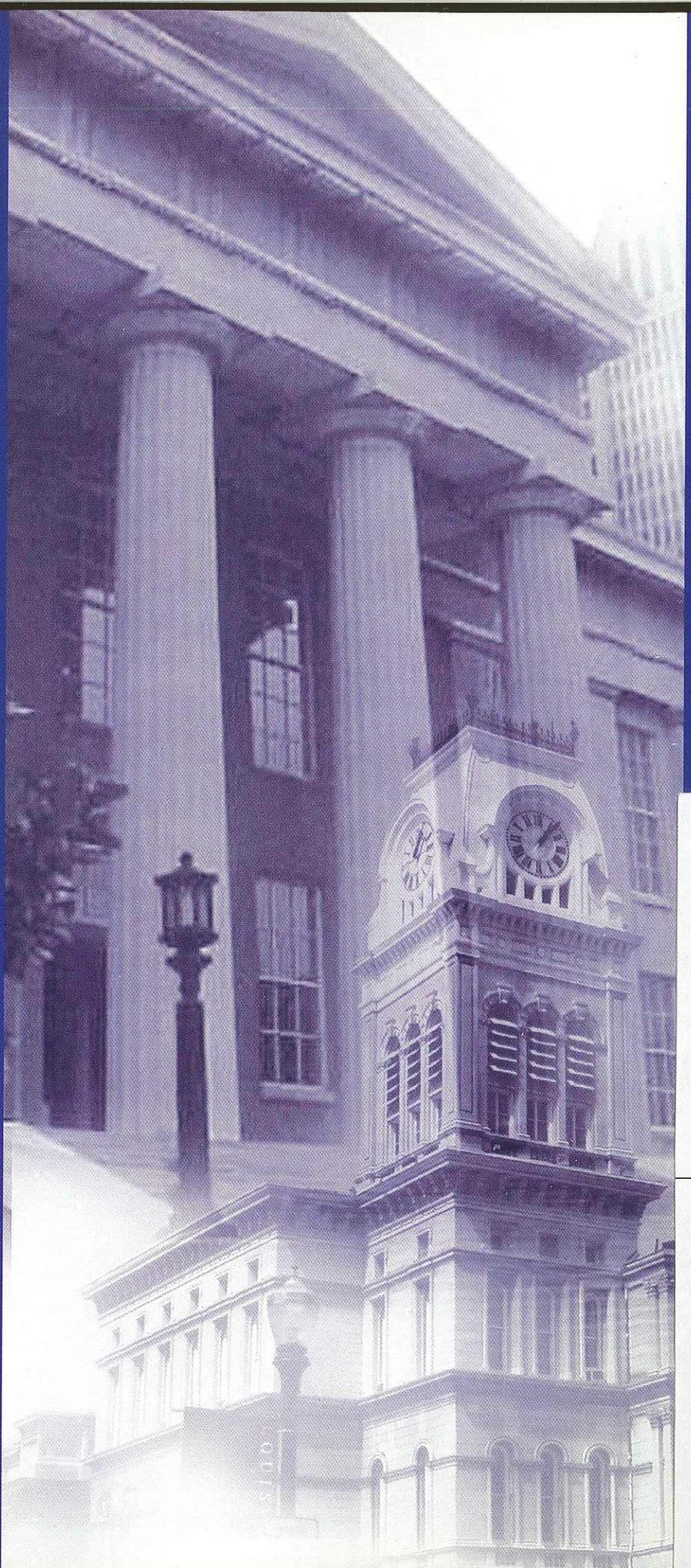




Jerry E. Abramson
Mayor

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 Council

Financial Operations

Audit Report

Office of Internal Audit

Louisville Metro Council

Financial Operations

December 2010



Louisville Metro Council

Financial Operations

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OFFICE OF INTERNAL AUDIT
LOUISVILLE, KENTUCKY

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THOMAS L. OWEN
PRESIDENT METRO COUNCIL

Transmittal Letter

December 3, 2010

The Honorable Thomas L. Owen
President of Louisville Metro Council
City Hall
Louisville, KY 40202

Subject: Audit of the Louisville Metro Council's Financial Operations

Introduction

An audit of the Louisville Metro Council's financial operations was performed. The primary focus of the review was the operational and fiscal administration of the procurement and payroll activity. This included how activity is processed, recorded, and monitored. The objective was to obtain assurance that risks are adequately mitigated through the internal control structure.

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 procedures for the administration of the Metro Council's procurement and payroll activity were reviewed through interviews with key personnel. The focus of the review was the operational and fiscal administration of the activity. Tests of sample data were performed on procurement and payroll activity from fiscal year 2010 (July 2009 through June 2010). The review included assessing whether activity was processed, recorded, monitored, and reported accurately and appropriately. The Neighborhood Development Funds, Capital Improvement Funds and out of town travel expenditures were not included in the procurement activity review. 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 a selective review of data.

Opinion

It is our opinion that the internal control structure for the administration of the Metro Council's procurement activity needs improvement; and the internal control structure for the administration of payroll activity needs improvement. The internal control ratings are on page 5 of this report. These ratings quantify our opinion on internal controls, and identify areas requiring corrective action. Opportunities to strengthen the internal control structure were noted.

- **Procurement.** Examples of the issues impairing the effectiveness of the internal control structure for the administration of the Metro Council's procurement activity include the following.
 - The public purpose for goods / services procured was insufficiently documented.
 - Supplier payments were not processed within 30 days as required by State law.
 - District operating financial center funds were used for activities not directly related to day-to-day operations, such as Neighborhood Development projects.
 - The Public Relations financial account was used for activity not related to public relations or meetings, such as food for a staff party, landscaping services, and postage stamps.
 - Monitoring and reconciliation of activity was not performed on a timely basis.
- **Payroll.** Examples of the issues impairing the effectiveness of the internal control structure for the administration of the Metro Council's payroll activity include the following.
 - Prior period adjustments were not adequately documented, which impacted the accuracy and integrity of payroll activity.

