



Office of the City Auditor

**Audit of Capital Improvement Program
Final Closeout Process**

Report Date: October 23, 2014

Office of the City Auditor
2401 Courthouse Drive, Room 344
Virginia Beach, Virginia 23456
757.385.5870

"Promoting Accountability and Integrity in City Operations"



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Lyndon Remias, CPA, CIA
Chris Ford, CPA

City Auditor
Deputy City Auditor

www.vbgov.com/cityauditor

Office of the City Auditor
2401 Courthouse Drive, Room 344
Virginia Beach, VA 23456
Telephone: 757.385.5870 Fax: 757.385.5875

Fraud, Waste, and Abuse Hotline 757.468.3330



Date: October 23, 2014

To: James K. Spore, City Manager

Subject: Audit of Capital Improvement Program
Final Closeout Process

I am pleased to present the report of our audit of the Capital Improvement Program (CIP) Final Closeout Process.

The objectives of our audit were to review the City's process of final closing CIP projects to:

- Document the processes, risks and related internal controls and assess whether the controls are adequately designed to reduce risk to an acceptable level.
- Test the controls determined to be designed adequately to reduce risk to an acceptable level to determine if the controls are operating as designed.
- Make recommendations to improve controls over the closeout process.

Findings considered to be of insignificant risk have been discussed with management. We completed field work on September 5, 2014.

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We would like to thank the Department of Finance for their courteous and prompt assistance during our audit. The staff was receptive and excellent to work with.

If you have any questions about this report, or any audit-related issue, I can be reached at 385.5872 or via email at lremias@vbgov.com.

Respectfully submitted,

A handwritten signature in blue ink that reads "Lyndon S. Remias". The signature is written in a cursive, professional style.

Lyndon S. Remias, CPA, CIA
City Auditor

c: City Council Members
Audit Committee Members
Dave Hansen, Deputy City Manager
Patricia Phillips, Director of Finance



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Purpose

The purpose of our audit was to document the Capital Improvement Program (CIP) final closeout process and related controls and to assess the design and compliance with those controls.

Scope & Objectives

The scope of the audit covered the CIP project closeout process for the fiscal year ended June 30, 2014. We also utilized the fiscal year end June 30, 2013 for a few select tests as well.

The objectives of our review were:

- To document in detail the procedures and related controls governing the final closing of CIP projects in the City.
- To assess whether those controls are designed effectively to reduce risk to an acceptable level.
- To test the controls deemed to be designed effectively to determine if they are operating as designed and offer recommendations to improve controls.

Methodology

To accomplish our objectives, we performed the following procedures:

- Obtained CIP background information from the Budget & Management Services' FY 2014-15 Adopted CIP Resource Management Plan (Budget), CIP Process Manual, various InSITE/GovMax CIP related reports, written closeout policies and procedures, Public Works' PPTS system of project status, various correspondence amongst City departments involving project status, prior years' closeout results, and various internet articles.
- Through interviews, written policies and procedures, walkthroughs, InSITE and Excel reports, documented in detail the CIP closeout process.
- Identified the related risks and key controls in the closeout process.
- Assessed whether the key controls were designed adequately (the project related information compiled on the master worksheets used to identify projects to close) to reduce the associated risks to an acceptable level.
- Performed tests of the key controls (verified the accuracy, reasonableness and completeness of the information, data, and criteria compiled on the master worksheets used to identify projects that are to be closed).
- Reviewed projects that were initially proposed (from data/criteria on project worksheets) for consideration to be closed but after further research and discussion it was decided not to final close to ascertain whether there were reasonable reasons given to not close.



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- Reviewed project information for projects never proposed /considered for final closure to ascertain if they should have been final closed.
- Offered recommendations to improve the design of the final close controls/process.



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Standards

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained during this audit provides a reasonable basis for our findings and conclusions based on our audit objectives.

The Office of the City Auditor reports to City Council through the Audit Committee and is organizationally independent of all City Departments. This report will be distributed to the City's Audit Committee, City Council, the Department of Finance, and appropriate management. This report will also be made available to the public.



