Item (2)

Memo

July 11, 2012

To: City Council Members

From: Audit Advisory Board

CC: Mayor Beutler, Mayor's Office

Re: Agreed-Upon Procedures Partial Response to City Council Resolution A-86267/A-86477

Recommendations of Audit Advisory Board

On June 27, 2012, the Audit Advisory Board met and reviewed the Agreed-Upon Procedures Report regarding the Engineering Revolving Fund from BKD. The Report did not note any exceptions and made two minor recommendations.

The scope of this audit/engagement with BKD, was limited to the provision of a Report and a Finding of Agreed-Upon Procedures regarding the Engineering Revolving Fund. After reviewing this Report, the Board makes the following findings regarding those items found in L.M.C. Section 4.66.040 (d) (1) (ii) and (iv):

1) Engineering Revolving Fund revenues earned from billable hours are recorded accurately in the general ledger and reconcile to the job cost system; the calculation of the overhead rate is accurate and includes proper operational costs.

2) Engineering Revolving Fund internal controls over Cost Accounting procedures, billing procedures, systems for tracking and allocating direct labor costs, and systems for allocating indirect labor costs to appropriate indirect labor categories, are adequate.

This Board did not make findings regarding those items found in L.M.C. Section 4.66.040 (d) (1) (i) and (iii) as those items were not addressed by the scope of this engagement.

As required by L.M.C. Section 4.66.040 (d) (2) a copy of the final audit report is attached. Also attached is the auditee response.

Because of the scope of this engagement this Board did not create a separate listing of any irregularities or failures to comply with legal or administrative policies as required by L.M.C. Section 4.66.040 (d) (3).

Based upon the report from BKD and the response from management, the Board makes no recommendation.

CITY OF LINCOLN
NEBRASKA

MAYOR CHRIS BEUTLER
lincoln.ne.gov

Public Works and Utilities Department
Miki Esposito, Director
555 South 10th Street
Suite 208
Lincoln, Nebraska 68508

July 11, 2012

The Members of the City of Lincoln Advisory Board
Engineering Revolving Fund
City of Lincoln, Nebraska

BKD, LLP has completed the Agreed-Upon Procedure engagement for the Engineering Revolving Fund. Below is our response to their recommendations.

Calculation of the Overhead Rate

Currently, the calculation of the overhead rate for the Engineering Revolving Fund is a detailed calculation which specifies all budgeted costs to be incurred by the Fund, by line item, with a subsequent line item adjustment based on actual results. We found no errors or discrepancies in the calculation during our application of agreed-upon procedures. However, it is our understanding that the process for obtaining and compiling the information necessary for the calculation requires a substantial amount of time on the part of management. We recommend this calculation be simplified to potentially reduce the time burden on management and mitigate the risk of error within the calculation due to its complexity. Several factors to consider when determining what revisions can be made to the calculation are, but are not limited to:

- Utilizing the net change in fund balance to determine adjustments to the overhead rate
- Evaluating what level of detail should be maintained within the calculation as support for management review and other interested parties
- Ensuring any changes to the calculation of the overhead rate conform to state and federal guidelines

Management Response: *Management realizes there is a simpler manner in which to calculate the annual overhead rate. However, the detailed and more comprehensive approach is used to satisfy our federal requirements (2 CFR Part 225 – Circular A-87).*

The Nebraska Department of Roads (NDOR) Controller Division – Audit Section recently reviewed the overhead rate. It was their opinion that the methodology used was acceptable and fulfilled all the federal requirements. The Nebraska Department of Federal Highway Administration also reviewed the report issued by NDOR and concurred with their opinion. (I have attached, for your review, the reports issued by the two agencies.)

In light of all the federal funds Public Works receives, we believe it is in our best interest to continue using the same process in the calculation of the overhead rate.

LINCOLN
The community of opportunity

Management Review of Hours Utilization

An effective management oversight tool is the evaluation of employee hours charged directly to projects compared to total available employee hours. Such an evaluation provides management with a determination of the utilization of time for certain employees of the Engineering Services Division. It is our understanding this evaluation is performed periodically by management, however, this assessment is not currently being performed on a regular basis. We recommend management consider the feasibility and cost-effectiveness of performing this evaluation more frequently.