- Timecard reports were not signed and prior approval for time accrual and usage was not documented.
- Individuals that were no longer employed by the Metro Council were not removed from active status in the Human Resources system in a timely manner.
- Monitoring and reconciliation of payroll activity was not performed.

The implementation of the recommendations in this report will help improve the internal control structure and effectiveness of the administration of the Metro Council's procurement and payroll activity.

Corrective Action Plan

The Metro Council Business Office was asked to provide a response / corrective action. The Business Office's responses / corrective action plans are included in this report in the Observations and Recommendations section. It is important to note that while the Business Office Representatives are in agreement with the recommendations, action from the Metro Council may be required in order to implement appropriate corrective actions. This is primarily in the area of updating policies and procedures. Therefore, the Metro Council President was also asked to respond. The President indicated that the results will be assigned to the Government Accountability and Oversight Committee for review and update of Council policies and procedures. The Office of Internal Audit will continue to work with the Metro Council to ensure the actions taken are effective to address the issues noted.

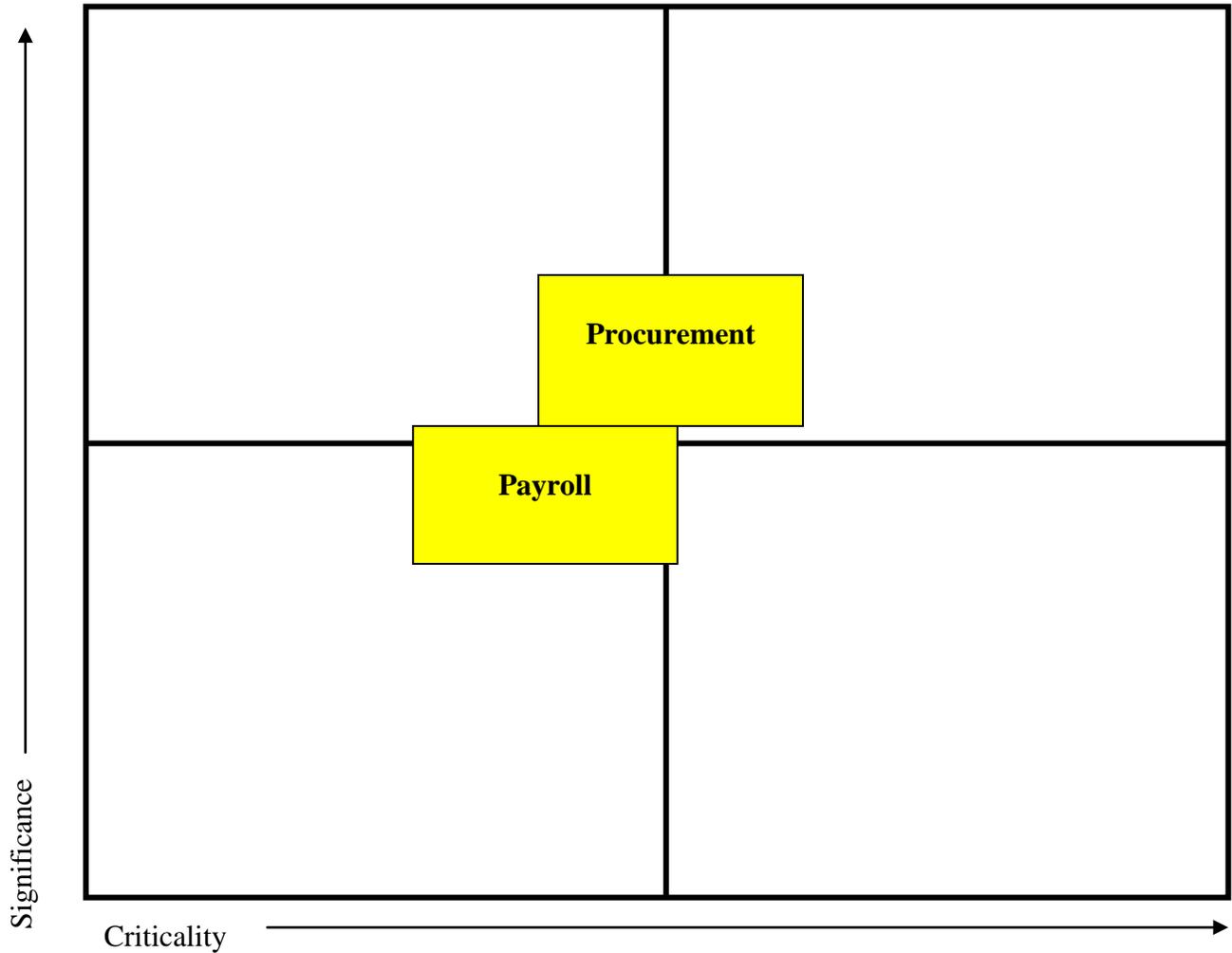
Sincerely,



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

cc: Louisville Metro Council Government Accountability and Oversight Committee
Louisville Metro Council
Louisville Metro External Auditors

Internal Control Rating



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

Background

The Louisville Metro Council is the legislative body for Louisville Metro Government. The 26 members of the Metro Council are elected by district to serve a four year staggered term. The Metro Council enacts legislation, approves budgets, and acts as a liaison for their respective districts. The annual operating appropriation for the Metro Council is divided among 26 operating financial centers (one for each district), and an administrative operating financial center.

For fiscal year 2010, the Metro Council's payroll related expenditures were approximately \$4,795,000 and supplier payments were approximately \$551,000. The supplier amount excludes payments from the Neighborhood Development Funds and Capital Improvement Funds. The Metro Council had approximately 117 positions during fiscal year 2010. This included elected officials, and full and part time employees.

This audit was scheduled at the request of the Metro Council President.

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 previous reviews of the Louisville Metro Council's financial operations.