Background

The City of Virginia Beach manages roughly 500 projects in the Capital Improvement Program (CIP) involving multiple departments serving as a project's managing agency. The Department of Finance provides accounting and closing responsibilities of projects while Budget & Management Services provides budget/funding decisions for the CIP. The diverse nature, volume and complexity of projects; the often extensive time frames of projects; the various funding sources/funding decisions; the long term debt ramifications and the overall complexity of the program is considerable. The dollar amount of the program, which for the CIP for fiscal year 2015 had appropriations of 1.275 billion to date and 281 million appropriated for 2015, as illustrated in *Appendix I* is substantial.

With the significant amount of funding involved and the associated resource allocation decisions, along with the time use of money and long-term debt considerations accompanying the program, it is essential that appropriated funds be utilized in a timely and efficient manner. One (funding is routinely shifted between projects at times *other than closing*) of the many aspects of that very complex dynamic is assuring that a process is in place in the City whereby the final closeout of CIP projects is performed in a timely and transparent manner so that projects can be closed and the unexpended funds be transferred to projects needing that funding.

Summary of CIP Closeout Process

The Department of Finance is tasked with final (and partial) closing of City CIP projects. In 2013, the Department of Finance hired a full time CIP accountant who manages the process. The department has very detailed written closeout procedures entitled "Capital Improvement Program Project Closeout" which can be found on page 71 of the *City of Virginia Beach Department of Finance Comptroller's Division Accounting Procedures*. The following is a summary of those procedures:

- 1) Finance obtains copies of the CIP project information submitted by departments to Budget & Management Services for the new budget year (CIP budget process). This includes unused funding for completed projects.
- 2) The CIP accountant utilizes eight worksheets, (Schools manages its own CIP section) – one for each City CIP section (Buildings, Roadways, Water & Sewer, CIT, Coastal, Stormwater, Economic & Tourism, Parks and Recreation) that lists in the first two columns each active project by project number and title. The CIP accountant researches and compiles an assortment of various data/information from a wide variety of sources throughout the City on *each* individual active project that yields information that allows him to consider which projects he may propose to consider for closing, see *Appendix II*.



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That key information is as follows:

- **Financial Information on each project** – most of this information is downloaded by two reports from InSITE, the City's accounting system, into the excel spreadsheets. The two reports are called C-CIP ANALYSIS REVENUE and C-CP BUILDING (or applicable section). The spreadsheet financial columns (Budget to date, prior years expenditures, current years expenditures, total expenditures, outstanding encumbrances) are used to compute the *unexpended balance* and *available balance* for each project at the date the information was downloaded (May 27, 2014 for FY 6/30/14 closing).
 - **Research** – the CIP accountant then researches the projects consulting a) Public Works Project Planning and Tracking System (PPTS). The PPTS is mostly used for roadway projects and requires project managers to update their project status every 3 months. b) CIP Resource Management Plan – The adopted CIP budget document containing a project sheet for each open project. c) GovMax – Budget & Management Services' resource allocation software containing detailed information on each project. d) The VDOT six year plan – State roadway budget information. The relevant information gained from the research is entered on the spreadsheet in the comments column.
- 3) The partially complete worksheet through step 2 is then given to the departments who are asked to enter the following information into the spreadsheet:
- Project percentage of completion.
 - Departmental notes concerning completion issues on projects; specifically on projects scheduled to be completed (as evidenced in CIP, GovMax, PPTS), projects with little activity or no activity in current fiscal year, projects that are 95% expended.
 - Identify and mark projects the *departments themselves* deem completed or will be by year end.
- 4) Meetings are scheduled with the managing departments to review the information on the spreadsheet, their notes/answers/explanations and discuss which proposed projects can be closed and why others cannot be. The CIP accountant maintains notes on these meetings.
- 5) From these meetings and followup correspondance (folders are maintained) Finance completes a final closeout list. Departments are responsible for liquidating all encumbrances and closing all remaining Purchase Orders. Finance monitors this to ensure completion as this must be done before they can perform the closing entries themselves.
- 6) Finance compiles the final list of Final and Partial Closeout Projects. This list is given to the Fixed Asset analyst and the CIP accountant prepares the necessary accounting



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entries to close the projects (see the Appendix of Finance's policies and procedures and looseleaf binder for the year end closeout entries actually made).

