Ellinger, Chair
Stinnett, Vice Chair
Gorton
Kay
Ford
Beard
Farmer
Scutchfield
Mossotti
Henson

AGENDA
Budget & Finance Committee
November 19, 2013
1:00 P.M.

1.	**October 22, 2013 Committee Summary**	(1-2)
2.	**Monthly Financial Report**	(3-16)
3.	**Outsourcing Internal Audit Functions**	(17-45)
4.	**Debt Management Policy Review – Stinnett**	(46-55)
5.	**Urban Services Refund Policy – Stinnett**	(56-57)
6.	**FY 15 Links Discussion**	(58)
7.	**Items Referred to Committee**	(59)

"Budget & Finance Committee, to which shall be referred matters relating to the Department of Finance and Administration and its divisions, and any related partner agencies, the urban county courts and constitutional officers, fiscal operations of the government, revenues and expenditures of the government, and organization changers which affect the fiscal operations of the government. Additionally, this committee shall review the final audit report and management letter of the accounting firm recommended by the Mayor and selected by the Council to conduct the annual financial audit of the Urban County Government and shall report its findings concerning the same to the Mayor and Council for appropriate action." Council Rules & Procedures, Section 2.102 (1) Effective January 1, 2011. Adopted by Urban County Council October 14, 2010

Future Meeting Schedule

March 19	June 18	**October 22**
April 30	August 27	November 19
May 28	October 1	December 10

BUDGET & FINANCE COMMITTEE
October 22, 2013
Summary

Ellinger called the meeting to order at 2:32 PM. All members present except Farmer. Akers was recognized as part of the quorum. Clark, Lawless, Myers and Lane also attended.

I. October 1 Committee Summary

On a motion by Beard second Scutchfield the summary of the October 1 Special Budget & Finance Committee was approved unanimously.

II. Monthly Financial Report

Bill O'Mara, Finance Commissioner provided the monthly financial report.
He discussed several economic indicators. He stated that the unemployment rate and other indicators were heading in a positive direction.

O'Mara also addressed the Code Enforcement abatement collections for September.

Melissa Lueker stated that actual revenue was about $ 818,000 ahead of the General Fund budget through September. She also stated that actual expenses were about $ 2.3 million below budget through September, along with a positive variance in transfers for a positive variance of $ 3.3 million.

In response to a question from Lane, Lueker addressed the timing of debt service payments.

In response to a question from Lane, Lueker stated that the positive variance in the Services revenue category was a function of increased Detention Center revenue.

III. Risk Management Review

Patrick Johnston discussed the role of Risk Management. He stated that the goal was to protect assets and resources while reducing risk costs. He discussed staffing and functions of the office.

Johnston discussed excess insurance premiums; LFUCG loss trends; auto damage and liability; general liability; property damage; and Workers' Compensation claims for the past several years.

In response to a question from Ellinger, Johnston stated that the presentation for was information and he didn't have any recommendations.

In response to a question from Ellinger, Johnston discussed the time line for Workers' Compensation claims. He stated that the process can involve several fiscal years.

IV. FY 15 Links

Ellinger stated that the Links discussion would be deferred until the November meeting. He asked Councilmembers to contact him if they had any suggestions for the Links.

In response to a question from Gorton, Ellinger stated that unless Council objected he would like to keep the Links membership to remain the same as this past year.

Meeting adjourned at 2:55 PM.