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

A draft report was issued to the Metro Council on October 18, 2010. An exit conference was held with the Metro Council Business Office on November 2, 2010. Attending were Tracy Gaines and Edwin Ernest representing the Metro Council; Michael Norman, Ingram Quick and Brittany Schaefer representing Internal Audit. Final audit results were discussed.

The Metro Council Business Office was asked to provide a response / corrective action plan. The views of the Metro Council Business Office were received on November 8, 2010 and are included in the Observations and Recommendations section of the report. The plans indicate an agreement with the need to address the issues noted.

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.”*

The Metro Council Business Office’s response was provided within this required timeframe.

It is important to note that while the Business Office Representatives are in agreement with the recommendations, action from the Metro Council may be needed in order to implement appropriate corrective actions. This is primarily in the area of updating policies and procedures. Therefore, the Metro Council President was asked to provide a response. The Metro Council President and the Chief Audit Executive met on November 19, 2010 to discuss the audit results. The Metro Council President’s response was received on December 2, 2010 and is included in the Observations and Recommendations section of the report.

Observations and Recommendations

1) Procurement

Scope

The Louisville Metro Council's procedures for administering procurement activity were reviewed through interviews with key personnel. The primary focus of the review was the operational and fiscal administration of the activity. This included assessing whether activity was processed, recorded, monitored, and reported accurately and appropriately. The objective was to obtain assurance that the risks are adequately mitigated through the internal control structure.

Tests of sample data were performed on transactions from fiscal year 2010 (July 2009 through June 2010). Procurement data was obtained from Louisville Metro's financial system. The sample consisted of eighty-five transactions. This was comprised of three transactions judgmentally selected from each of the 26 district operating financial centers and seven transactions from the administrative office operating financial center. Transactions related to out of town travel, Neighborhood Development Funds, and Capital Infrastructure Funds were excluded from this review.

In addition, all suppliers receiving more than \$10,000 from the Metro Council during fiscal year 2010 were identified. Activity for these suppliers was reviewed to ensure it was in compliance with contractual requirements in the Louisville Metro procurement policies. The review would not reveal all issues because it was based on selective review of data.

Observations

Issues were noted with the administration of the Metro Council's procurement activity. As a result, the effectiveness of the internal control structure is impaired and needs improvement. Opportunities noted to strengthen the controls are as follows.

1a) Public Purpose

1b) Compliance

1c) Processing

1d) General Administration

Details of these begin on the following page.

1a) Public Purpose

Louisville Metro Government's expenditures should be for a public purpose, i.e., for the good of the citizens the government serves. The foundation for this principle is in the Kentucky Constitution, Section §171. Since some expenditure activity may appear to benefit individuals or groups more than the general public, it is important that the public purpose is clearly defined and documented. The Metro Council uses an internal purchase approval form to document the public purpose of expenditure activity. There were issues noted involving the documentation of public purpose for the activity reviewed.

- **Insufficient Documentation.** Fifteen of the eighty-five transactions reviewed did not have sufficient documentation for the public purpose of the goods / services procured. The information noted on the internal purchase approval form did not fully explain the public purpose of the activity. Examples of the goods / services procured include the following.

- Food and refreshments
- Shirts
- Postage
- Insurance
- Membership dues
- Nursing services
- Mediation services
- Decorations

The value of these fifteen cases was approximately \$9,800.

- **Events.** Ten cases were noted in which the public purpose for attending an event was not sufficiently documented. This involved transactions in which several tickets were purchased for an event. The information noted on the purchase approval form, or included with the payment documentation, did not fully document who was receiving the tickets for the event, why they were receiving the tickets, or how attending the event served a public purpose.

- The value of these ten cases was approximately \$7,550.

- **Giveaway Items.** Six cases were noted in which the public purpose for advertisements on giveaway items (e.g., tote bags, tee shirts) was not sufficiently documented. It appears these items were intended for giveaway at community events. The public purpose was not clearly documented and visual examples of the advertisements and items were not included.

- The value of these six cases was approximately \$6,145.

- **Web Hosting.** Two cases were noted in which the public purpose for web hosting services was not sufficiently documented. It appears the web site is for the Council member to communicate with their respective district's constituents. It was not clear

why this service was used in addition to, or instead of, the website provided by Louisville Metro Government.

- The value of these two cases was approximately \$95.
- **Missing Forms.** Two cases were noted in which the internal purchase approval form was not included in the payment documentation for the expenditure. Therefore, there was no documentation of the public purpose.
 - It appears the public purpose for one transaction could be determined based on the services provided, i.e., captioning services for Metro Council meetings. The value of this case was \$1,785.
 - The public purpose for the other transaction could not be determined since it was for entertainment during community events. The value of this case was \$4,205.

Recommendations

Appropriate Metro Council personnel should take corrective actions to address the issues noted. Specifics include the following.

- ✓ The Metro Council's policies should be revised to include guidance on public purpose. The policies should address appropriate uses of public funds, as well as necessary documentation required for activities (e.g., distribution of items).
- ✓ The public purpose of all expenditures should be sufficiently documented. Sufficient documentation should be provided to allow a reasonable person to determine the public purpose of expenditures solely by reviewing the supporting documentation. If the payment documentation and invoice do not clearly provide this level of detail, additional explanation should be provided.
- ✓ If there is any doubt to the public purpose of a proposed expenditure, a legal opinion should be obtained from the Jefferson County Attorney prior to ordering the goods / services. The legal opinion stating there is a legitimate public purpose to the proposed goods / services should be included with the payment documentation.
- ✓ Expenditures for event tickets should include documentation identifying the recipients of the tickets, the reason public funds were used to provide the tickets to the recipients, and how attendance serves a public purpose.
- ✓ The public purpose of advertisements on giveaway items should have prior approval from the Jefferson County Attorney. This would be similar to the current Metro Council requirement involving mailings of more than 200 items.
- ✓ The public purpose of external web site hosting services should be approved by the Jefferson County Attorney.
- ✓ The public purpose of entertainment during community events should include information regarding the event, such as who was invited, why public funds were used, and how the entertainment serves a public purpose.