Management Response: *Management informally performs this evaluation, but will consider formalizing the process.*

Sincerely,

Fran Mejer

Fran Mejer
Public Works & Utilities Business Manager

Attachments

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Review Of

City of Lincoln
Public Works Department
555 South 10th Street / Suite 203
Lincoln, NE 68508-3994

State - Engineering Revolving Fund Overhead Rate Review – FY2011/2012

This report is prepared for the use of the Nebraska Department of Roads administrative officials. Final determinations establishing the official position of the Nebraska Department of Roads on the matters reported herein are made by these officials.

Date Issued: April 19, 2012

Nebraska Department of Roads
Controller Division - Audit Section
Report No. 2012-35

Approved: _____
James A. Dietsch
Highway Audit Manager

PART I – SCOPE AND OPINION

A. Scope of Review

In response to the requirements of 2 CFR Part 225 (Circular A-87) we have conducted a review of the State - Engineering Revolving Fund Overhead Rate Proposal for FY-12, submitted by the City of Lincoln, Public Works Department..

The objectives of our review were to provide reasonable assurance that the proposed rate was calculated using a method that was consistent with the applicable requirements of 2 CFR Part 225; that the costs used to calculate the proposed rate (both actual and proposed) correctly reflect expenses actually incurred by the City of Lincoln, Public Works Department, Engineering Section and that the proposed costs were consistent with the approved budget for the fiscal year for which the rate was proposed and that the cost elements used in the calculation do not contain costs deemed unallowable by the above referenced, governing requirements.

We have conducted a desk review of documents requested and supplied by the City of Lincoln, Department of Public Works that support the rate proposed.

B. Opinion Statement

It is our opinion that the methodology used by the City of Lincoln – Public Works Department in the development of the proposed State - Engineering Revolving Fund overhead rate for FY-12 (September 1, 2011 through August 31, 2012) is acceptable. However one of the cost components, the one associated with the city "Central Services" ($121,094.00), has been determined to be unallowable and cannot be included in the calculation of an acceptable State - Engineering Revolving Fund Overhead Rate. The rate proposed by the City of Lincoln / Public Works Department is 201.5%. Based on our review, a rate acceptable and consistent with the provisions of 2 CFR Part 225 is 195.7%, for a difference of 5.8%.

It is recommended that the acceptable State - Engineering Revolving Fund Overhead Rate of 195.7% be used by The City of Lincoln / Public Works Department for the remainder of the current fiscal year (FY-12).

We have no objection to the release of this report to the City of Lincoln, at the discretion of Nebraska Department of Roads administrative officials.

C. Acceptable State - Engineering Revolving Fund Rate for FY-2011/2012

Description	Proposed 2012 (Budget)	Over/Under Adjustments from Prior Fiscal Year	Adjusted 2012 base	Rate	
Base Salary Costs	2,257,127.00	(152,247.00)	2,104,880.00		
Direct and Indirect Costs	4,788,674.00	(548,251.00)	4,240,423.00	201.5%	Proposed Rate
		Less: Central Services	(121,094.00)		
			4,119,329.00	195.70%	Adjusted, Acceptable Rate

U.S. Department of Transportation
Federal Highway Administration

NEBRASKA DIVISION

100 Centennial Mall North
Room 220
Lincoln, NE 68508
(402)742-8460

July 2, 2012

In Reply Refer To:
HDA-NE

Mr. Anthony Dirks
Nebraska Department of Roads
Local Projects Division
Lincoln, NE

Dear Mr. Dirks:

City of Lincoln Engineering Revolving Fund Overhead Rate for FY 2012

The Nebraska Division of the Federal Highway Administration has reviewed Report 2012-35 of the Nebraska Department of Roads (NDOR), Controller Division – Audit Section, dated April 19, 2012. The purpose of our review was to confirm that the NDOR recommended City of Lincoln Engineering Revolving Fund Overhead Rate for FY12 was determined in accordance with the requirements of 2 CFR 225 as it pertains to the allowability, eligibility, and allocability of costs.

The rate as currently proposed by the City of Lincoln was 201.5%. From the NDOR review, there was one adjustment needed to bring the rate into conformity with 2 CFR 225. The adjustment was:

> Disallowance of the cost component from the "Central Services" allocation as this component was calculated using a predetermined rate. The impact of this adjustment would be to reduce the proposed rate by 5.8%.

Based on our review of your report, we concur with your recommended adjustment and approve the proposed engineering revolving fund overhead rate of 195.7%.

If you have any questions, please feel free to contact James Lockwood at (402)742-8468.