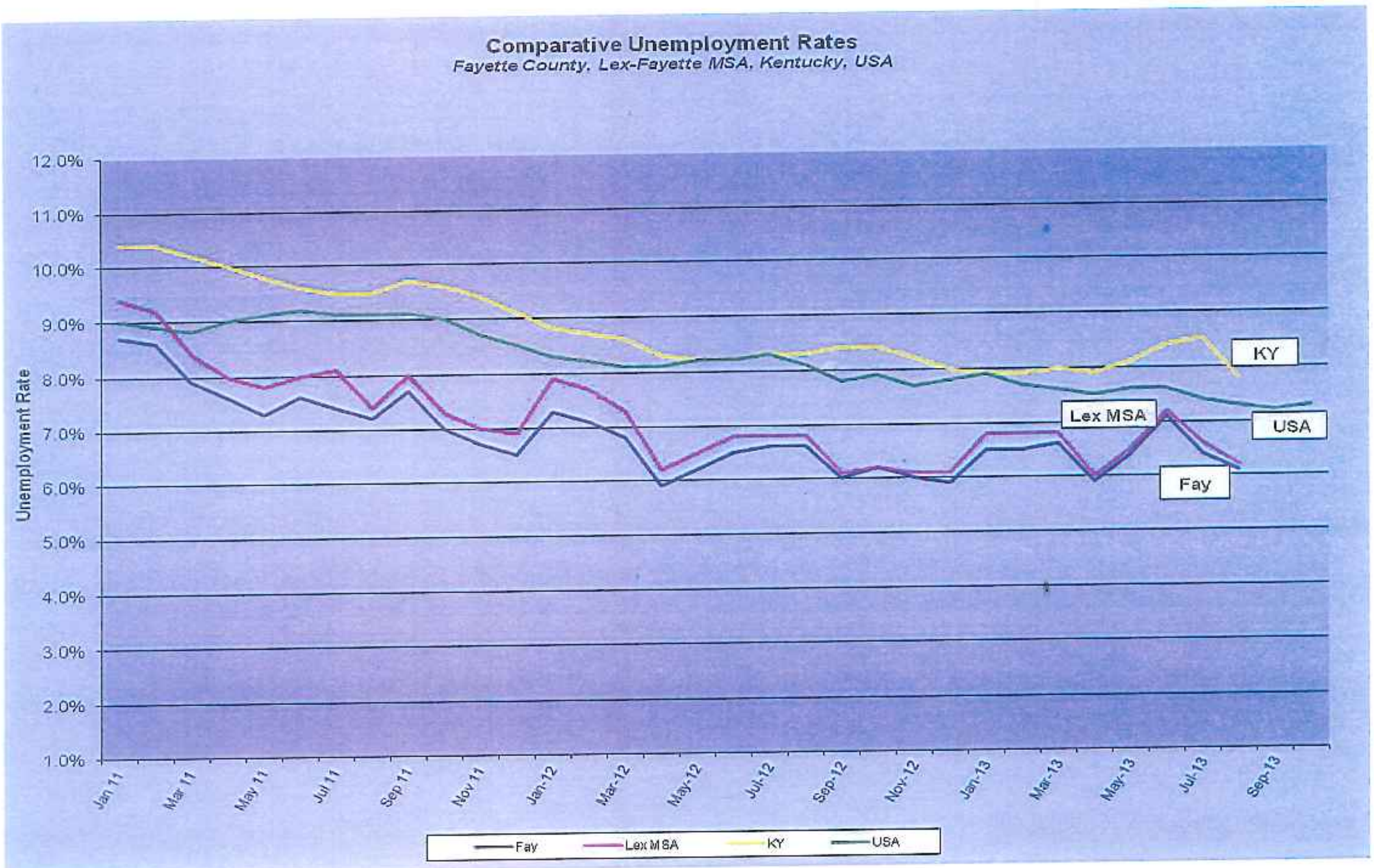
PAS 10/26/13

Budget & Finance Committee

Financial Update

November 19, 2013

Comparative Unemployment Rates



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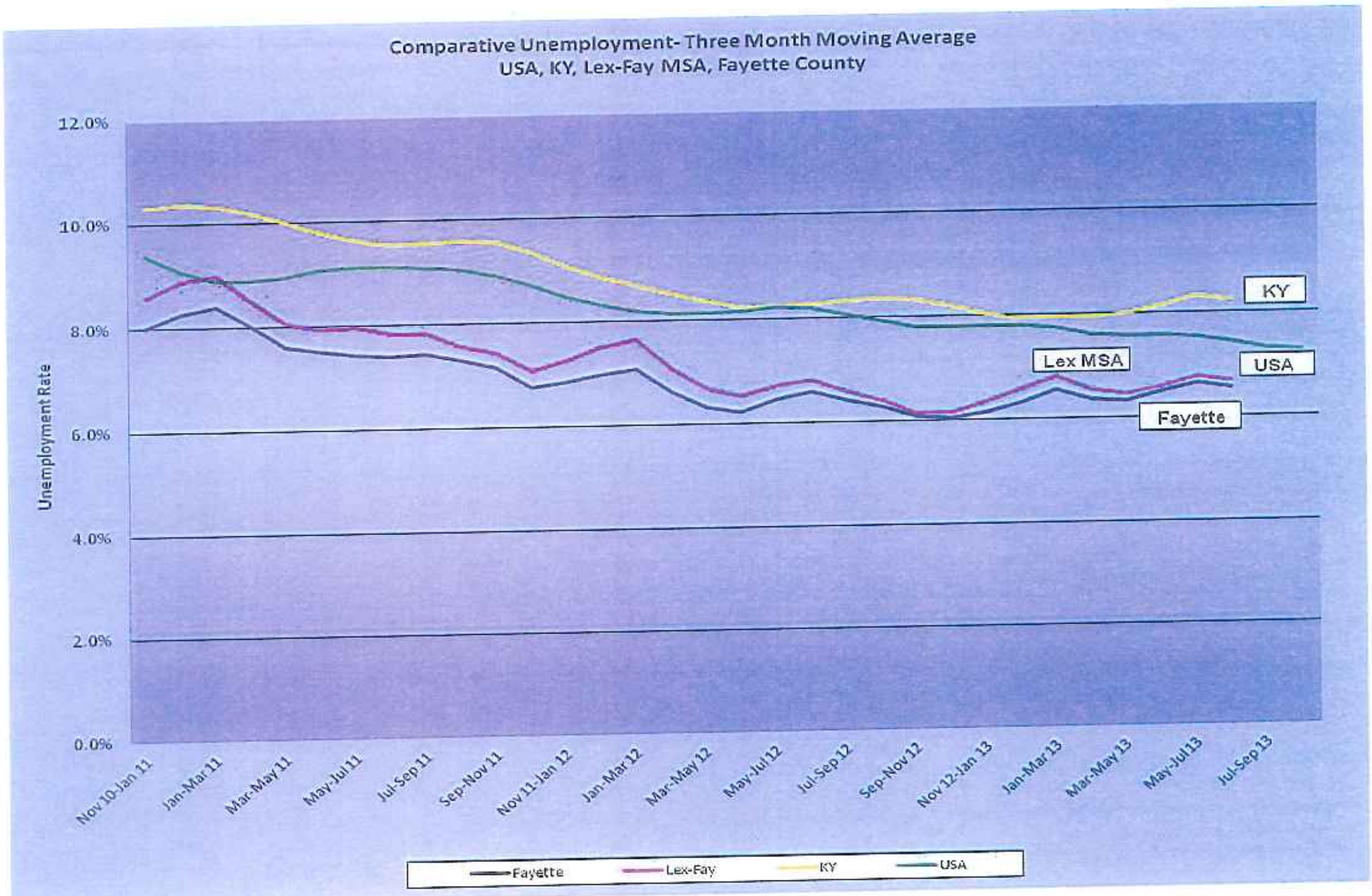
Comparative Unemployment Rates
Three Month Moving Average



Comparison of Economic Indicators 2013 / 2014

Comparison of Economic Indicators

Economic Indicators		Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Fayette Co. Unemployment Rate	2011	8.7%	8.6%	7.9%	7.6%	7.3%	7.6%	7.4%	7.2%	7.7%	7.0%	6.7%	6.5%
	2012	7.3%	7.1%	6.8%	5.9%	6.2%	6.5%	6.6%	6.6%	6.0%	6.2%	6.0%	5.9%
	2013	6.5%	6.5%	6.6%	5.9%	6.4%	7.1%	6.4%	6.1%	N/A	N/A		
Quarterly Fayette County Employment	2011	-	-	169,500	-	-	175,000	-	-	176,500	-	-	179,500
	2012	-	-	174,800	-	-	178,500	-	-	180,700	-	-	183,700
	2013	-	-	178,300	-	-	N/A	-	-	N/A	-	-	N/A
Fayette County Permits Issued	2011	793	786	1,019	1,169	1,187	1,405	1,195	1,292	1,102	1,109	893	726
	2012	929	903	1,169	1,220	1,544	1,492	1,218	1,609	1,064	1,244	1,257	870
	2013	1,169	955	1,131	1,299	1,781	1,490	1,692	1,411	1,201	1,295	-	-
Fayette County New Business Licenses	2011	205	245	446	873	223	199	223	224	223	265	187	128
	2012	183	281	373	718	371	212	209	216	210	254	178	132
	2013	218	258	339	634	456	222	152	218	183	285	-	-
Home Sales (MSA)	2011	328	352	520	586	657	720	614	713	610	512	552	596
	2012	400	448	632	649	783	785	864	850	676	727	673	605
	2013	511	541	758	809	984	956	1,075	1,009	829	N/A	-	-
Fayette County Foreclosures	2011	59	59	40	33	33	39	39	53	25	29	38	33
	2012	71	76	45	68	75	65	61	57	66	92	90	72
	2013	79	44	46	42	38	54	89	52	41	47	-	-

N/A indicates information not available.
BLS Releases Date for Fayette Co. Quarterly Employment - 6 months after quarter end

October 2013 MTD Actual/Adopted Budget

October 2013 Monthly Actual Compared to Adopted Budget

Revenue Category	Actual	Budget	Variance	% Var
OLT- Employee Withholding	8,236,178	10,601,940	(2,365,762)	-22.3%
OLT - Net Profit	1,495,318	1,187,332	307,986	25.9%
Insurance	4,859,926	4,192,269	667,657	15.9%
Franchise Fees	1,334,272	1,234,148	100,124	8.1%
TOTALS	15,925,694	17,215,689	(1,289,995)	-7.5%

October 2013 YTD Actual/Adopted Budget

October 2013 YTD Actual Compared to Adopted YTD Budget

Revenue Category	Actual	Budget	Variance	% Var
OLT- Employee Withholding	49,374,464	51,134,483	(1,760,019)	-3.4%
OLT - Net Profit	5,830,691	6,315,972	(485,281)	-7.7%
Insurance	11,359,643	10,451,999	907,644	8.7%
Franchise Fees	5,738,077	6,329,222	(591,145)	-9.3%
TOTALS	72,302,875	74,231,676	(1,928,801)	-2.6%

October 2013 MTD/October 2012 MTD

Actual Monthly Compared to Prior Year

Revenue Category	Oct '13	Oct '12	Diff	% Var
OLT- Employee Withholding	8,236,178	9,158,179	(922,001)	-10.07%
OLT - Net Profit	1,495,318	1,018,581	476,737	46.80%
Insurance	4,859,926	3,693,432	1,166,494	31.58%
Franchise Fees	1,334,272	410,796	923,476	224.80%
TOTALS	15,925,694	14,280,988	1,644,706	11.52%

October 2013 YTD/October 2012 YTD

Actual YTD Compared to Actual Prior YTD

Revenue Category	Oct '13 YTD	Oct '12 YTD	Variance	% Var
OLT- Employee Withholding	49,374,464	49,796,505	(422,041)	-0.8%
OLT - Net Profit	5,830,691	5,877,785	(47,094)	-0.8%
Insurance	11,359,643	9,572,536	1,787,107	18.7%
Franchise Fees	5,738,077	4,331,639	1,406,438	32.5%
TOTALS	72,302,875	69,578,465	2,724,410	3.9%

FY 2014 Code Enforcement
Nuisance Abatement/Lien Collections

Code Enforcement Lien Collections

Month	Administrative Collection Fees		Miscellaneous		Penalty & Interest		Total Collections	
	FY 2014	FY 2013	FY2014	FY2013	FY2014	FY2013	FY2014	FY 2013
July	1,875	975	1,366	1,430	35,459	22,987	38,700	25,392
August	1,950	1,676	1,489	959	53,878	15,261	57,317	17,896
September	1,475	975	1,568	573	57,003	11,445	60,045	12,993
October	1,575	2,400	1,305	1,572	38,168	28,214	41,048	32,186
Totals	6,875	6,026	5,727	4,534	184,508	77,907	197,110	88,467

2014 Fiscal Year - Cash Flow Variance
Revenue (Actual to Budget)

For the four months ended Oct 31, 2013

	ACTUAL	BUDGET	Variance
Revenue			
Payroll Withholding	$49,374,464	$51,134,483	($1,760,019)
Net Profit	5,830,691	6,315,972	(485,281)
Insurance	11,359,643	10,451,999	907,644
Franchise Fees	5,738,077	6,329,222	(591,145)
Other Licenses & Permits	1,205,269	955,304	249,966
Ad Valorem	906,060	726,964	179,096
Services	8,685,983	7,165,832	1,520,151
Fines and Forfeitures	88,410	59,558	28,852
Property Sale	19,250	3,095	16,156
Intergovernmental	556,741	453,113	103,628
Investment Income	(33,170)	40,000	(73,170)
Other Financing Sources	50,000	50,000	
Other Income	1,109,792	452,306	657,485
Total Revenue	$84,891,210	$84,137,849	$753,361

2014 Fiscal Year - Cash Flow Variance Expense (Actual to Budget)

For the four months ended Oct 31, 2013	ACTUAL	BUDGET	Variance
Expenses			
Personnel	($55,314,399)	($55,664,284)	$349,885
Operating	(10,961,311)	(13,759,289)	2,797,978
Debt Service	(10,805,107)	(10,805,108)	1
Partner Agencies	(6,303,811)	(6,542,809)	238,998
Insurance - Expense	(1,038,600)	(1,038,600)	(0)
Operating Capital Expenditures	(439,600)	(155,236)	(284,363)
Total Expenses	**(84,862,829)**	**(87,965,327)**	**3,102,498**
Interfund Transfers			
Transfers	(614,783)	(965,310)	350,527
Change in Net Position	**($586,402)**	**($4,792,788)**	**$4,206,386**