Metro Council Business Office Response / Corrective Action Plan

- **Insufficient Documentation** - The Council has been using the Purchase Approval Form that Internal Audit suggested after both governments merged. We have since learned that OMB does not acknowledge it and there is a new form with similar requested information when refreshments are being purchased. To gather sufficient documentation we may have to revise our form and be specific in requesting the information we need.
- **Events** - In a recent training held by Office of Management and Budget and the County Attorney Office it is clear that there is some confusion as to how to handle events that are being sponsored by a Council office or if the Council office is a co-sponsor. Tickets to an event are another gray area. We no longer have a limit on tickets and if a Council office is purchasing a table or tables they're asked to have those paid from their NDF. That process can take up to 2 weeks and therefore, Council offices would rather attach a memo to acknowledge and request that they be processed from their Operating Budget. In some cases, some Council offices will provide a detail list of attendees or list the name of the group (e.g., xxxClean up Crew, Block Watch leaders, etc.).
- **Giveaway Items** - The giveaway items noted in the audit are for events held in a Council district and in some cases that would include Kroger Gift cards which we aren't comfortable with.
- **Web Hosting** - The Business Office questioned these services when they were first introduced to us and with no policy or a Metro Council website at the time we proceeded. The two cases noted in the audit will terminate at the end of the calendar year. We should consider including a policy to address as we have some Council members with sites connected to the Council's page.
- **Missing Forms** - The items referenced in this section are purchase approval forms (PAF) from the Council Administrative Budget. The Captioning services normally have the PAF attached, but there is a separate form for our CMP requests. Both of these are Professional Services Contracts.

1b) Compliance

Compliance issues were noted. This involved compliance with statutory requirements as well as Louisville Metro policies. Examples include the following.

- **Payment Timeliness.** Kentucky Revised Statutes require that Louisville Metro government pay suppliers within 30 days of receipt of the invoice. Of the 85 invoices reviewed, 26 were not paid within the 30 day limit. The payments for the twenty-six invoices ranged from 31 to 174 days.
 - The Metro Council's policies do not require date stamping of invoices when received. The absence of a date stamp makes it impossible to determine the actual date the invoice was received, so the timeliness of payment cannot be determined with certainty. For invoices without date stamps, the invoice date has to be used to calculate timeliness. This may distort the payment time calculation.
- **Supplier's Revenue Commission Status.** Louisville Metro suppliers are required to register with the Louisville Metro Revenue Commission and be in good standing. This helps ensure that suppliers doing business with Louisville Metro Government are paying applicable taxes and fees. Five of the Metro Council suppliers were not in good standing with the Revenue Commission. This indicates the supplier had not filed appropriate forms, or made payments, with the Revenue Commission as required.
- **Contractual Agreements.** Louisville Metro's procurement policies, which are based on State statutes, require the use of contractual agreements whenever a supplier receives more than \$10,000 during the fiscal year. There were thirteen suppliers identified that received more than \$10,000 from the Metro Council during fiscal year 2010. Of these, the activity for one supplier was processed without any type of contractual agreement. The Metro Council paid the supplier approximately \$13,480 during fiscal year 2010. This involved 192 invoices.
- **Use of Existing Contractual Agreements.** There were two cases in which cellular telephones were purchased outside of the existing contractual agreements with the supplier. Not using the contract could result in Louisville Metro paying more for the telephones than the contractual rate, and could violate other terms of the contract.
 - One of these involved a reimbursement to the employee for using their personal funds to purchase the cellular telephone. Louisville Metro policy allows reimbursement for the cost of business calls made on personal cellular telephones, but does not allow for reimbursement for the cost of personal cellular telephones.
- **Rental of Office Space.** There was one case in which the expenditure was for rental of office space. This was done to provide a satellite office within the Council District. It does not appear a formal lease agreement was executed for this space. A formal agreement would address issues such as responsibilities and rights of the parties involved. It would also allow for review / approval by appropriate Louisville Metro entities (e.g., Risk Management, Jefferson County Attorney) prior to the execution of the agreement.

Recommendations

Appropriate Metro Council personnel should take corrective actions to address the issues noted. Specifics include the following.

- ✓ Care should be taken to ensure invoices are processed in a timely manner in compliance with State law. Any situations in which an invoice will not be paid within 30 days, such as disputes with the supplier, should be properly documented. Additional training of key personnel may be necessary in order to ensure compliance with statutory requirements.
- ✓ The Metro Council should consider date stamping all invoices when received. This would allow determination of timeliness and identify areas where delays may be occurring. It may be beneficial to have all invoices come into one central location (e.g., Business Office) for date stamping and tracking. The invoices could then be distributed to the applicable Council District offices for review and approval.
- ✓ The Metro Council Business Office should request access to the Revenue Commission's internet-based site that allows verification of potential suppliers. The registration status and standing of suppliers should be verified prior to the procurement of goods / services. The verification should be documented.
- ✓ The Metro Council should comply with contractual threshold limits as stated in Louisville Metro's procurement policies. The Metro Council's procedures may need to be revised to ensure cumulative payment amounts are considered prior to procurement of goods / services. This would require the Council District offices to consult the Business Office prior to initiating procurement of goods / services from suppliers. This proactive approach would help ensure the activity is in compliance with contractual requirements. Additional training of personnel within the Council District offices should also help ensure compliance with policy requirements.
- ✓ Existing contractual agreements should be used for the procurement of goods / services. This requires review of contractual agreements prior to the procurement of goods / services to determine if agreements are available. The Metro Council policies may need to be revised to ensure the Business Office is consulted to help identify existing contractual agreements prior to the Council District offices initiating procurement of goods / services.
- ✓ Formal lease agreements should be used for the rental of office space. The lease agreements should be reviewed by appropriate Louisville Metro entities, such as the Jefferson County Attorney and Risk Management division of the Office of Management and Budget, prior to the execution of the agreement.

