Finance; and Michael Norman representing Internal Audit. Preliminary audit results were discussed. A follow up meeting was held at Finance on July 1, 2009. Participating were Jane Driskell, Kevin Moore, and Daniel Frockt representing Finance; and Ingram Quick representing Internal Audit. Audit results were discussed.

A final draft report was issued to the Metro Department of Finance and Administration on August 18, 2009. The views of Finance and Administration officials were received on September 18, 2009 and are included as corrective action plans in the Observations and Recommendations section of the report.

LMCO §30.36(B) requires Louisville Metro Agencies to respond to draft audit reports in a timely manner. It specifically states that

*“The response must be forwarded to the Office of Internal Audit within 15 days of the exit conference, or no longer than 30 days of receipt of the draft report.”*

Finance and Administration’s response was provided within this required timeframe.

## Observations and Recommendations

### **Scope and Methodology**

The Miscellaneous Building Repairs and Minor Renovations capital project was reviewed. The objective was assessing compliance with the intended use of the appropriations, and with the terms of supplier contracts. Detailed policies and procedures were not considered within the scope of the review, nor was the bid and award process for supplier contracts.

An understanding of the capital project was obtained through the examination of supporting documentation. This included obtaining an understanding of project objectives, goals and expenditure activity. Research was performed and background information obtained in order to identify guidelines and authorizations associated with the capital project expenditures.

A judgmental sample of expenditures from the capital project was examined. In addition, all budget revisions associated with the capital project were reviewed. Documentation reviewed included Louisville Metro Ordinances, capital budgets, budget revisions, financial system records, purchase orders, contracts with specific vendors, invoices, payment documents and other supporting documentation. The activity reviewed was from project inception through January 2009. The audit would not reveal all issues because it was based on a selective review of data.

### **Observations**

Some issues were noted with the Miscellaneous Building Repairs and Minor Renovations capital project activity. As a result, the internal control structure is impaired and needs improvement. Results are as follows.

#1 – General Administration

#2 – Appropriations

Details of these begin on the following page.

## **#1 – General Administration**

Issues were noted with the general administration of the Miscellaneous Building Repairs and Minor Renovations capital project. Specifics include the following.

- **Processing of Activity.** Beginning in Fiscal Year 2007, Finance and Administration personnel initiated, authorized, and processed activity in the Miscellaneous Building Repairs and Minor Renovations capital project account. This activity was related to the renovation of Finance’s office space. This was a Public Works and Assets capital project account. Therefore, Finance personnel should not have had the ability to charge activity to this account without the involvement of Public Works and Assets.
  - According to current Public Works and Assets Business Office personnel, they were under the assumption the Miscellaneous Building Repair and Minor Renovations capital project account was dormant. They were aware that funds had been set aside in the account for the Finance renovations, but they were not aware that Finance processed activity in the account. This may have been the result of miscommunication when a departmental transition occurred involving Public Works and Assets.
  - Finance and Administration was asked to provide an explanation of why a separate capital project account was not established for the Finance Renovation. Finance provided the following response.

“Facility repairs and minor renovations are budgeted in Facilities Management because they oversee those projects. As your documentation shows, the invoices were received in Facilities Management and approved by Facilities Management staff that were involved in the Finance renovation. General repairs are not distinct projects that are budgeted in each department. Multiple capital accounts are treated in this manner. For example, sidewalk repairs are budgeted in one capital account, not a distinct account for each sidewalk project. Another example is the capital roadway repair account. Roadway repair projects are budgeted to one project account, not a separate account for each repair project.”
  - The following is a general summary of items related to the Finance office renovations that were charged to the Miscellaneous Building Repairs and Minor Renovations capital project account. This activity was processed by Finance.

– Office Furniture and Equipment	\$47,215
– Carpet	\$17,150
– Window Replacement	\$ 5,182
– Moving Expenses	\$ 1,415
- **Procurement Policy.** Metro policy requires that purchases exceeding \$10,000 be procured using one of several methods. The primary methods are competitive negotiations, competitive bidding, noncompetitive negotiations, sole source, and state contract. There was a policy compliance issue noted.
  - Finance did not comply with Metro policies and procedures in the procurement of carpet for Phase B of the office renovation. Finance personnel created a purchase

order for \$17,150 without going through Metro Purchasing. Therefore, it was not procured using one of the approved methods. It could not be determined if this occurred because of a financial system weakness, or if it was the result of the internal controls being overridden.