2014 Fiscal Year - Cash Flow Variance Revenue (CY to PY)

Current YTD Actual compared to Prior YTD Actual	Oct '13	Oct '12	Variance
Revenue			
Payroll Withholding	$49,374,464	$49,796,505	($422,041)
Net Profit	5,830,691	5,877,785	(47,094)
Insurance	11,359,643	9,572,536	1,787,107
Franchise Fees	5,738,077	4,331,639	1,406,438
Other Licenses & Permits	1,205,269	1,104,113	101,156
Ad Valorem	906,060	852,514	53,546
Services	8,685,983	7,916,829	769,153
Fines and Forfeitures	88,410	128,414	(40,004)
Property Sale	19,250	22,058	(2,807)
Intergovernmental	556,741	665,077	(108,336)
Investment Income	(33,170)	100,982	(134,153)
Other Financing Sources	50,000	50,000	
Other Income	1,109,792	714,411	395,380
Total Revenue	**$84,891,210**	**$81,132,864**	**$3,758,346**

2014 Fiscal Year - Cash Flow Variance Expense (CY to PY)

Current YTD Actual compared to Prior YTD Actual	Oct '13	Oct '12	Variance
Expenses			
Personnel	($55,314,399)	($51,806,641)	($3,507,758)
Operating	(10,961,311)	(10,623,840)	(337,472)
Debt Service	(10,805,107)	(7,694,260)	(3,110,847)
Partner Agencies	(6,303,811)	(5,909,806)	(394,005)
Insurance - Expense	(1,038,600)	(962,529)	(76,071)
Operating Capital Expenditures	(439,600)	(21,830)	(417,770)
Total Expenses	(84,862,829)	(77,018,907)	(7,843,922)
Interfund Transfers			
Transfers	(614,783)	(369,581)	(245,202)
Change in Net Position	($586,402)	$3,744,376	($4,330,778)

Questions ?

16

TO: Budget and Finance Committee

FROM: Department of Law

DATE: November 12, 2013

RE: Outsourcing – Internal Audit
File No. 13-CC0906

MEMORANDUM

This memorandum responds to your request for an opinion concerning whether the Lexington-Fayette Urban County Government (LFUCG) may outsource the Division of Internal Audit.

Internal Audit – A Brief History

LFUCG first created the position of Internal Auditor in 1978. Ordinance No. 297-78 (November 30, 1978) created two internal auditor positions under Chapter 21 of the Code of Ordinances (Classified Civil Service). When originally created, these positions were located in the office of the Chief Administrative Officer. In 1983, the internal auditors who had been hired in 1979 became council staff when Sections 1.301 to 1.304 of Appendix A, Rules and Procedures of the Lexington-Fayette Urban County Council were adopted by Resolution No. 102-83. Those rules established an internal audit unit within the Council Office that operated under the day-to-day supervision of the Council Administrator and under general supervision of the Council as a whole.

In 2000, a proposal was made to create an internal audit program for LFUCG. The most significant changes that grew out of this proposal were (1) the creation of an Internal Audit Board to conduct scheduled or special audits and (2) the creation of the Office of Internal Audit and the transferring of the internal auditors to that office. Ordinance No. 63-2002 established the Internal Audit Board. Thereafter, the Division of Internal Audit was created; it was later renamed the Office of Internal Audit. The Office of Internal Audit is under the direct supervision of the Internal Audit Board, which consists of seven (7) voting members appointed by the Mayor (including the Mayor or his designee, two (2) members of the Urban County Council, and four (4) members from the audit, accounting, or legal professions) and two (2) ex-officio non-voting members (i.e., the Council Administrator and the Chief Administrative Officer).

Internal Audit – Classified Civil Service

All positions in the Office of Internal Audit are Classified Civil Service positions governed by KRS Chapter 67A and Chapter 21 of the Code of Ordinances. KRS Chapter 67A provides that the legislative body of urban county governments shall "fix by ordinance the number and classification of urban-county employees, and the salaries for each classification." See KRS 67A.300(1) and Code Section 21-2(b). However, KRS § 67A.300(2) also provides that, "whenever in the exercise of a reasonable discretion, it shall be the judgment of the legislative body of the urban-county government **that economic necessity requires it**, or that **there is no longer a need for a particular office or position to exist**, the legislative body may abolish said office or position and any officer or employee occupying said office or position may be laid-off or suspended until and if such office or position is re-created or reestablished" (emphasis added). See also Section 21-20(a) of the Code of Ordinances.

Thus, KRS § 67A.300(2) and Section 21-20 link the abolition of civil service positions to "economic necessity" or to the determination that there is "no longer any need for a particular office or position to exist." KRS § 67A.300(3) and Section 21-20(d) provide that any employee aggrieved by the abolition or proposed abolition of his position may, within ninety (90) days, file a petition in Fayette Circuit Court challenging the abolition of his office. If that happens, the burden is placed upon LFUCG "to establish the necessity for and the good faith of the urban county government in abolishing said office or position," KRS § 67A.300(3) and Section 21-20(d) of the Code of Ordinances. Finally, if the office or position is reestablished within one (1) year, any person who was deprived of his position because it was abolished must be restored to the office or position formerly held, see KRS § 67A.300(4) and Section 21-21(a).

Outsourcing May Contradict Economic Necessity and/or
Suggest Continuing Need for the Position, Undermining Layoffs

KRS § 67A.300(2) and Section 21-20(a) of the Code of Ordinances present a significant obstacle to the proposal to abolish classified civil service positions and outsource those functions. If a function is outsourced, such outsourcing would, in and of itself, be evidence that there is a need for the position, undermining the basis for the layoffs required to implement the outsourcing. Furthermore, if LFUCG pays an outside entity at a contract rate to perform a function that has customarily and historically been performed by civil service employees, it may be difficult to demonstrate that the layoffs of those employees was an "economic necessity," since LFUCG will continue to pay for those functions at a contract rate. LFUCG would have to demonstrate, in good faith, that the savings generated by outsourcing are so substantial and the economic condition of LFUCG is such that abolishing the position is an "economic necessity." This may be a difficult burden if the functions of that position have been outsourced by contract.

If you have any questions or need additional assistance, please let me know.

Glenda Humphrey George
Managing Attorney

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Lexington-Fayette Urban County Council

TO: Budget & Finance Committee

FROM: Paul Schoninger
Research Analyst

DATE: November 11, 2013

SUBJECT: Outsourcing Internal Audit Functions

As part of the FY 14 budget deliberations, the General Government link referred the matter of outsourcing Internal Audit functions. As I understand it the link was concerned abort the effectiveness and efficiency of Internal Audit.

Numerous private sector organizations have outsourced internal audits functions. However I could only identify one local government that has outsourced its internal audit function. The City of Stockton, CA has outsourced its interval audit function as part of the City's overall bankruptcy plan.

As part of the review I contacted the Association of Local Government Auditors (ALGA) which is based in Lexington. ALGA represents over 220 internal auditors that work for local government or local school boards.

Both Bill Greene, the President of ALGA, who is the City Auditor with the City of Phoenix, AZ; and Jay Poole, Director of Auditing, Chesapeake, VA offered useful advice regarding creating and managing a cost effective public sector internal audit function. They offered alternatives to outsourcing the internal audit functions.

Mr. Poole reviewed several of the audits found on our web site as well as the Quality Assessment Review a self assessment exercise that the Internal Audit staff went through last year.

Mr. Poole expressed some concerns about the depth, breadth and effectiveness of some of the audits that he reviewed and offered a few suggestions including:

1. Using ALGA standards instead of the Institute of Internal Auditors (IIA) Standards that the Office presently uses. He stated that the IIA is geared toward the private sector, while ALGA is specifically utilized for local governments. Poole stated that the findings and recommendations of audits using ALGA standards would be stronger and more appropriate that those offered under IIA standards. He stated that the ALGA standards are based on

Budget & Finance Committee
Outsourcing Internal Audit Functions
November 11, 2013
Page Two

the "Yellow Book", developed by the US Government Accountability Office GAO. The GAO is the investigative arm of the US Congress. The Yellow Book "provides a framework for conducting high quality audits with competence, integrity, objectivity, and independence. " The Yellow Book is for use of government entities, entities that receive government awards and other public organizations performing audits.

2. A cost benefit analysis should be included in the Annual Report. This would give policy makers a clear concise view of the effectiveness and efficiency of the Internal Audit office and its audits.
3. Join the ALGA and utilize the peer review exercise offered. He stated that the peer review was much more effective than the self assessment that the Internal Audit office conducts. (Attached is a summary of the last peer review that Chesapeake VA undertook in June 2011.

Mr. Greene also suggested that an attempt be made to merge or combine functions within Internal Audit and Risk Management office. He stated that both offices are concerned with environment and activity control and risk assessment and management.

If, after reviewing this memo and attached materials, you have any questions, comments or need clarification, please don't hesitate to contact me.

Paul Schoninger
Research Analyst

Association of Local Government Auditors

June 9, 2011

Jay Poole, City Auditor
Audit Services Department
306 Cedar Road
P.O. Box 15225
Chesapeake, Virginia 23328

Dear Mr. Poole,

We have completed a peer review of the City of Chesapeake Audit Services Department for the period January 1, 2008 to March 31, 2011. In conducting our review, we followed the standards and guidelines contained in the *Peer Review Guide* published in April, 2008, by the Association of Local Government Auditors (ALGA).