Metro Council Business Office Response / Corrective Action Plan

- **Payment Timeliness** - Unfortunately we don't have any control in this area as the invoices are received by the Council office. The Business Office, however, clocks in items upon receipt and if we're contacted by a vendor of an outstanding invoice (that we're not aware of), we contact the office and have a copy faxed to us.
- **Supplier's Revenue Commission Status** - This policy actually started in the middle of the fiscal year, but certainly have increased notification to Council offices.

Suppliers should be aware of their responsibilities and not allow themselves to be put in an awkward and financial debt situation.

- **Contractual Agreements** - This is another concern that we are aware of and asked if the Business Managers can be informed by OMB or Purchasing if a vendor has reached their \$10,000 limit, especially since it affects Metro Government as a whole. As an agency that has 26 buyers, the Business Office is not always informed of business being done with vendors and therefore we have to take the necessary steps to figure out how we're going to pay the vendor.
- **Use of Existing Contractual Agreements** - The Business Office has always encouraged Metro employees to utilize contracts for most services and goods. Cell phones have been an ongoing issue as we have some employees on contract, we have some that may use the same vendor, but not on contract, and then there are those that use their personal phones and choose to be reimbursed. There are still concerns about the reimbursement rate for the various plans and vendors.
- **Rental of Office Space** - This is in reference to a satellite office, but we've also had comments regarding the rental of places to meet (churches, schools and/or other businesses). For those organizations that request/require a lease agreement we are to work with Public Works or CAO for review and signature. As employees we cannot and should not enter into agreements as we don't have signature authority.

1c) Processing

Processing issues were noted with some of the Metro Council's procurement activity reviewed. Examples include the following.

- **Use of Operating Center Funds.** Funds are appropriated to each Metro Council District for operating costs. The funds are budgeted in the respective operating financial centers, and are intended for use in day-to-day operations of the Council Districts. There were instances noted in which it appears the operating center funds were not used appropriately. Examples include the following.
 - *Neighborhood Development Fund Projects.* There were two cases in which expenses associated with cleanup and landscaping projects were paid with operating center funds. Documentation with the payments noted that the Council District was not able to process the invoices through Neighborhood Development Funds so the operating center was used.
 - *Professional Organization.* There was one case in which membership dues to a professional organization were paid with operating center funds. Metro Council policies allow the use of operating center funds “for and generally associated with maintaining the good will of the government with a community association or civic organization”. It does not appear that membership in this professional organization was for the good will of the government, and membership does not appear to be required for the individual's official position with the Metro Council. The membership appears to benefit the individual personally.
 - *Food for Dismas Workers.* There was one case in which food was purchased for Dismas workers who assisted in the Council District's flood cleanup project. This does not appear to be associated with the day-to-day operations of the Council District office. In addition, providing food to Dismas workers may be a violation of Dismas guidelines and requirements.
- **Public Relations Account.** Account codes are used to classify expenditure activity in the financial system. These codes are used for budgetary and management purposes, such as providing information on the costs for operating the Metro Council. According to the Metro Council policies, the Public Relations financial account is for all costs of having a public meeting, such as meeting room rental, refreshments, and costs of promotion of goodwill. There were several cases in which the Public Relations financial account code was used even though it was not descriptive of the activity. Examples include food purchased for a staff holiday party; landscaping services; postage stamps; dumpster rental; and insurance coverage.
- **Data Charge.** There was one case in which a reimbursement for business activity on the employee's personal cellular telephone included the total data charge for the device. The appropriateness of reimbursing the entire data charge cannot be determined since it does not list detail of personal or business usage. The total data charge was approximately \$45.
- **Sales Tax.** There was one case in which the supplier's invoice included Kentucky State sales tax. The sales tax was paid even though Louisville Metro Government is tax exempt. The amount of the sales tax was approximately \$24.

Recommendations

Appropriate Metro Council personnel should take corrective actions to address the issues noted. Specifics include the following.

- ✓ The operating financial center funds should only be used for the day-to-day operations of the Council district. The operating center funds should not be used for projects normally funded through the Neighborhood Development Funds or Capital Infrastructure Funds process. The Jefferson County Attorney should be consulted whenever there is any question as to the appropriateness of using the operating financial center funds.
- ✓ Care should be taken to ensure that invoices are coded to the financial accounts most descriptive of the goods / services received. The Public Relations financial account should only be used for costs associated with a public meeting.
- ✓ The Metro Council policies may need to be revised to include other financial accounts that are used in the day-to-day operations of the Council District offices.
- ✓ The appropriateness of reimbursing the entire data charge for personal cellular telephone devices should be determined. It may be necessary to prorate these charges to account for potential personal use.
- ✓ Appropriate Metro Council personnel should ensure invoices do not include sales taxes that Louisville Metro is exempt from paying. In cases where an invoice includes sales tax, an adjustment should be made deducting the applicable amount.

Metro Council Business Office Response / Corrective Action Plan

- **Use of Operating Center Funds** - The Operating Budget continues to be the quick stop for processing items due to the minimum requirements to process an invoice. There's also concern for items being past due or vendors not in compliance. There have been policies created for Dismas workers, specifically by Human Resources (HR), and the Council offices have even been invited to attend one of Metro's regular HR meetings.
- **Public Relations Account** - We are totally in agreement that this budget account is heavily used and misused.

1d) General Administration

Issues were noted with the general administration of the Metro Council's procurement activity. Examples include the following.