- Finance had a contract with the same supplier for carpet for Phase A of the office renovation. This contract had been bid, and had a purchase order established by Metro Purchasing. The full amount of this contract had been expended on Phase A of the renovation. Finance personnel could have initiated a change order to use the existing contract. This would have required the assistance of Metro Purchasing. This was not done.
- **Contractual Compliance.** Issues were noted in verifying compliance of activity with contractual terms.
    - *Price List Documentation.* There were two cases in which it could not be determined if the expenditure was in compliance with contractual terms. This was due to the inability to obtain the price list effective at the time of the procurement. The contract states the price of the goods or services will be a fixed percentage price reduction discounted from the manufacturer's price list at the time of purchase. The manufacturer's price list at the time of purchase was not documented. Therefore, there was no way to determine if the amount charged was in accordance with the contractual terms.
      - One case involved the procurement of fifty-two chairs at a total cost of \$22,100.
      - The other case involved the procurement of various office furniture and equipment at a total cost of \$25,114.
    - *Invoice Documentation.* One transaction involved services procured to replace windows. It could not be determined if the expenditure was in compliance with contractual terms due to the lack of detail on the invoice. The invoice only listed a lump sum amount for removing six windows and replacing them with six new arch type windows. However, the contract's price list included the type of glass and the cost per square foot for each type of glass. The documentation did not include the type and size of the glass, so the price charged could not be verified.
      - The total invoice amount was \$10,182 but only \$5,182 was charged to the Miscellaneous Building Repairs and Minor Renovations capital account. The remaining \$5,000 was charged to another capital project titled Facilities Consolidation. There was no documentation explaining why the invoice was split between these two capital projects. Determining the appropriateness of using the Facilities Consolidation capital project account was not within the scope of this audit. Therefore, it was not reviewed.

### **Recommendations**

Appropriate personnel should take corrective action to address the issues noted. Specific recommendations include the following.

- ✓ The ability for Finance personnel to charge activity to a capital project under the management of another department is not a recommended business practice. This practice weakens accountability for activity. The financial system should be

reviewed to determine if this occurred because of control weaknesses or override of controls. Any control weaknesses identified should be corrected. In the case of override of controls, there should be documentation explaining the need for the override. The documentation should include appropriate levels of approval. In addition, overrides should be tracked and fully disclosed to external financial auditors.

- ✓ The department responsible for the capital project should be authorizing charges and processing payment documents for project expenditures. Departments should not have the ability to process activity to capital projects that they are not responsible for administering. Activity could still be charged to the capital project, but it should go through the administering department.
- ✓ System administrator and other “super user” type roles should be reviewed to ensure they are assigned to individuals that are not involved in processing activity. This helps ensure the integrity of financial activity and compliance with Metro policies by appropriately segregating duties and access rights. Ideally, the financial system administrator would not be part of the Finance department, but instead should be part of the Information Technology group.
- ✓ Metro procurement policies are designed to help ensure compliance with applicable state and local laws and requirements. All personnel involved in procuring goods or services should be properly trained on the policies. Exceptions to policy should be thoroughly documented and approved.
- ✓ Departments procuring goods and services using contracts should ensure the goods or services are covered by the contract. In addition, a copy of the contract effective at the time of the procurement should be retained, and terms verified prior to authorizing payments.
- ✓ Activity processed using contracts in which the price terms are a discount from current prices should be properly documented. The documentation should include the price at the time the order was placed, and the discounted price that will be invoiced. This should be part of the supporting documentation with the payment document.
- ✓ As part of the payment approval process, appropriate personnel should thoroughly review invoices to ensure accuracy, appropriateness, and agreement to contractual terms. Supporting documentation should be explicit as to the services / work performed or goods provided. Enough documentation should be provided to allow independent verification of expenditures to the contractual terms. This should be accomplished solely by reviewing the supporting documents. If this level of detail is not provided, an additional documented explanation should be included in the supporting documentation.
- ✓ Care should be taken to ensure invoices are charged to the proper capital project financial coding. If an invoice is charged to two different capital projects, there should be a documented explanation as to why two different capital projects paid for the invoice.
- ✓ Routine supervisory review should be performed by departments to assess the completeness of capital project files and the accuracy of the activity, including the adherence to the procurement policy. These reviews, and any necessary corrective actions, should be documented.

### **Finance and Administration's Corrective Action Plan**

Finance is responsible for maintaining all financial transactions and places great importance on the administration of Capital Projects.

This project was active when the Facilities Management was a division under General Services Administration Department. The Director of Facilities Management at the time of the project was fully aware of the funds that were set aside for the renovation; the expenditures were being reviewed and approved by the Facilities Management project manager but processed by Finance personnel and charged to the Miscellaneous Building Repair and Minor Renovations account.

The director left Facilities Management in May 2007 and there have been several staff changes in the Public Works & Assets (PW&A) business office since this project was completed. Information related to this project may not have been communicated during the business office transition.

The invoices the auditor has commented on were mailed to Louisville Metro GSA, 531 Court Place, STE 801, and have a stamp on them that states "Received – GSA Business Office". These documents were reviewed and signed by the PW&A project manager, indicating the goods/services were received in accordance with contractual terms. Finance believes this information substantiates the fact that at the time of the project, appropriate PW&A (Facilities Management, General Services Administration) staffs were aware of and authorized the expenditures.

