



DATE: April 3, 2009

TO: PATRICK WIEMILLER, Director  
Public Works Department

THROUGH: RENENA SMITH, Budget Director  
Budget and Management Studies Division

FROM: BOB KOURY, Principal Internal Auditor  
Budget and Management Studies Division - Internal Audit

SUBJECT: FOLLOWUP REVIEW - AUDIT OF PUBLIC WORKS CAPITAL PROJECTS  
PROCESSES AND OVERHEAD RATES/BILLING PROCEDURES SPECIFIC  
TO CITY ("CUSTOMER") DEPARTMENT PROJECTS

Attached is the Final Follow-Up Audit Report with the current implementation status of the 10 recommendations made in the Public Works Capital Projects Processes and Overhead Rates/Billing Procedures Audit Report issued March 25, 2008. This Follow-Up Audit was performed in accordance with AO 1-12 and Government Auditing Standards.

Internal Audit has concluded the current implementation status for the 10 audit recommendations as follows:

Implemented	3
In Progress	4
Not Implemented	<u>3</u>
Total	<u>10</u>

Thank you for your assistance during the course of this follow-up audit. If you have any questions, please contact Bob Koury, Principal Internal Auditor, at 621-7072.

Attachment

cc: Ashley Swearengin, Mayor  
Council Members  
Andrew T. Souza, City Manager  
Bruce Rudd, Assistant City Manager  
Margaret Arechiga, Deputy City Manager  
Susan Derpinghaus, MA III, Public Works Administration  
Karen Bradley, Interim Finance Director/City Controller, Finance Department  
Scott Motsenbocher, Budget Analyst, Budget and Management Studies Division



## **FINAL FOLLOW-UP AUDIT REPORT**

# **PUBLIC WORKS CAPITAL PROJECTS PROCESSES AND OVERHEAD RATES/BILLING PROCEDURES AUDIT**

**Performed by:  
Bob Koury, Principal Internal Auditor  
Budget and Management Studies Division – Internal Audit**

**Issued on April 3, 2009**

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## **AUDIT RESULTS AND RECOMMENDATIONS**

### **Finding 1 – Lack of Formal (Written) and Standardized Policies and Procedures Related to Capital Projects Completed and/or Managed by Public Works for City Departments, and Need for Improved Communication Between Public Works and Their “Customer” Departments**

- ▶ It was noted during the course of this audit that no formalized (written) and standardized policies and procedures exist for both Public Works and City “Customer” Departments related to:
  - 1) the Capital Projects processes and time-lines from initiation to completion;
  - 2) time-keeping for direct labor and other project costs recordkeeping;
  - 3) project cost monitoring, oversight and reporting;
  - 4) the defined and clear roles and functions for both Public Works project managers and “Customer” Department staff;
  - 5) billings process of direct labor, equipment charges and overhead;
  - 6) formalized, documented and regularly scheduled project status meetings; and
  - 7) the budgeting and accounting for such capital projects, within the appropriate fund(s), throughout the “life” of the capital project.
  
- ▶ Overall feeling by most Public Works Division Managers interviewed that most City “Customer” Departments do not fully and clearly understand: 1) how capital projects processes flow, 2) critical time-frames for projects, 3) charging of time by Public Works staff working on their projects, 4) adequate budgeting for, and monitoring of, capital projects jointly between Public Works and City Departments, and 5) what overhead rates represent and how they impact the costs of the project, Public Works billings procedures, etc.

Failure to have in place formalized and standardized policies and procedures/guidelines, for both Public Works and “Customer” Departments related to capital projects processes and procedures, leaves much to individual interpretation; creates frustration and inconsistencies in job performance; reduces efficiency and effectiveness of accomplishing the particular task or assignment (capital project) being completed; and impacts communication and working relationships for parties involved.

Consistent, ongoing and clear communication between both parties is also critical in order to have an efficient and effective capital projects system of record-keeping, reporting, documentation and for the completion of such projects in a timely and appropriate manner.

### **Audit Recommendations**

1. Public Works Management should immediately develop formalized (written) policies and procedures related to the various capital projects processes and functions as cited in Finding 1 above. This recommendation should be performed jointly and in concerted efforts with Public Works’ “Customer” Department Management.

2. Upon the completion of recommendation 1 above, these formalized policies and procedures should be clearly and formally communicated to all applicable Public Works Managers and staff and to their “Customer” Department managers and staff. They should also be monitored for compliance by appropriate management staff within Public Works and the respective “Customer” Departments.
3. If any of the formalized capital projects policies and procedures developed and implemented by Public Works were to subsequently change due to either City policy or Departmental policy changes, appropriate revisions should be made to said policies and procedures. These changes should then be formally and clearly communicated and distributed to all appropriate Public Works and “Customer” Department managers and staff.