We reviewed the internal quality control system of your audit organization and conducted tests in order to determine if your internal quality control system operated to provide reasonable assurance of compliance with *Government Auditing Standards* issued by the Comptroller General of the United States. Due to variances in individual performance and judgment, compliance does not imply adherence to standards in every case, but does imply adherence in most situations.

Based on the results of our review, it is our opinion that the City of Chesapeake Audit Services Department's internal quality control system was suitably designed and operating effectively to provide reasonable assurance of compliance with *Government Auditing Standards* for audits and attestation engagements during the period January 1, 2008 to March 31, 2011.

We have prepared a separate letter offering suggestions to further strengthen your internal quality control system.

Stuart C. Ford	Ann H. Clark
Team Leader	Team Member
Deputy City Auditor	Senior Auditor
Office of the City Auditor	Municipal Auditing
City of Virginia Beach, VA	City of Roanoke, VA

Association of Local Government Auditors

June 9, 2011

Jay Poole, City Auditor
Audit Services Department
306 Cedar Road
P.O. Box 15225
Chesapeake, Virginia 23328

Dear Mr. Poole,

We have completed a peer review of the City of Chesapeake Audit Services Department for the period January 1, 2008 to March 31, 2011 and issued our report thereon dated June 9, 2011. We are issuing this companion letter to offer certain observations and suggestions stemming from our peer review.

We would like to mention some of the areas in which we believe your office excels:

- The Audit Committee is very complimentary and values the work of the Audit Services Department. The committee itself is knowledgeable concerning audit issues and appears to work well with the department.

- The effort to automate the entire audit process without the use of an off the shelf automated workpaper software package shows both commitment to excellence and consideration of difficult budget times.

- The experience of the audit staff is evident in the quality of the audit reports issued.

We offer the following observations and suggestions to enhance your organization's demonstrated adherence to *Government Auditing Standards*:

- Standard 1.33 requires audit organizations to communicate, as appropriate, to the requestor and those charged with governance, the clarification that the scope of nonaudit work performed does not constitute an audit under GAGAS. We observed during our review this standard was not being addressed under the current procedures.

  We suggest that this requirement be addressed via the NONAUDIT SERVICES WORKSHEET as a line item to the worksheet.

- Standard 7.46 states "auditors should communicate an overview of the objectives, scope and methodology, and timing of the performance audit and planned reporting to management of the audited entity."

  The current procedures include an Initial Opening Conference template which includes a discussion of general audit areas which may be included along with a statement which indicates an additional meeting would be held after the initial planning phase to discuss the specific areas and operations to be audited.

  We suggest the current informal meetings currently being held be documented and included in the workpapers.

We extend our thanks to you, your staff and the other city officials we met for the hospitality and cooperation extended to us during our review.

Sincerely,

Stuart C. Ford	Ann H. Clark,
Team Leader	Team Member
City of Virginia Beach, VA	City of Roanoke, VA

Chesapeake
VIRGINIA

Audit Services Department
306 Cedar Road
Post Office Box 15225
Chesapeake, Virginia 23328
(757) 382-8511
Fax (757) 382-8860

June 9, 2011

Stuart C. Ford
Team Leader
Deputy City Auditor
City of Virginia Beach
2401 Courthouse Drive, Room 344
Virginia Beach, Virginia 23456

Dear Mr. Ford:

We have reviewed the conditions and recommendations from your ALGA Peer Review Committee's external quality control review of the City of Chesapeake Audit Services Department for audits conducted during the period January 1, 2008 through March 31, 2011. Enclosed is the response to your management comments. We have already implemented both recommendations.

Recommendation:

- Standard 1.33 requires audit organizations to communicate, as appropriate, to the requestor and those charged with governance, the clarification that the scope of nonaudit work performed does not constitute an audit under GAGAS. We observed during our review this standard was not being addressed under the current procedures.

  We suggest that this requirement be addressed via the NONAUDIT SERVICES WORKSHEET as a line item to the worksheet.

Response:

This recommendation has been implemented. We have added the following line to the Nonaudit Services Worksheet:

"E. Does the requesting management entity or City Council need to be advised that work performed does not constitute an audit under GAO Standards?"

Recommendation:

- Standard 7.46 states "auditors should communicate an overview of the objectives, scope and methodology, and timing of the performance audit and planned reporting to management of the audited entity."

  The current procedures include an Initial Opening Conference template which includes a discussion of general audit areas which may be included along with a statement which indicates an additional meeting would be held after the initial planning phase to discuss the specific areas and operations to be audited.

  We suggest the current informal meetings currently being held be documented and included in the workpapers.

Response:

This recommendation has been implemented. The Initial Opening Conference template has been revised to include a "Subsequent Audit Plan/Audit program Comments section that documents audit plan or audit program comments or adjustments made during the course of the audit.

Thank you and Ann again for your hard work, thoughtful insight, and valuable assistance on this peer review. Please call if you have questions.

Sincerely,

Jay Poole

Jay Poole
City Auditor
City of Chesapeake, Virginia

cc: Ann H. Clark, Team Member
Paul Geib, ALGA Peer Review Coordinator

OFFICE OF INTERNAL AUDIT
Providing Value to the LFUCG

Presented by Bruce Sahli, CIA
Director of Internal Audit

Introduction

- The Office of Internal Audit (OIA) was formed in 2002 by the Urban County Council at the recommendation of the external auditors.
- The Director of Internal Audit reports operationally to the Internal Audit Board and administratively to the CAO. This reporting arrangement ensures the independence of the OIA in selecting audits and conducting audits, and communicating results.

Internal Audit Board

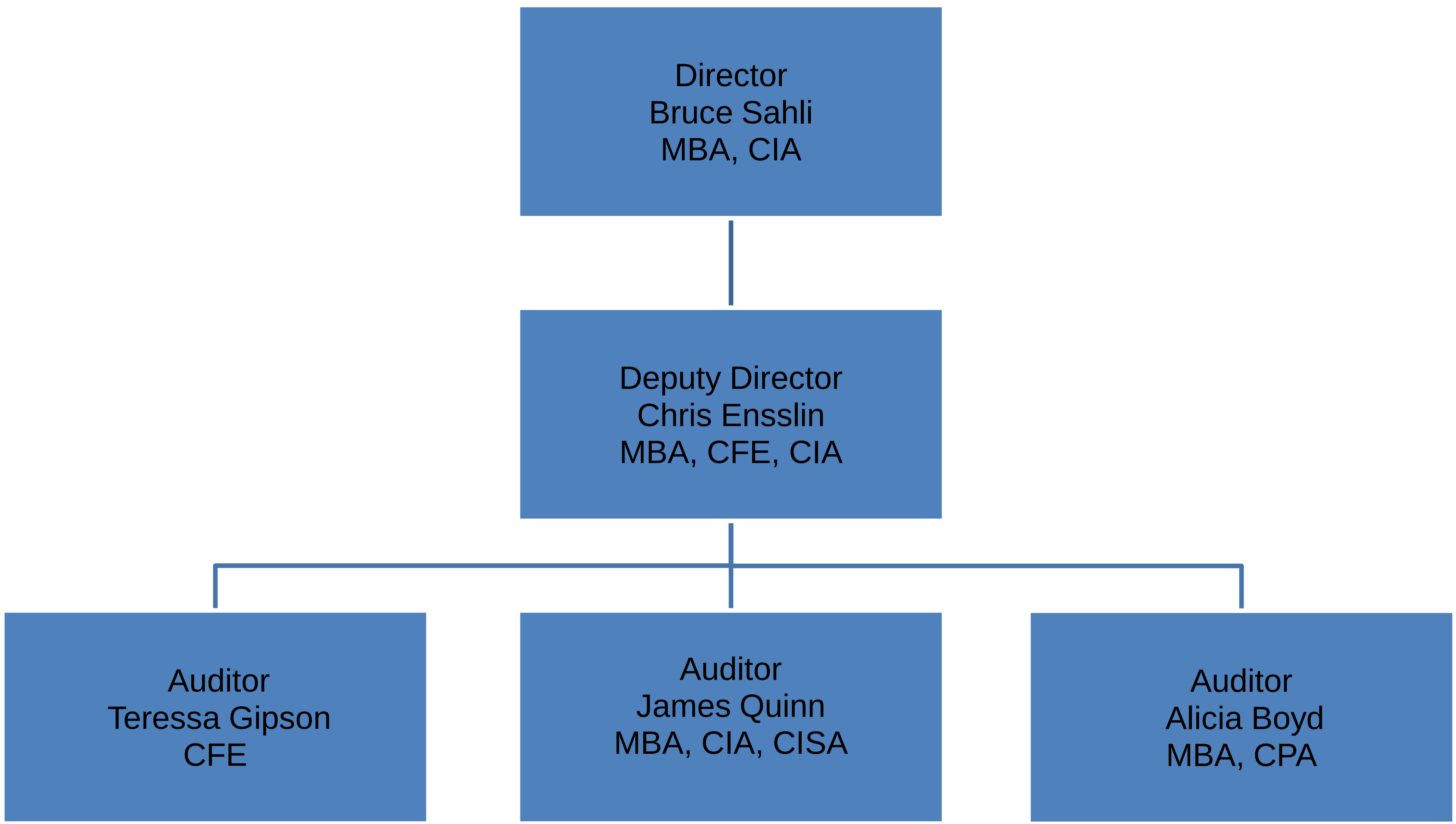
- The Internal Audit Board contains seven voting members:
  - Jennifer Burke, Partner with Crowe Horwath, CPA, Certified Risk Professional, Certified Fraud Specialist, AICPA Certified in Financial Forensics
  - Gary Ludwick, retired FBI Supervisory Special Agent and CPA
  - Fred Brown, CPA, Partner of Brown & Dougherty, former 8th District Council member
  - Gwen R. Pinson, Attorney with Stoll Keenon Ogden PLLC, former General Counsel of the Finance and Administration Cabinet
  - Ed Lane, Council Member
  - Julian Beard, Council Member
  - William O'Mara, Commissioner of Finance & Administration , CMA