Note: When considering the above CIP *final* closeout procedures it is important to note the following:

- 1) When Budget & Management Services considers a project complete for *budget* purposes and removes it from the CIP it is not necessarily complete or close to completion from a finance/accounting or construction perspective. Budget & Management Services only removes it when they are finished appropriating funds to the project. The project could still have significant work left to be done as well as a significant amount of appropriated funding left to pay for that work.
- 2) Finance may identify and "*partially* close out" certain projects during this process as well. *Partially* closed projects may have certain aspects in service (either constructed or purchased) but are not ready to be fully closed out due to outstanding items such as outstanding work still to be done, pending vendor payments, litigation, real estate issues, punch list items or unrealized revenues. Thus the project remains open but appropriations are reduced by an equal capitalized amount creating an asset in the accounting records, yet not creating unexpended funds to be transferred/spent on other projects.
- 3) It should also be noted that appropriations can and are transferred between projects if the availability and need is identified at any stage – *not just when a project is final closed*. The Department of Finance and Budget & Management Services work together on this.

Results

Documented the CIP final closing process

We documented the CIP final closeout process by obtaining *Department of Finance Comptroller's Division Accounting Procedures* section on the closing of CIP projects (beginning of page 71) and reviewing those procedures in detail with Finance's CIP accountant charged with performing the procedures. We also obtained and reviewed each of the CIP section closeout worksheets and related documents for the fiscal year ending June 30, 2014. A summary of those procedures is in the Background section of this report.

Assessed the design of the controls of the CIP closing process

The CIP project closing procedures and process (mainly the criteria compiled on the worksheets for the active projects) are themselves the controls assuring that the final identification and closing of CIP projects is performed in a timely and transparent manner so the projects can be closed and the unexpended funds be transferred to projects needing that funding.



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The design is discussed below:

The completed CIP section worksheets are used to identify projects to close and yield the following key criteria for each project in determining which projects can possibly be closed:

- Project number and name.
- Identifies active or closed budget for the project .
- Percentage of project that is complete.
- Whether the project is partially closed and in service.
- Total project budget to date.
- Total expenditures to date segregated as to *prior years* and *current year*.
- *Current year* expenditures reveals whether and how much current activity was in project.
- *Unexpended balance* remaining (Budget less total expenditures to date).
- *Available balance* remaining (unexpended balance less outstanding encumbrances) gives the *unencumbered balance* left in the project.
- Revenues Due (unrealized) – particularly large federal and state amounts that can delay a projects closure.
- Research – Construction/Funding start and estimated completion dates, *project specifics* such as delays, lawsuits, contingencies, open work orders/punch list items etc.
- Which projects were considered (from the spreadsheet criteria) for final closure but were not and reasons why.
- The differences in the projects departments submitted to Budget & Management Services to close and what the data is suggesting could be possibly be closed and the reasons for not closing.
- Departmental discussions/answers to closure questions (details maintained in files, conclusions entered on spreadsheet).

The CIP closeout process utilizes information from the following sources in determining which projects to consider for closing and to ultimately close:

- InSITE financial information.
- CIP Resource Management Plan (The adopted CIP budget document containing individual project specifics).
- Govmax – Budget & Management Services resource allocation software.
- PPTS – Public Works' system, mostly roadway projects showing individual project status that is updated every 3 months.
- VDOT six year plan – State transportation budget information.
- Project Manager & Other Departmental Representatives Data/Information – project specific requested both originally when compiling worksheet data and followup.
- Meetings with Departmental Representatives – Discussions regarding projects, notes available on meetings.



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- Project Specific Followup questions and answers – Hardcopy files of emails are available.

With the utilization of the extensive data/criteria and source information cited above, the design of the process/controls in place to identify and close CIP projects is thorough and adequate to reduce risk to an acceptable level the risk that projects will not be closed in a timely and efficient manner