#### Original Management Response to Recommendations 1 – 3

The Public Works Department (PW) concurs with the findings. We will draft written policies and procedures for the capital project processes and communicate the information to both PW staff and Customer Departments. Ongoing monitoring for compliance will occur once the policies and procedures are complete. Amendments to the policies and procedures will be incorporated into the document and communicated to all parties as needed. Estimated completion date: June 30, 2008

#### Current Response & Status of Recommendations 1 – 3 – In Progress

Over the last year, the Department wrote portions of the policies and procedures manuals to meet the recommendations. Specifically, portions of the Accounting and Design Services manuals were updated as needed. The Department also stays up to date with the Caltrans Local Assistance Procedure Manual which is the required manual for all State and Federal grants (the majority of the Department’s funding). The joint project with CSUF graduate students to map the entire capital project process from beginning to end was completed. This project provides visual aides of the capital process. The Department will continue to work toward completing the manuals as time permits.

During the audit, the Department expanded its regular meetings with clients to discuss all aspects of the capital projects under management. Examples of the topics covered include, but are not limited to, the overall project process, expectations of the client and project management staff, communication, project budgets and costs, and project critical path timelines and estimated completion date. At these meetings, held at intervals requested by the client (some weekly, others biweekly or monthly), the project’s status is discussed and client questions are answered.

4. A formalized system of communication between the Public Works Department and its “Customer” Departments should also be established in conjunction with the formalized policies and procedures to be implemented in the above audit recommendations. The frequency and mode of communications between both

parties throughout the “life” of the capital project should be clearly spelled out in such procedures and complied with by all applicable staff. (Also see audit recommendations 5 and 6.)

#### Original Management Response to Recommendation 4

PW concurs with the finding and has already begun implementation. Frequent project meetings are held with client departments on some capital projects. PW will continue to meet with clients and provide them with information throughout the life of the projects. Clients will be informed on policies and procedures ensuring that communication of key project milestones and issues. Estimated completion date: Ongoing

#### Current Response & Status of Recommendation 4 - Implemented

The capital project meetings described in Update to Recommendation 1-3 is the formalized system of communication in place. Clients are also encouraged to contact the project management team at any time via phone or e-mail even outside normal business hours if necessary. The project management team discusses and advises the client on policies and procedures applicable to the capital project at these meetings along with other pertinent project information.

### **Finding 2 – Inconsistencies and Inefficiencies in Time-Keeping Systems for Capital Projects**

Throughout the interviews conducted by Internal Audit of various Public Works Managers, as well as City “Customer” Department staff, time-keeping for capital projects was a constant issue of frustration and consternation from most individuals interviewed. Some of the comments and related audit findings noted via the interviews related to capital projects time-keeping:

- ▶ Some Departments use KRONOS and some Departments use PeopleSoft “Time and Labor” module for direct labor related to capital projects, i.e. inconsistency in coding direct labor by Public Works and their “Customer” Departments for capital projects. Although there is no negative impacts to capital project accounts as a result of this practice, it does make it difficult for comparison and/or reporting purposes when two separate time-keeping systems are used for this process.
- ▶ Some “Customer” Departments code some of their own time related to their capital projects while other Departments do not code any of their time to their capital projects, i.e. inconsistency amongst “Customer” Departments of capturing and “charging” all true costs of a particular capital project.
- ▶ Specific issues encountered by both Public Works and their “Customer” Departments related to capital project time-keeping and billing are as follows:
  - a) Untimely “set-up” of Capital Project Fund/Org/KRA and Project Number into KRONOS by Payroll for Public Works managers and staff to code

their time related to “Customer” Department capital projects.

This issue is caused by both a lack of adequate planning and communication between Public Works and “Customer Departments”.

Result: Public Works staff will code their time to another, inappropriate “open” project in order to keep their time coded into KRONOS on a daily basis, as required by their own management.

- b) “Deactivation” of specific capital projects within KRONOS by Payroll per the request of “Customer” Departments, even if Public Works still incurring direct labor related to the capital project. Public Works also will be instructed by some “Customer” Departments to not code anymore of their time to a capital project because “they were out of funds”, and Public Works may or may not be instructed on what other fund/project they could bill for their time.

These issues were stated by both Public Works and “Customer Department” managers during the audit specific to the processes of “deactivating” project numbers in the time-keeping systems and/or that Public Works should not code anymore time to a particular project, i.e. there was no specific audit tests performed of project costs effected from these issues as there would be no “audit trail” for such tests.

Result: Public Works either absorbs their time (costs) related to the particular capital project or simply codes their time inappropriately to another “open” capital project on KRONOS.