- **Monitoring and Reconciliation.** The Metro Council Business Office generates financial activity reports for each of the Council District operating financial centers. These monthly reports are distributed to the applicable Council District offices for monitoring and reconciliation. This monitoring and reconciliation is not documented.
 - The Administrative financial center is reconciled quarterly by the Business Office. Not reconciling this center on a monthly basis increases the risk that inaccuracies and misstatements may go undetected.
- **Do Not Mail Activity.** It appears the Metro Council does not document the reason when supplier checks are not mailed directly from the Office of Management and Budget. There were eight transactions in which there was a "Do Not Mail" stamp on the payment document but there was no supporting documentation indicating why this needed to be processed as a do not mail check. Reasons for not mailing checks include situations in which additional documentation, such as registration forms, needs to be included with the check. Having supplier checks mailed directly from one central location, such as the Office of Management and Budget, is a fundamental internal control.

Recommendations

Appropriate Metro Council personnel should take corrective actions to address the issues noted. Specifics include the following.

- ✓ A formal, documented reconciliation process should be implemented for all financial centers. The detailed monthly financial reports should be compared to some type of source documentation (e.g., payment document). This helps ensure the transactions were processed as intended and posted to the proper financial centers. This also helps strengthen the reliability of the financial statements. The reconciliation should be documented and errors properly addressed.
- ✓ A major component of any reporting system is proper reconciliation and monitoring. It is imperative that financial information is reviewed on a regular basis. This includes reviewing individual transactions for appropriateness, completeness and adherence to requirements. In order to promote proper segregation of duties, an individual independent of the actual processing of activity should perform the monitoring of activity, and at least review the monthly reconciliations.
- ✓ Supplier checks should be mailed directly to the suppliers by the Office of Management and Budget. In situations in which the Metro Council needs to mail the check, the reason should be documented with the payment document.

Metro Council Business Office Response / Corrective Action Plan

- **Monitoring and Reconciliation** - Operating Budget reports are distributed after the closing of each month to the various Council offices. On a quarterly basis they will receive a journal detail report to review expenditures or corrections as well as adjustments. Depending on the time of year or coverage the Business Office may not always be able to do it in a timely fashion. We've been operating without 1 full-time position as well as a part-time position for almost 2 ½ years.
- **Do Not Mail Activity** - OMB will not mail attachments out for us and therefore we request Do not mail's for our newspaper accounts as that vendor has requested that we do that, so the check is credited to the account. We also pick up some NDF checks as our Clerk's office has letters and other documentation to be sent to the non-profit organization.

2) Payroll

Scope

The Louisville Metro Council's procedures for administering payroll were reviewed through interviews with key personnel. The primary focus of the review was the operational and fiscal administration of the activity. This included assessing whether activity was processed, recorded, monitored and reported accurately and appropriately. The objective was to obtain assurance that the risks are adequately mitigated through the internal control structure.

Tests of sample data were performed on transactions from fiscal year 2010 (July 2009 through June 2010). Payroll data was obtained from Louisville Metro's PeopleSoft system. The data was for two different pay periods and included all Metro Council employees paid for the periods. A total of 178 payroll transactions were reviewed for the pay periods ending March 6, 2010 and April 17, 2010.

The payroll activity was compared to supporting documentation, such as timecard reports and leave requests, to verify the activity was processed completely and accurately. Compliance with Louisville Metro policies was reviewed. This included verification of employee and supervisor signatures on the timecard reports, the use of direct deposit, and approval for overtime / compensatory time earned. In addition, employee addresses were compared to Metro Council supplier addresses, and any matches were reviewed. The review would not reveal all issues because it was based on selective review of data.

Observations

Issues were noted with the administration of the Metro Council's payroll activity. As a result, the effectiveness of the internal control structure is impaired and needs improvement. Opportunities noted to strengthen the controls are as follows.

2a) Prior Period Adjustments

2b) Policy Compliance

2c) General Administration

Details of these begin on the following page.

2a) Prior Period Adjustments

The lack of adequate documentation for adjustments to prior payroll periods impaired the effectiveness of the internal controls for the Metro Council's payroll activity. The Louisville Metro PeopleSoft system is used for processing payroll. Using the self-service function of the PeopleSoft system, Metro Council employees enter their time directly into the system. At the end of the pay period, a timecard report is prepared that lists the employee's activity (e.g., daily time in and out, total hours to be paid). The timecard report is signed by both the employee and their supervisor, and serves as the official document of time worked.

The self service functionality also allows employees to make changes to their time for payroll periods other than the current one. These are considered prior period adjustments. Authorization is required before these adjustments are processed. These adjustments can impact the accuracy of the timecard reports if new reports are not run after adjustments are made (or if documentation for the adjustments is not maintained).

- **Insufficient Documentation.** There were five cases in which the employee's pay data (e.g., number and type of hours) did not agree to the timecard reports. These were all due to prior period adjustments. Documentation of the prior period adjustments were not included with the timecard reports. This made it appear the timecard report, which is the official payroll record, was incorrect.

- **Non-Reporting of Time Worked.** The Metro Council Business Office enters leave time (e.g., vacation) for any employees that do not enter their actual work time by the processing cutoff deadline. This is done so that the employee receives a paycheck. The employee then has to do a prior period adjustment to correct the time reported (i.e., entering time worked to replace vacation). This practice may be resulting in additional prior period adjustment activity for the Metro Council. While the reason for this practice is understandable, the practice may be causing more issues than the benefit it provides.

- **Weekly Standard Hours.** The prior period adjustment activity is impairing the effectiveness of the weekly standard hours control within the PeopleSoft system. All Louisville Metro employees have weekly standard hours established in the PeopleSoft system. For example, a regular full-time employee has 40 standard hours each week. The standard hours are an important control to help ensure employees are paid accurately, i.e., an employee should not receive more than 40 hours of pay each week unless overtime is earned. However, regardless of the pay period the prior period adjustments are for, the activity is processed for the current pay period. As a result, an employee can receive more than their standard hours of pay without receiving overtime pay.
 - It does not appear that the PeopleSoft system has an exception report for changes made to prior periods where an employee exceeds their standard hours.
 - It should be noted that this issue impacts all Louisville Metro Government departments that use the self-service functionality of the PeopleSoft system. Therefore, this will be addressed to appropriate Louisville Metro departments (e.g., Human Resources, Office of Management and Budget, and Information Technology) for resolution.