Internal Audit Board

- The Internal Audit Board also contains two non-voting Ex-Officio members:
  - Sally Hamilton, CAO
  - Stacey Maynard, Council Administrator

- Honkamp Krueger & Company, CPAs & Business Consultants, performed a quality assessment of the Louisville Metro Government Office of Internal Audit and specifically identified the LFUCG Internal Audit Board as an innovative practice.

Office of Internal Audit



Quality Control

- Quality Self Assessments were conducted in 2007 and 2012 to ensure compliance with the IIA Standards. The results were validated by an independent CIA/CPA. The OIA received the highest possible compliance rating in both QSAs.

Internal Audit Services

- The OIA conducts audits selected via a risk assessment process, as well as special requests received from the Administration and Council. The OIA also conducts periodic on-site follow-up reviews to determine that management has implemented action plans to address audit findings.
- Since October 2006 OIA has issued 68 reports containing 385 findings with recommendations for management consideration.

Best Practices

- The OIA uses ACL audit software for data mining and the identification of potentially inappropriate transactions.
- The OIA developed the LFUCG Ethics Tip Line based on a recommendation from the State Auditor and is responsible for Tip Line administration. The Tip Line was approved by the Board and funded by the Urban County Council.

Examples of Significant Audit Results

- An OIA report issued in 2004 identified 106 golf course deposits totaling $106,366 that were never accounted for. The missing deposit activity ended on the same day it was announced an internal audit was being conducted.
- An OIA report issued in 2005 identified a Waste Management practice where employees were paid significant amounts of overtime that was not actually worked. This audit resulted in the significant reduction of future Waste Management overtime costs.
- An OIA report issued in 2009 identified $1.2 Million held in a Community Corrections discretionary account unknown to the Administration and Council. These funds were subsequently transferred to the LFUCG General Fund, with all future revenue from the discretionary account being applied to the General Fund.

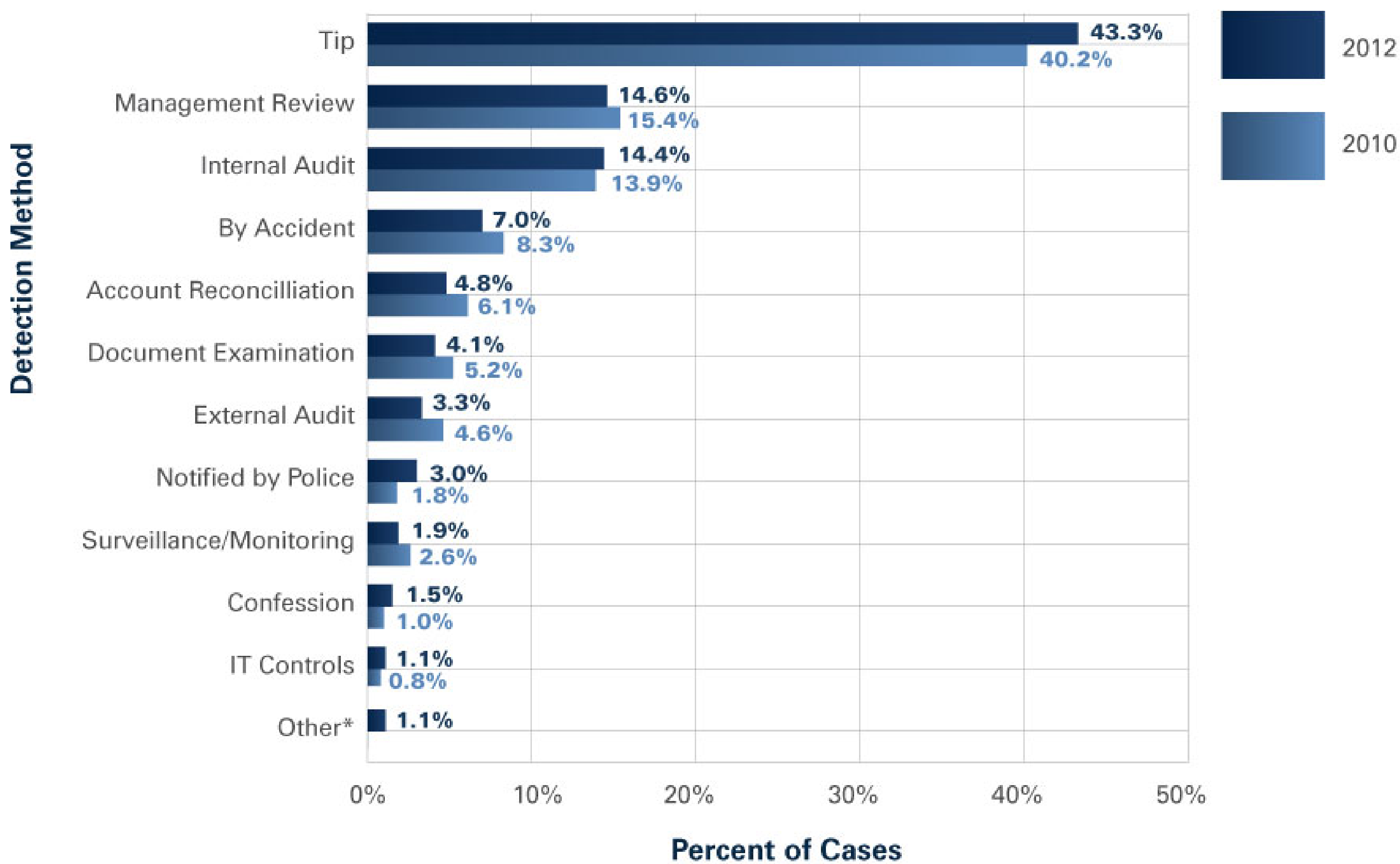
Examples of Significant Audit Results

- An OIA report issued in 2009 identified expenditure issues, appearances of a conflict of interest, improper use of a library laptop, and significant IT control issues at the Lexington Public Library.
- An OIA report issued in 2013 identified the need for a CAO Policy addressing LFUCG-wide inventory control issues.
- The OIA identified PeopleSoft as a significant potential risk to LFUCG's objectives and operations and in 2013 co-sourced with Protiviti to conduct a comprehensive audit of PeopleSoft.