- c) It is not clear to “Customer” Departments that some higher level Public Works managers will charge time to their capital projects even though they may not be physically on the project site at all, i.e. lack of clear and ongoing communication between Public Works and “Customer” Departments.
- d) Significant problems were stated by “Customer” Departments when Public Works managers or staff do not follow their instructions at the commencement of the capital projects as to which Fund/Org/KRA and Project Number to use in coding their time into KRONOS for each specific capital project.

Result: The “Customer” Departments must spend a significant amount of time every pay period correcting charges (direct labor) inappropriately coded to the wrong capital project by Public Works staff.

- e) A lack of knowledge noted by both Public Works Managers, staff and “Customer” Departments on the KRONOS system itself. For example, when and how capital projects are “set up” as well as “deactivated” by Payroll, time-lines and critical “cut-off times” related to the KRONOS system and its interface into the PeopleSoft Payroll System, overhead

billings calculated on direct labor time, and general payroll processes and issues that do arise related to capital projects that both Public Works and "Customer" Departments may or may not be aware of that can impact this area of capital project time-keeping.

#### Audit Recommendations

5. Public Works Administration should request that their Accounting staff and the Finance Department Payroll staff representatives formally meet with all Public Works Division Managers and appropriate "Customer" Department staff on a quarterly basis to discuss, clarify and resolve such issues as:
  - a) when and how capital projects are "set up" as well as "deactivated" by Payroll in KRONOS and/or PeopleSoft;
  - b) time-lines and critical "cut-off times" related to the KRONOS system and its interface into the PeopleSoft Payroll System;
  - c) overhead billings processes and impacts by direct labor time-keeping for such calculations; and
  - d) to discuss and resolve any type of time-keeping problem encountered via KRONOS or PeopleSoft related to capital projects being completed and/or managed by Public Works for their "Customer" Departments to minimize such problems and enhance efficiencies.

#### Original Management Response to Recommendation 5

Many of the findings are not specific to PW's timekeeping in Kronos as they relate to the client department. PW will not address those findings here.

It should be noted that the finding related to the Untimely "set-up" of Capital Project Fund/Org/KRA and Project Number into Kronos is a Citywide policy that requested by the client departments. PW addressed the noted consequences of this policy with Finance, Payroll staff and was told that the policy would stand. Based on this decision, PW, Finance, Payroll and the client departments do their best to set-up Kronos as quickly as possible once the request for service is received.

For those findings and recommendations that are specific to PW, the Department is aware of the issues and has already begun implementation of procedures to address them.

Frequent project meetings are held with client departments on some capital projects. Funding issues and charges are addressed at these meetings on an as needed basis. In addition, PW Finance staff regularly communicates with client department accounting staff to resolve any

issues that the client departments bring to PW's attention. PW will continue to meet with and communicate with clients and provide them with information throughout the life of the projects. Clients will be informed on policies and procedures ensuring that communication of key project issues. PW will also continue to meet with its own managers and staff to educate them on Kronos time-lines, cut-off times and timekeeping processes. Estimated completion date: Ongoing

#### Current Response & Status of Recommendation 5 – In Progress

There is no update to the Department's response. The Department continues to work with client departments and Finance, payroll to set up new projects in Kronos as quickly as possible. The Accounting Section maintains contact with Department staff on an ongoing basis to explain the timekeeping and overhead processes and address any issues that arise. Funding issues and charges are addressed and resolved as the issues arise whether in the capital project meetings or as the Department communicates with the client outside of these meetings.

6. Formalized meetings should also occur on a regular basis (e.g. quarterly) between Public Works Project Managers and their "Customer" Department staff to discuss the status of all current capital projects and any problems with the timely completion of such projects as planned, anticipated problems and/or change orders and related fiscal impacts to such projects. These meetings should also allow Public Works Managers to fully and adequately explain the capital projects processes, time-lines, staff who will be charging their labor to such projects, budgetary and funding issues, etc. to their Customer Department staff for improved communication between both parties.

The meetings referenced in recommendations 5 and 6 above should be documented for future reference and/or audit purposes.

#### Original Management Response to Recommendation 6

PW concurs with the recommendation. See Management Response to Recommendation 5 related to frequent project meetings. Estimated completion date: Ongoing

#### Current Response & Status of Recommendation 6 - Implemented

The regular meetings with client departments are held. See response in Updates to Recommendations 1-4 above for details. In addition, weekly meetings between the Project Management Manager and the project staff are held to discuss the status of the projects and address any issues.

### **Finding 3 - Public Works Capital Projects Overhead Rates and Related Billings Issues**

During this audit, various issues were noted related to the Public Works capital projects overhead rates currently being used and the billings process of such overhead rates by Public Works to their "Customer" Departments, as follows:

- ▶ The current Public Works overhead rates being billed by Public Works to their "Customer" Departments were developed in October 2003, with charges/billings commencing in FY04 and continuing through FY08. These overhead rates are obviously out of date and undocumented as to the methodology and supporting details and amounts used to calculate such rates in October 2003; thus, the Internal Auditor was unable to audit such rates as to reasonableness and appropriateness for billing purposes.