Recommendations

Appropriate Metro Council personnel should take corrective actions to address the issues noted. Specifics include the following.

- ✓ The importance of accurately recording time in the PeopleSoft system should be stressed to all employees. Metro Council employees are responsible for accurately recording time worked and should be held accountable for doing so. Whenever a prior period adjustment is necessary, the Business Office should be informed.
- ✓ Business Office personnel should monitor prior period payroll adjustments made by employees. This should include verifying the adjustment is appropriate, and the proper earn codes and hours are adjusted. Approval should not be given without this level of review.
- ✓ Prior period payroll adjustments should be properly documented. The documentation is needed so that any discrepancy between the timecard report and the actual pay is explained and justified. The Office of Management and Budget issued a directive in August 2010 requiring the generation of a new timecard report for any employee with a prior period adjustment. The timecard report with adjustments should be distributed for proper signature and maintained with the timecard reports for the effective period.
- ✓ The Business Office's practice of entering leave time for the employees that did not enter their time worked before the payroll deadline should be evaluated. The resulting adjustments may be causing more issues with the Metro Council's payroll activity than can be justified.
- ✓ The impact of the prior period adjustments on the effectiveness of the controls will be directed to the appropriate Louisville Metro departments (e.g., Human Resources, Office of Management and Budget, Information Technology) for resolution. This issue may be addressed by restricting the ability to process prior period adjustments to key individuals within Louisville Metro departments.

Metro Council Business Office Response / Corrective Action Plan

- **Insufficient Documentation** - The Business Office is made aware of prior period adjustments only when payroll is being processed (usually every other Monday). Whenever prior period adjustments are processed, a new timecard is printed and sent to the employee to sign. The new timesheet is placed in the appropriate file. There is not a policy in place that will make it mandatory that the employee notify the Business Office of the adjustment nor is there a control feature in People Soft that can automatically notify us of adjustments as there are made.
- **Non-Reporting of Time Worked** - The practice of using employee's leave time in lieu of no pay was something that had been recommended by the Payroll Department. It was the intent that the deduction of this time would prompt the employee to be more diligent in putting in their time. Also, if time is not put in, a manual check will be done on the actual payday that requires additional hardships on others. It should be noted that before leave time is used there are several attempts made to contact the employee notifying them of the missing information and the deadline for payroll submission. We are working to move away from this practice and to allow employees to be compensated for the hours that they key in. Employees are made aware of this.

2b) Policy Compliance

Compliance issues were noted. This involved compliance with Louisville Metro policies. Examples include the following.

- **Timecard Report Signatures.** Louisville Metro policy requires that the timecard reports be signed by both the employee and their supervisor. The employee's signature indicates the time is reported accurately, and the supervisor's signature indicates authorization to process the employee's payroll. The timecard report is the official record of the payroll activity. Issues were noted with the timecard signatures.
 - There were eight individual timecard reports that were not signed by the employee.
 - There were forty-four individual timecard reports for elected officials that were not signed. Louisville Metro policy does not address signature requirements for elected officials, and the Office of Internal Audit was unable to obtain a policy clarification during the review. It is important to note that the elected officials are paid a salary for serving in the position, not for time worked, so individual timecard reports may not even be necessary.
 - There were fourteen timecard reports that were not signed by the supervisor.
 - The timecard reports are prepared in the Metro Council Business Office and distributed to the applicable Council District offices for review and signatures. The timecard reports are supposed to be returned to the Business Office. The Business Office uses the unsigned electronic copy as the official record for the pay period if the timecard reports with signatures are not returned. These are maintained electronically, nothing is filed with the other timecard reports. This practice does not provide sufficient documentation for the payroll activity.

- **Prior Approval for Time Earned / Leave Time Used.** Louisville Metro policies require prior approval for the earning of overtime / compensatory time and the usage of leave time. While the policies do not require standardized documentation for approvals, it is needed in order to demonstrate prior approval was obtained in compliance with policies.
 - There were forty-six cases in which an employee earned compensatory time or overtime but documented prior approval was not available. The reason for earning the time was not noted on the timecard report.
 - There were twenty cases in which an employee used one full day or more of leave time (e.g., vacation, sick) but documented prior approval was not available. Time used less than one day was excluded since it is reasonable to expect that less than one day would not be planned in advance.

Recommendations

Appropriate Metro Council personnel should take corrective actions to address the issues noted. Specifics include the following.

- ✓ The importance of adhering to Louisville Metro policies should be stressed to all Metro Council employees. Additional training of personnel may be necessary in order to ensure compliance.

- ✓ Timecard reports should be signed by both the employee and the supervisor. Once approved, the timecard report should be returned to the Business Office in a timely manner (e.g., within one week). Supervisors should be accountable for reviewing and signing the timecard reports, and ensuring they are returned to the Business Office in a timely manner.
- ✓ The necessity of elected officials signing their individual timecard report should be determined. The assistance of the Jefferson County Attorney may be needed in order to ensure the practice is in compliance with applicable laws and regulations.
- ✓ Prior approval should be obtained from the supervisor for overtime / compensatory time earned. The reason for overtime / compensatory time should be documented for each occurrence on the timecard report. This provides documentation for the reason and necessity of earning the time. The purpose of the compensatory / overtime should be reviewed and approved by the supervisor during the review of the individual timecard reports.
- ✓ Request for use of leave time should be approved in advance and documented. This should apply for, at a minimum, any use of one full day or more. This helps to ensure that proper coverage is available for the absent employee.