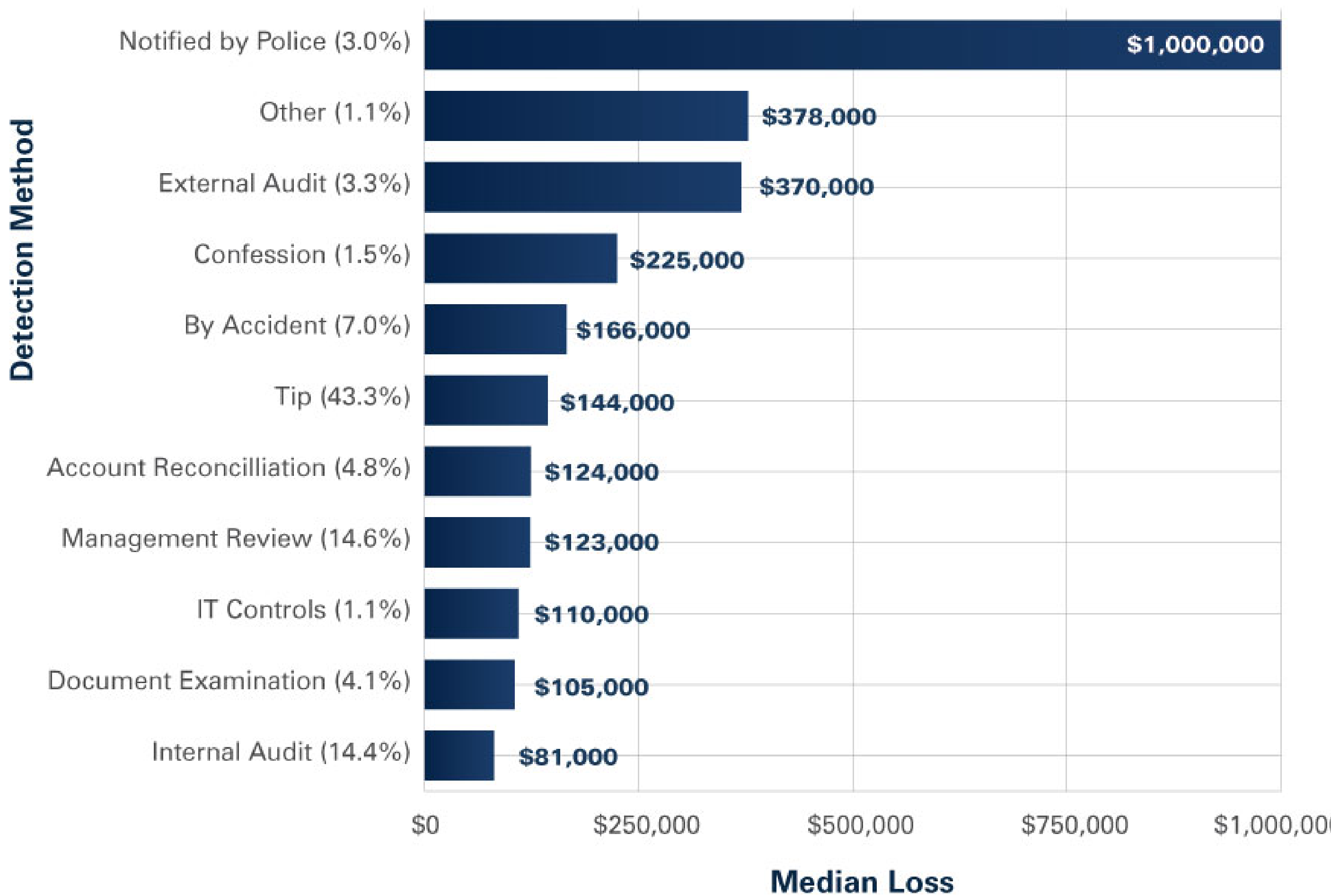
Covington, KY Embezzlement

- In August 2013 the Cincinnati Enquirer reported that the city of Covington, KY had suffered a $600,000 embezzlement perpetrated by their former Finance Director.
- The Covington City Commission is now in the process of hiring an internal auditor.
- OIA routinely audits for incompatible duties and the lack of sufficient controls which could prevent or detect incidents such as the one experienced by Covington.