The Streets Division processes their own overhead billings through the CFTI program, whose rates are also undocumented and were implemented in November 2003.

Result: The current overhead charges being billed by Public Works to their "Customer" Department capital projects may be understated or overstated, impacting the total costs of such capital projects.

#### Current Overhead Rates Developed in October 2003:

##### General Engineering

Division Rate = 74.31%

Admin – General Government Rate = 40.69%

##### Construction Management

Division Rate = 42.10%

Admin – General Government Rate = 5.90%

##### Streets

Division Rate = 51.16%

TSSL (Traffic Signal & Street Lights) = 65.35%

PW Admin = 8.46%

- ▶ Public Works overhead billings are processed, in most cases, every pay period via the CFTI program which in turn posts to the PeopleSoft Financial System. Both overhead and equipment charges are processed by Public Works via the CFTI program.

During the audit, several of Public Works' "Customer" Departments indicated that they do not have an opportunity to review the CFTI Reports related to overhead billings prior to the charges being processed into PeopleSoft Financial System. Only one Department indicated that they were, in fact, provided the "CFTI Transaction Group Reports" from Public Works for their review and corrections prior to Public Works processing their charges into PeopleSoft.

The “Customer” Departments who did not have the opportunity to review their equipment and overhead billings prior to these charges posting to PeopleSoft indicated they had to spend significant amount of time correcting these type charges within PeopleSoft every pay period due to errors in coding by Public Works staff, e.g. incorrect fund, org, account or project number used by Public Works. These particular “Customer” Departments either did not know they could obtain the “preliminary CFTI reports” of their charges prior to being processed into PeopleSoft by Public Works or simply did not request them as the one Department noted above did.

#### Audit Recommendations

7. The Public Works Department should immediately develop current, appropriate and reasonable overhead rates for all applicable Divisions involved with capital projects for their “Customer” Departments. These overhead rates should be adequately documented and then reviewed and approved by Public Works Management prior to implementation.
8. Once the new overhead rates for the Public Works Department have been developed, documented and approved, they should be programmed into the CFTI program, tested for accuracy of calculation of overhead charges, and then implemented.
9. Prior to the implementation of the new Public Works capital projects overhead rates, these rates and effective billing implementation date should be formally communicated to all of Public Works “Customer” Departments for planning, budgeting and accounting purposes.

#### Original Management Response to Recommendations 7 - 9

PW concurs with the recommendation, however, due to the multitude of tasks currently assigned to the PW Accounting staff, the analysis and implementation of new overhead rates will take time. Once the analysis is completed, the new rates will be tested and implemented. Estimated completion date: June 30, 2008

#### Current Response & Status of Recommendations 7 – 9 – Not Implemented

There is no update to the Department’s response. Due to the significant economic and staffing difficulties encountered by the Department in the last year, this project was not completed. The Department still plans to review the current overhead rates for reasonableness and implement the new rates as soon as is practical.

#### Internal Audit Comment

**Recommendations 7 through 9 must be implemented immediately. As the current overhead rates are over five years old, it is critical for these rates to be updated for appropriate and accurate capital project costing for both Public Works and City “Customer” Departments budgeting purposes.**

10. Public Works Accounting and Streets Maintenance Divisions should immediately commence providing “preliminary” overhead and equipment charges reports (via CFTI) to all of their “Customer” Departments for their review prior to processing such charges into the PeopleSoft Financial System. This will allow such “Customer” Departments to review and correct any inaccuracies in such billings by the Public Works Department for improved efficiencies and capital

projects reporting purposes. Public Works Divisions should, of course, establish appropriate time limits for the “Customer” Departments for this review process in order to continue to process such overhead and equipment charges in a timely manner.

#### Original Management Response to Recommendation 10

PW concurs with the recommendation. Client departments will be able to review the charges for proper fund/org./project/activity. They will be given 5 business days to respond before the charges will be automatically posted. This will delay recording of the transactions, but will provide the review that is recommended. Estimated implementation date: February, 2008

#### Current Response & Status of Recommendation 10 – Implemented

The recommendation was implemented in a manner different than originally proposed. For the Street Maintenance Division, estimated overhead and equipment charges are provided to the client at the time the client hires the Division. During the project, the client reviews project costs and requests additional information from Street Maintenance if needed. At this time, client departments are comfortable with this process.

For Capital Management, the process is similar. The project budget is discussed with the client at the time the client hires the project management team. Throughout the project, at the capital project meetings and any other time the client contacts the Department, any concerns with the overhead and equipment charges are discussed. Client departments also contact the Department’s Accounting Section directly with questions or concerns. At this time, client departments are comfortable with the process and do not desire more detail information on these charges.