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- **Timecard Report Signatures.** There are instances when an employee is no longer an employee of the agency and has left the department prior to signing their final timesheets. The Minority Caucus has given authority to the Caucus Director to sign the timesheets of the Republican staff in their absence. Councilmember's are not required to input time or sign the timecards for the hours reported for the pay period. Timecards are sent with a cover sheet attached that specifies the expected date of return. Timesheets are clocked in as they are returned back to the Business Office and filed away. It is documented on the cover sheet that the Business Office copy will be used if the original is not returned.
- **Prior Approval for Time Earned/ Leave Time Used.** Each Council office is overseen by the Council representative and the employees within that office work at the pleasure of the Council member. Compensatory hours earned are done so with the full understanding and approval of the supervisor. Employees are also encouraged to input any comments reflecting hours work outside of a standard work day (8am-6pm), however the time reporting system does not include those comments when the timecards are printed off for signatures. Leave request forms are used by the Metro Council Administrative staff and Clerk's Office only. All other employees schedule time off in conjunction with their Council member and this is done independently of the Business Office. Therefore, they are not required to submit a leave request.

2c) General Administration

Issues were noted with the general administration of the Metro Council's payroll activity. Examples include the following.

- **Monitoring and Reconciliation.** The Metro Council Business Office does not perform monitoring and reconciliation of the payroll activity to ensure it is recorded accurately in the financial system. Payroll expense data is generated in the PeopleSoft system and automatically recorded in the financial system. The PeopleSoft expense reports produced each pay period are not used for monitoring and reconciling activity.
- **Employee Statuses.** There were four employees identified that received no pay for the pay periods examined because they did not report any hours worked. It was determined that none of these employees were still working for Louisville Metro Government, but their status in the PeopleSoft system had not been updated to reflect this change. Maintaining departed employees as active distorts the information regarding Metro Council operations and can increase the risk of inappropriate payments (e.g., ghost employees).
- **Supplier Relationships.** Metro Council employees with a home address that was also the business address for any Louisville Metro suppliers were identified. Further review was done in order to determine if the supplier activity was legitimate.
 - There was one case in which a Metro Council supplier was a relative of a Metro Council employee. During fiscal year 2010, approximately \$3,900 was paid to the supplier from the Metro Council. It does not appear that the Metro Council employee had direct responsibility or authorization for these payments, (i.e., the employee did not authorize the payments). However, the employee may have been associated with the Council District offices that used the supplier at the time of the transaction. There was no documentation addressing this potential conflict of interest.
- **Standard Hours.** All Louisville Metro employees have weekly standard work hours established for their position. These standard hours are a control within the PeopleSoft system to help ensure accuracy of payroll activity.
 - There were five cases where an employee did not work their standard hours for the pay period. Personal, vacation, or compensatory time were not used to make up for the remainder of the hours, so the employee received less pay than the standard hours. Documentation indicating why the hours were not worked was not available.
 - There were two cases where an employee worked more than their standard hours but the time was not recorded as overtime or compensatory time earned. Both of these involved permanent part time employees with 25 standard hours per week. The time exceeding their standard hours should have been charged to straight overtime or compensatory time earned.

Recommendations

Appropriate Metro Council personnel should take corrective actions to address the issues noted. Specifics include the following.

- ✓ A formal, documented payroll reconciliation process should be implemented. This should include the review of information contained on the PeopleSoft reports and verification of accurate postings to the financial system. Exceptions should be investigated and properly documented. In order to promote proper segregation of duties, an individual independent of the actual processing of activity should at least review the reconciliations.
- ✓ The Metro Council should have a policy to ensure the timely notification of the Business Office whenever someone leaves employment with the Metro Council. Also, the Business Office should review payroll activity to identify employees not reporting any hours worked for a pay period. Follow-up can be performed to determine if the individual has left employment with the Metro Council.
- ✓ The Business Office should ensure that the statuses of employees who are no longer employed with the Metro Council are properly updated in the PeopleSoft system in a timely manner.
- ✓ Metro Council employees with relationships with potential suppliers should comply with Louisville Metro policies regarding supplier relationships and conflicts of interest.
- ✓ Appropriate personnel should review the activity with the supplier identified to determine if a conflict of interest exists. The assistance of the Jefferson County Attorney may be needed. The results should be properly documented.
- ✓ Metro Council employees should record their time in accordance with policy, including accurately reporting time in relation to their standard work hours.

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- **Monitoring and Reconciliation** - Payroll reconciliation is performed by the Business Manager on a quarterly basis to verify payroll expenses are being recorded to the appropriate accounts. Also, the Business Office performs reconciliation of staff assistant expenses on a bi-weekly basis and sends a memo to each office to inform them of the expense.
- **Employee Statuses** - The Business Office may not receive advanced notification regarding the termination of an employee and therefore the employee may continue to show up as an active employee when they are no longer employed by the office. Also, since many employees of the offices do not have a set schedule we must rely on the office to notify us of changes. However, it should be noted that the Business Office will make attempts to verify the status of employees to see if they should be terminated, however many offices choose to keep an employee as active though they may not work for an unknown amount of time.
- **Standard Hours** - We have been advised that employees in the Administrative Clerk position are paid for hours worked and any hours over 40 are paid at the overtime rate

of time and a half. Employees in the Legislative Assistant position whose standard work week is 25 hours are paid for all hours reported up to the 25 and any hours over that amount is recorded as compensatory earned. To address the issue of inputting time for employees the Business Office notifies employees via email that they will be compensated for the hours that he/she actually key in. Those staff members that fail to make the needed corrections could potentially be paid for hours less than the standard work hours.

Metro Council President's Response

Early in my tenure, I asked the Office of Internal Audit to conduct an audit of our business practices to determine if there were any areas that needed attention or ways we could be more efficient. I have reviewed the Metro Council Financial Operations Audit Report and determined that as a starting point, the results should be assigned to the Government Accountability and Oversight Committee in an effort to at a minimum, review the Metro Council Policy and Procedures and update them accordingly.

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