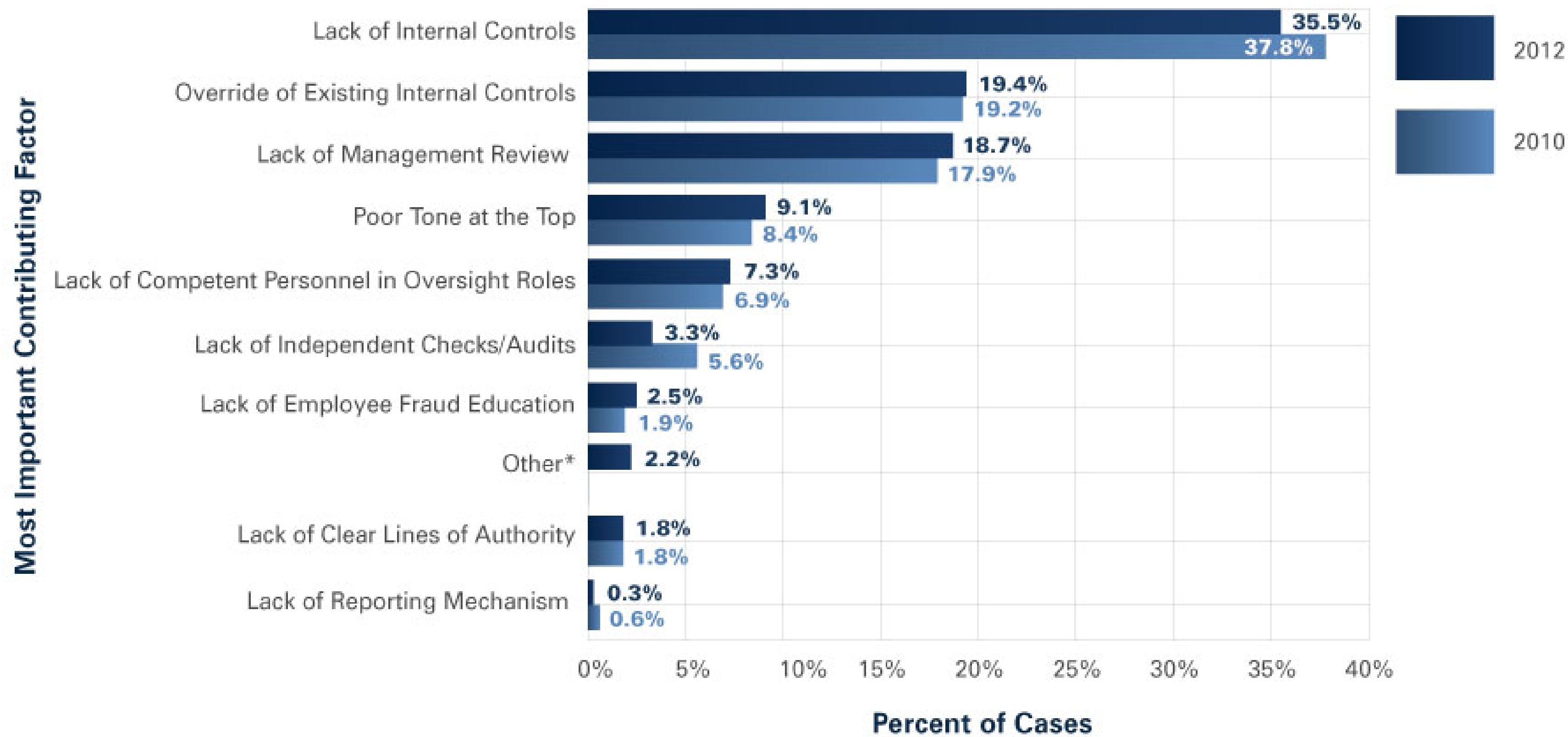
Reducing Fraud Risk



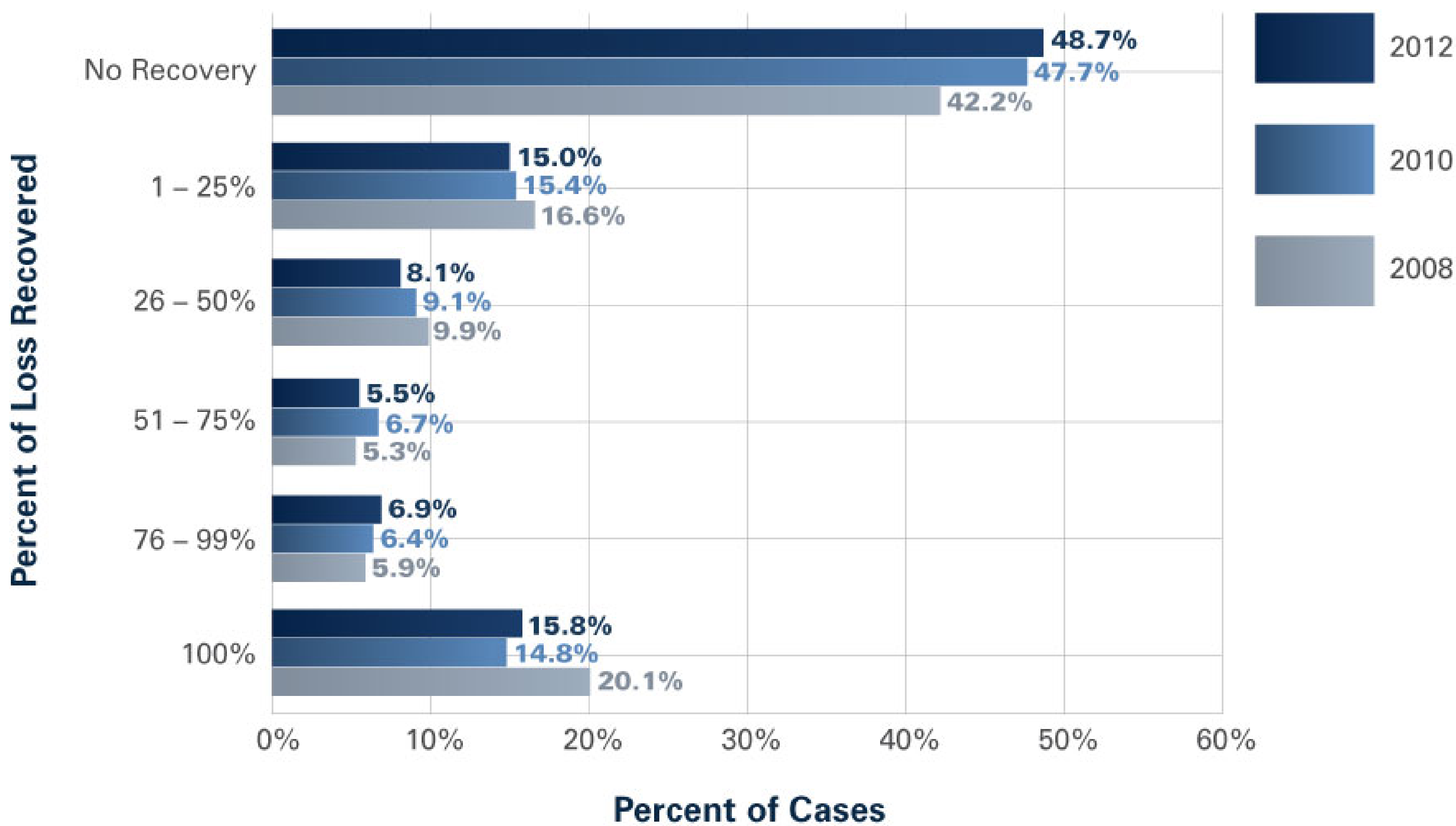
Reducing Fraud Risk



Reducing Fraud Risk



Reducing Fraud Risk



Reducing LFUCG’s Financial & Reputational Risk

- The OIA audits all LFUCG funds when the risk assessment process, special requests, or Tip Line allegations justify it. The OIA isn’t limited to General Fund audits.
- OIA’s FY 2014 total budget is approximately 1/10 of 1% of LFUCG’s total annual budget.

Questions?

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258-3286

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2014 INTERNAL AUDIT PLAN

Approved by the IA Board on November 12, 2013

TIER ONE

PeopleSoft Payroll Financial Transaction Audit - Utilize PeopleSoft queries and other resources to examine payroll transactions in the PeopleSoft environment. Evaluate anomalies and outliers and report exceptions to management for resolution. This audit is dependent on the availability of Enterprise Solution staff and other IT staff as needed to assist in the extraction of data for analysis, etc.

Revenue Collections Allocated Properly to the Various Funds – This audit will examine the allocation of revenues to the various LFUCG funds for proper allocation to the appropriate funds.

Accounts Payable Continuous Monitoring - Using the analytics that IA, ACL, and Metaformers developed; identify possible duplicate payments. Determine if false positives can be reduced thereby making it more efficient and effective for doing this on a quarterly, semi-annual, or annual basis.

Form I-9 Audit – This audit will examine employee files for evidence that Form I-9's are properly filed and any re-verification requirements are met.

TIER TWO

PeopleSoft Review - Based on Protiviti audit results, OIA will seek external funding for continued outsourced audit services regarding the PeopleSoft system.

Procurement Card Audit - This audit would examine controls related to the use of procurement cards by LFUCG personnel.

Social Media Audit - This audit will evaluate the opportunities and risks of social media, determine if social media is being used as a tool and it is being monitored properly, are we complying with Federal Trade Commission guidelines, determine if tracking metrics were implemented, and determine if tracking metrics implemented are the right ones.

Community Corrections IT Security & Maintenance - This audit will examine the security policies of IT, physical security of hardware, and software change management & version control practices.

TIER THREE

Police Confiscated Fund - Examine use of this fund for compliance with applicable federal and state regulations and efficient use of funds, for appropriate accounting of funds received via the federal and state programs, etc.

Employee Workers Comp and Sick Pay Match Audit – This audit would examine Workers Comp and Sick Pay files for simultaneous payments to employees for Workers Comp and Sick Pay, etc.

MANAGEMENT PROGRESS ON THE IA RECOMENDATIONS FROM PREVIOUS AUDITS:

- PeopleSoft Management Progress (based on recommendation for additional OIA audit work from Protiviti report). Time Budget Estimate = 250 hours
- Engineering Collections - Time Budget Estimate = 120 hours
- New Development Process - Time Budget Estimate = 120 hours
- Golf Operations - Time Budget Estimate = 120 hours
- Inventory Control Process - Time Budget Estimate = 120 hours
- Change Order Process - Time Budget Estimate = 120 hours
- Revenue Tax Gap - Time Budget Estimate = 120 hours
- Material Recycling Facility - Time Budget Estimate = 120 hours
- Inmate Accounts - Time Budget Estimate = 120 hours
- Building Inspection Collections - Time Budget Estimate = 120 hours
- Fleet Repair & Maintenance - Time Budget Estimate = 120 hours
- Electronic Recycling Facility (ERF) - Time Budget Estimate = 120 hours
- Municipal Aid Fund (MAP) & County Aid Fund (CAP) - Time Budget Estimate = 120 hours
- G&A Cost Allocation - Time Budget Estimate = 60 hours
- Consent Decree Contracts - Time Budget Estimate = 60 hours
- Family Care Center Collections Process - Time Budget Estimate = 120 hours
- Swimming Pools Collections - Time Budget Estimate = 120 hours

NOTE: This is an aggressive Audit Plan for an audit office the size of LFUCG's, and therefore the completion thereof represents a best case scenario. As has occurred in past years, the carry forward of some of these projects to the next year is a distinct possibility. The estimated hours per project are for general planning and project management purposes only. Actual time to complete a given project could be substantially greater depending on complexities encountered during actual project field work. In addition, the effects of any special project requests as well as the possibility of increased volume of audit activity driven by Ethics Tip Line reports that could be received in 2014 are at present unknown and therefore unpredictable, but could substantially affect the completion of this Audit Plan.

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DEBT MANAGEMENT POLICY

BUDGET AND FINANCE COMMITTEE
NOVEMBER 19, 2013

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AGENDA

- What is a debt management policy?
- Goals of a debt management policy
- LFUCG actions to research best practices
- LFUCG Debt Management Policy

DEBT MANAGEMENT POLICY

- Serves as a guide to LFUCG
  - How LFUCG may issue debt
  - The types of acceptable debt
  - The level of debt the government can support
- Intended to establish guidelines regarding
  - The purpose, type, and structure of debt
  - Method of sale
  - Usage
  - Maintenance of debt

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GOALS OF THE DEBT MANAGEMENT POLICY

- Improve the quality of decisions
- Provide guidelines for the structure of debt issuance
- Demonstrate a commitment to long-term capital and financial planning
- Assure rating agencies and capital markets of good government

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LFUCG DEBT POLICY

- Researched the GFOA 2003-2012 Best Practice Paper on Debt Management Policy
- Consulted with the University of Kentucky Gatton School
- Reviewed published city debt management policies

LFUCG DEBT MANAGEMENT POLICY

1. Credit Quality
   - Maintain or improve on a 'AA' rating
2. Purposes for Issuing Bond Debt
   - Acquisition or construction of capital projects
3. Types of Debt Permitted and Criteria for Issuance
   - General Obligation
   - Revenue
   - Special Assessments (TIFs)

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LFUCG DEBT MANAGEMENT POLICY

4. Debt Structures
   - Terms
   - Front loading / back loading
   - Variable debt
   - Synthetic debt (derivatives)
5. Methods of Sale
   - Competitive sale

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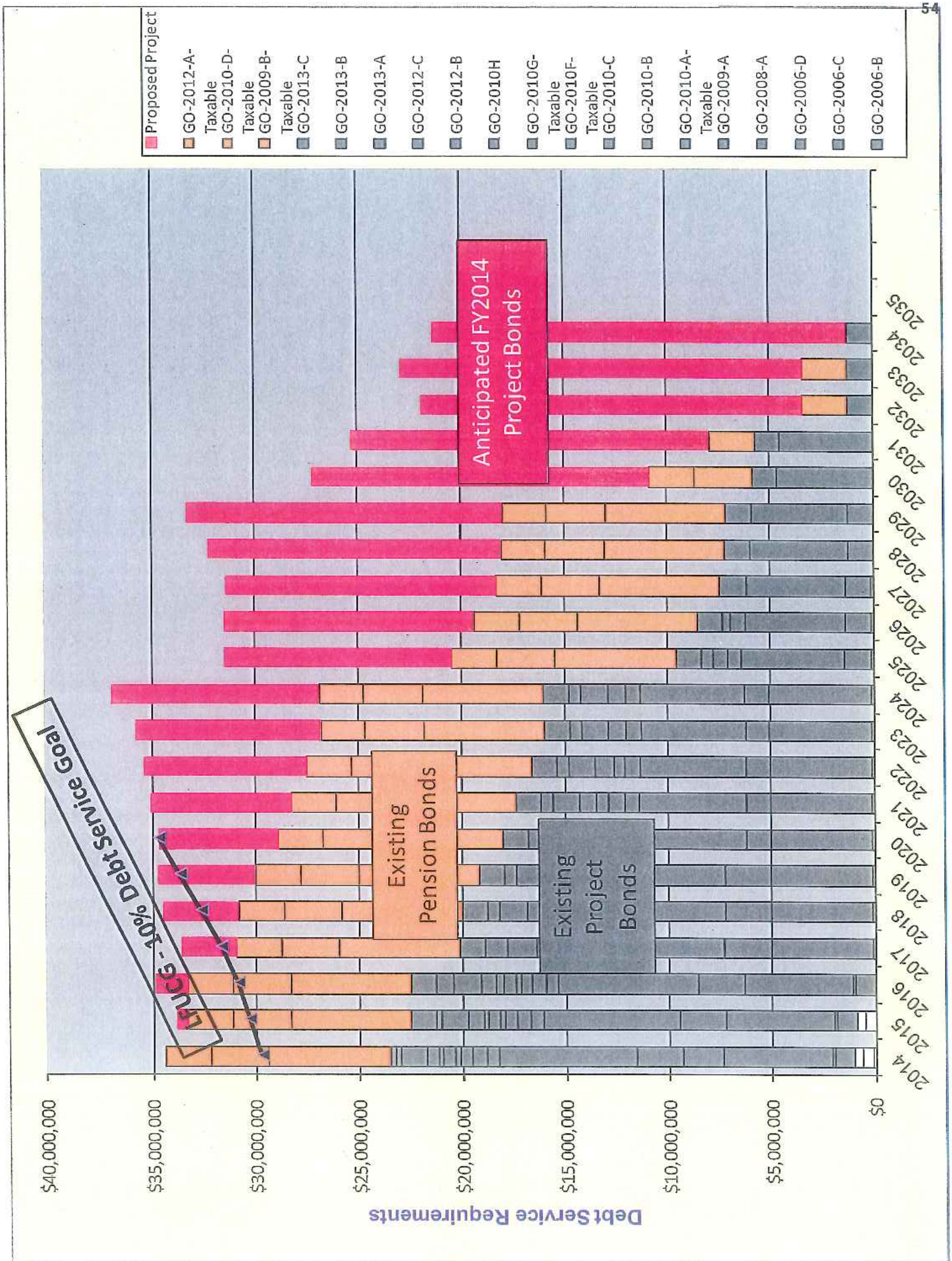
LFUCG DEBT MANAGEMENT POLICY