Sincerely yours,

Joseph A. Werning
Division Administrator

Enclosure

RECEIVED
JUL 6 2012
BY:

Review Of

City of Lincoln
Public Works Department
555 South 10th Street / Suite 203
Lincoln, NE 68508-3994

State - Engineering Revolving Fund Overhead Rate Review – FY2011/2012

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Date Issued: April 19, 2012

Nebraska Department of Roads
Controller Division - Audit Section
Report No. 2012-35

Approved: _____
James A. Dietsch
Highway Audit Manager

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BKD LLP
CPAs & Advisors

1248 "O" Street, Suite 1040
Lincoln, NE 68508-1461
402.473.7600 Fax 402.473.7698 www.bkd.com

The Honorable Mayor
and Members of the City Council
Engineering Revolving Fund
City of Lincoln, Nebraska

During our application of agreed-upon procedures with respect to the Engineering Revolving Fund for the period of September 1, 2009 through August 31, 2011, we observed the following matters and offer these comments and suggestions. The matters discussed herein are offered as recommendations to implement certain best practices and to enhance the financial reporting process.

Calculation of the Overhead Rate

Currently, the calculation of the overhead rate for the Engineering Revolving Fund is a detailed calculation which specifies all budgeted costs to be incurred by the Fund, by line item, with a subsequent line item adjustment based on actual results. We found no errors or discrepancies in the calculation during our application of agreed-upon procedures. However, it is our understanding that the process for obtaining and compiling the information necessary for the calculation requires a substantial amount of time on the part of management. We recommend this calculation be simplified to potentially reduce the time burden on management and mitigate the risk of error within the calculation due to its complexity. Several factors to consider when determining what revisions can be made to the calculation are, but are not limited to:

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An effective management oversight tool is the evaluation of employee hours charged directly to projects compared to total available employee hours. Such an evaluation provides management with a determination of the utilization of time for certain employees of the Engineering Services Division. It is our understanding this evaluation is performed periodically by management, however, this assessment is not currently being performed on a regular basis. We recommend management consider the feasibility and cost-effectiveness of performing this evaluation more frequently.

* * * *

We appreciate the opportunity to present these comments and suggestions. We can discuss these matters further at your convenience and may provide implementation assistance for changes or improvements if you require.

experience BKD

Praxity MEMBER
GLOBAL ALLIANCE OF INDEPENDENT FIRMS

This communication is intended solely for the information and use of management, the Mayor and members of the City Council and is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

March 14, 2012

BKD LLP
CPAs & Advisors

1248 "O" Street, Suite 1040
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Independent Accountants' Report on Application of Agreed-Upon Procedures

The Honorable Mayor
and Members of the City Council
Engineering Revolving Fund
City of Lincoln, Nebraska

We have performed the procedures enumerated in the attachment to this report, which were agreed to by the management of the City of Lincoln, Nebraska solely to assist you with respect to accounting procedures for the Engineering Revolving Fund for the period of September 1, 2009 through August 31, 2011. The management of the City of Lincoln, Nebraska is responsible for the proper recording of transactions and for financial statement elements and accounts of the Engineering Revolving Fund. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of the parties specified in this report. Consequently, we make no representation regarding the sufficiency of the procedures described in the attachment to this report for the purpose for which this report has been requested or for any other purpose.

There were no exceptions noted in the procedures we performed.

We were not engaged to, and did not, conduct an examination, the objective of which would be the expression of an opinion on the specified financial statement elements and accounts described above. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the specified parties identified above and is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

March 14, 2012

experience BKD

Praxity MEMBER
GLOBAL ALLIANCE OF INDEPENDENT FIRMS

City of Lincoln, Nebraska
Agreed Upon Procedures – Engineering Revolving Fund

Time Period for all Testing: September 1, 2009 – August 31, 2011

1. Examine and test internal control structure for the following elements:

    - Cost accounting practices and procedures
    - Billing procedures and controls
    - Systems for tracking and allocating direct labor costs
    - Systems for allocating indirect labor costs to appropriate indirect labor categories

2. Track 25 labor samples from employees time records to:

    - The payroll records to assure hours recorded are paid
    - The cost system to assure hours are posted properly to jobs
    - The general ledger to assure the total posted is recorded in the financial accounting system

3. Verify the revenue earned from billable hours is recorded accurately in the general ledger and reconciles to the job cost system. A test of three is required.

4. Verify the accuracy of the calculation of the overhead rate.

5. Verify if costs included in the overhead rate are operational costs incurred by the Fund and are properly included.