Testing of the June 30, 2014 CIP closeout procedures and controls

- To gain assurance that all *active* projects were included on the CIP worksheets we selected one CIP section worksheet – Stormwater (7000s) – and reconciled the worksheet listing with the listing in InSITE via the CIP Revenue Analysis report without exception.
- To verify that the financial information utilized on the spreadsheet is accurate we downloaded InSITE information for May 2014 (what was used in the CIP spreadsheets) from C-CIP ANALYSIS REVENUE and C-CPSTORMWATER and verified the accuracy of 1) prior years expenditures, 2) total expenditures, 3) current years expenditures and budget to date for each Stormwater project without exception. We also traced the active project budget amounts to the CIP budget documents and verified the report used to download encumbrance totals without exception.
- Verified the math on the spreadsheet to assure that 1) budget to date less total expenditures equals unexpended balance, 2) unexpended balance less outstanding encumbrances equal available balance, 3) current years expenditures plus prior years expenditures equal total expenditures. This was done without exception.
- Reviewed and researched each project from *all* CIP sections that was proposed for possible closing for June 30, 2014 based on the criteria and research gathered and quantified in the CIP worksheets, but the decision was made not to close. Researched for reasonableness the CIP accountant's explanations for leaving the project open and the departmental documentation of such by meeting notes, written communications with the project manager, and departmental representatives and the reasons were found to be reasonable.
- Scanned all of the active projects on the closeout sheets that were not considered for closing (criteria did not warrant such), made inquiries and determined that they were not in fact ready for closeout.
- Traced a sample of the projects determined to be final closed via the CIP worksheet results and verified that they were in fact closed by tracing to the InSITE CIP closing entries.



Findings and Recommendations

Finding 1: The “% complete” was not often entered

We noted that one column of information, required by departments to enter – the “% complete” was often not entered. This was a new data field added this year at the request of the City Auditor. Though it may not be a key field when considering all of the other data, research and inquiry on each project to determine closure, it is valuable information and should be required to be submitted as requested.

Recommendation:

- 1.1 We recommend requesting departments to supply the information and if they do not initially then remind them again until the information is obtained.

Finding 2: Transparency of CIP closing process

Part of the importance of the CIP closing process is the transparency the process affords to the various City stakeholders. The Department of Finance and Budget & Management Services are continually researching, inquiring, monitoring and documenting the progress of individual projects which informs stakeholders of the specific progress and funding issues of those projects. The two departments already cooperate and share a good deal of information concerning the CIP. The Department of Finance’s closing process is detailed and thorough, resulting in a wealth of knowledge concerning individual projects at each year end and would be of great benefit to Budget & Management Services in the CIP budget process.

Recommendation:

- 2.1 We recommend the Department of Finance share the ending CIP section worksheets of complied active project information with Budget & Management Services as they enter the budget process. As noted the two departments already cooperate and share a good deal of CIP information and help one another. This information could also greatly help facilitate the CIP budget process and Budget & Management Services agrees that it would be useful information.



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Conclusion

Overall, based on the results of our audit, we determined that that controls related to the identification and closure of CIP projects are designed effectively to reduce risk to an acceptable level that CIP projects are not closed timely and unexpended funds related to completed CIP projects are not identified for use in a timely manner. Compliance with the procedures and controls is strong. The CIP final closeout process utilizes every available/usable information source, is thorough, and well documented.

Acknowledgements

We would like to thank the Department of Finance for their assistance during our review. They were open to our suggestions and accommodating. They were also prompt with our information requests and willing to address all of our inquiries.



Management's Response

The below Management's Response provided by Patricia Phillips, Director, Department of Finance via email to Lyndon Remias, City Auditor, on October 22, 2014:

I am pleased that the CIP audit of the final closeout process found that the process is designed effectively, compliance with the procedures and controls is strong, and the process utilizes every available information source. The audit also found that the process is thorough and well documented. This process involves many Departments and we all take it very seriously.

#1 I would like to clarify the recommendation "% complete was not often entered". Since this isn't a key field when a project is in the beginning stages, we didn't require this information unless the project was proposed for final closeout. We will update our process to require this information from Departments if a project is more than 75% complete. It isn't in the City's best interest to require the time to obtain information if it isn't going to benefit the process.

#2 Finance has always had the philosophy of working together and sharing information with Budget & Management Services. During the closeout process, Finance already shares the preliminary closeout worksheets with Budget & Management Services. This information allowed for unused funds to be identified and transferred for the upcoming budget. Finance will initiate a more formal meeting with Budget & Management Services to discuss the final closeout worksheet and formally share available funding found during the closeout process.

We are pleased with the overall positive conclusion of the CIP final closeout process audit. We continuously review our process for more efficient and effective procedures. We appreciate the professionalism and effort put into this audit by the City auditors and would like to thank them for their effectiveness.