6. Refunding of Debt
   - Target of 3% savings
   - Avoid extension of debt terms
7. Legal Debt Limits
   - KRS 66.041: 10% of taxable property $2.7 billion
   - Revenue debt not subject to debt limitations
8. Affordability/Capacity Target
   - 10% Debt service as % of *operating expenditures*
   - 10%Debt service as % of *recurring revenue*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Debt Service Requirements
$40,000,000
$35,000,000
$30,000,000
$25,000,000
$20,000,000
$15,000,000
$10,000,000
$5,000,000
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LFUCG - 10% Debt Service Goal
Existing Pension Bonds
Existing Project Bonds
Anticipated FY2014 Project Bonds
Proposed Project
GO-2012-A-Taxable
GO-2010-D-Taxable
GO-2009-B-Taxable
GO-2013-C
GO-2013-B
GO-2013-A
GO-2012-C
GO-2012-B
GO-2010H
GO-2010G-Taxable
GO-2010F-Taxable
GO-2010-C
GO-2010-B
GO-2010-A-Taxable
GO-2009-A
GO-2008-A
GO-2006-D
GO-2006-C
GO-2006-B

Questions

Ad Valorem Tax Refunds – Special Tax Districts

During the merger process most property within the old city limits of Lexington was placed in the full urban service area tax district, which includes all 3 of the special ad valorem taxes – street lighting, garbage and refuse collection, and street cleaning.

New Development

LFUCG has had a long-standing policy that all new development will be brought into the full urban service area tax district.

Existing Development

Previously developed properties can expand on the existing services provided by LFUCG through a petition-type process to add one or more of the extra ad valorem tax services.

Service Availability

The applicable law requires that the urban county government make available to all of those properties within a special tax district the same kind, type, level and character of services. Section 2.02 of the Urban Charter, KRS 67A.150. This does not mean that the government has to provide special services beyond those which it normally provides to other taxpayers within the district. Nor does it mean that an undeveloped, vacant, and/or abandoned property is entitled to a refund because it is not actively using the service, or that a property owner can refuse to pay the tax because he or she does not want or need the service.

Basis for Refunds/Process

The ad valorem tax refund process is driven by state law. See KRS 134.590. The law requires that each taxpayer individually apply to the LFUCG within two (2) years from the date the payment was made.

Pursuant to the applicable IRS regulations and guidelines, LFUCG is supposed to issue a W-9 form G to each taxpayer who receives a refund of more than $10.

Timing of Services

The LFUCG uses January 1st as the date of assessment for all ad valorem real property taxes. However, the taxes actually fund LFUCG's operations on a fiscal year basis

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commencing on July 1st of each year. This means that properties being brought into a special tax services district should be established by January 1st, but that LFUCG is not required to provide any actual services until July 1st of that same year. As a result, there would be no basis for a refund for services not being provided by LFUCG during the first 6 months of the calendar year in which a property was brought into the special tax district.

<u>Street Lights</u>

Of the 3 types of special taxes assessed by LFUCG – street lighting, street cleaning, and garbage and refuse collection - LFUCG has historically provided ad valorem tax refunds to property owners on the basis that street lights have yet to be installed within the immediate vicinity of their property.

A variation from this practice would have to be given careful consideration, as there is a fundamental argument that the taxpayer is entitled to receive the same kind, type, level and character of services as other taxpayers within that district.

<u>Garbage and Refuse Collection</u>

Service availability within a new development scenario is potentially more complicated in that it is sometimes the case that there are a limited number of properties actually availing themselves of the service at any given time until the development is completed. However, the applicability of the tax is based upon the service being made available by LFUCG to parcels within the development - it is not driven by how many of the properties actually generate garbage, trash or debris.

<u>Street Cleaning</u>

With respect to new development, street cleaning appears to be the most potentially complicated service in terms determining service availability. This is primarily due to the issues presented in instances where the developer has yet to complete the final improvement to a street (i.e. the final layer of asphalt) and/or has not yet released a particular street to be maintained by LFUCG. These issues can create a situation where it is not safe to operate the equipment, and as result that particular street(s) is not cleaned.

FY 14 Council Links

	Finance/Social Services	General Services	Public Works/Environmental Quality	General Government	Public Safety
Members	Ford **Beard** Akers	Gorton **Clarke** Mossotti	Kay **Farmer** Stinnett	Myers **Ellinger** Lawless	Lane **Henson** Scutchfield
Holdovers	Beard, Ford		Farmer		Henson
What it Reviews **General Fund**	Finance Social Services Non Departmental	General Services Planning & Development	Public Works & Env Quality	Council Mayor CAO Internal Audit Law Constitutional Offices	Public Safety: Police Fire DEEM E911 Corrections
Partner Agencies	SS Agencies Finance Agencies CD Agencies	Economic Development Agencies: Commerce Lexington Downtown Arts Center Downtown Lexington Corporation KY Workd Trade Center SCORE Lyric Theatre Bluegrass Area Development Authority Lexington Center Corporation Downtown Development Authority Lexington Convention & Visitors Bureau	EQ Partner Agencies	Public Library Constitutional Offices: Circuit Judges County Clerk County Clerk Elections Board of Elections Commonwealth Attorney County Judge Executive County Attorney Coroner Property Valuation Administrator	
Capital	Capital	Capital	Capital	Capital	Capital
Other Funds	Urban Services Tenant Relocation Fund Sanitary Sewer Public Facilities Water Quality Landfill Extended School Fiduciary Insurance Fund	Urban Services Sanitary Sewer Public Facilities Water Quality Landfill Extended School	Urban Services MAP CO Aid Mineral Severance Coal Severance Miscellanous Revenue Fund Sanitary Sewer Water Quality Landfill Right of Way	Urban Services Sanitary Sewer Water Quality Landfill E911 Insurance Fund	Federal Confiscated Assets State Confiscated Assets Public Safety Fund Treasury Confiscated Assets E911

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Budget & Finance Committee Referrals

Item	Referred By	Date Referred	Status
Solid Waste Costs/Revenue/Tax Structure Cost Per Ton; Cost Per Customer Impact of User Fee Structure	Gorton	2-1-11	Waste Management Task Force
Local Vendor Preference*	Gorton	10-14-10	11.29 WS
Minority/Women Business Recruitment*	Stinnett	10-7-10	Procurement Task Force
Purchasing, Procurement & Professional* Service Selection Process	Crosbie/Ellinger	9-24-10	Procurement Task Force
Activity Based Costing/Financial Efficiency	Lane	1-16-12	1.31.12
Affordable Housing Trust Fund Report	Gorton	4-10-12	9.25.12 & 11.27.12
Financial Implications of the Mayor's Homelessness Commission	Kay	1-29-13	2.19.13
Discussion of Fund Balance	Farmer	2-12-13	
Franchise Fees	Gorton	2-26-13	
Risk Management Review	Gen Govt Link/Gorton	8-22-13	
Outsourcing Internal Audit Functions	Gen Govt Link/Gorton	8-22-13	
Debt Management Policy Review	Stinnett	10-22-13	
Refunding Urban Services Property Tax	Stinnett	11-5-13	

* Purchasing related items were also referred to Purchasing & Procurement Task Force

PAS 11-11-13