Finance has reviewed the general administration recommendations of Internal Audit and has commented on the recommendation or provided the corrective action below. It is important to note that many of the auditor's recommendations were addressed prior to the review of this activity from 2007 or the issuance of this report.

- ✓ Internal Audit is aware that Finance maintains access to departmental charge accounts outside of Finance. Finance currently processes invoices on behalf of and at the request of Internal Audit, Human Resources and Information Technology departments.
- ✓ Expenditures processed by Finance and charged to other departments have been reviewed and the standard operating procedure changed. Documentation will substantiate approval for the transaction. A recent example of this was a payment that was processed by Finance and charged to Information Technology. The payment documentation on file in Accounts Payable clearly substantiates IT's understanding of the transaction.
- ✓ Financial system access verification is complete. The functional system administrator that works in Finance is dedicated solely to supporting financial system users and does not engage in processing activity outside of helping system users understand the functionality of Oracle Financials. Finance believes its ideal for this person to work in and report to the Chief Financial Officer. Moreover,

operating, database and technical system administration functions are fully controlled by Information Technology through a managed service provider that Metro Government contracted with in October 2008.

- ✓ Prior to the issuance of this report, Finance reorganized its business office and a thorough review of financial system access has been performed. All personnel responsible for Finance invoice processing have appropriate approval levels established in the financial system, using the same core system responsibility as all other business units in Metro Government. Additionally, invoices are thoroughly reviewed by a minimum of two staff persons to ensure accuracy, appropriateness, and agreement to contractual terms prior to approval for payment and submission to Accounts Payable for final processing.
- ✓ The Purchasing, Accounts Payable, Accounting, Grants, Payroll and Risk Management divisions of Finance offer training opportunities to departmental business staff. Finance continues to hold monthly business manager meeting to disseminate information to appropriate departmental staff and to promote consistency in applying Metro's policies and procedures.
- ✓ Departments using State contracts are required to submit copies of the contract when processing the requisition to Purchasing. While the State contract was valid, it cannot be determined why the contract price list was not provided; however, purchasing staff approved the Purchase Order. The Purchasing department became a division of Finance after this activity occurred. As a result of this review, the use of State contracts and the necessity of maintaining copies of the State contract have been reviewed with the Purchasing Manager.
- ✓ Metro policies do not prohibit a department from distributing costs to two capital projects as long as the activity being charged to the capital project(s) is within the scope of that project and accounted for properly.
- ✓ Routine supervisory review is performed to ensure completeness of files and the accuracy of the activity, including the adherence to Metro's procurement policy.

## **#2 – Appropriations**

The activity for the Miscellaneous Building Repairs and Minor Renovations capital project was in compliance with the intended use of the appropriations. There was one minor documentation issue noted. Additional explanation had to be provided by Metro Budget personnel for a \$150,000 budget revision. The explanation provided appears reasonable. However, the lack of complete documentation weakens the paper trail and impairs accountability by increasing dependence on key individual's memories to explain activity.

### **Recommendations**

Appropriate personnel should take corrective action to address the issues noted. Specific recommendations include the following.

- ✓ Budget revision activity should have sufficient documentation to support the transaction. The documentation should include both the authorization for the activity, as well as the justification.
- ✓ Periodic supervisory review should be performed to ensure appropriate support documentation is retained for the budget revision activity.

### **Finance and Administration's Corrective Action Plan**

Finance has reviewed the appropriation recommendations of Internal Audit. Finance agrees with both recommendations suggested; however, Finance asserts that the very budget revision noted is an example of its ongoing commitment to documentation and periodic supervisory review (the two recommendations listed). It should also be noted that more than half a dozen budget revisions (aside from the one noted) were pulled for review, none of which required additional explanation.

As to the specific budget revision noted, it was believed to be appropriate to list the transfer of operating funds to a capital project as part of the year-end ordinance (FY07). Since the prior year's transfer was similar in nature to the FY07 year-end transfer, it was decided after a periodic review and with regard to documentation of the FY06 transfer that it too should be listed in the ordinance as well.

It is unclear from the recommendation how a periodic supervisory review of budget revision activity could be undertaken and acted upon without becoming an item of note—that is, how are supplemental actions based on periodic review to be undertaken?



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**Name of Report** Miscellaneous Building Repairs and Minor Renovations Capital Project

<b>How do you rate this report?</b>			
	<b>Beneficial</b>	<b>Somewhat Helpful</b>	<b>Needs Improvement</b>
Background Information	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Details	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Length of Report	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Clarity of Writing	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Potential Impact	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Suggestions, comments, ideas, thoughts: \_\_\_\_\_

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