



ADAM H. EDELEN
AUDITOR OF PUBLIC ACCOUNTS

October 21, 2013

Michael P. Scalise, Mayor
City of Audubon Park
3340 Robin Road
Louisville, KY 40213

Dear Mayor Scalise:

Due to numerous concerns reported to my office, limited procedures were performed to determine whether those concerns warranted a special examination of the City of Audubon Park. These limited procedures identified several weaknesses that are being communicated to you through this letter. We believe the findings noted during the limited procedures were sufficient to assess and evaluate the significant risks brought to our attention. Therefore, we are not expanding our procedures to perform a more detailed special examination at this time.

The limited procedures performed included reviewing accounting detail for certain accounts, reviewing written policies and procedures and documentation supporting certain transactions or events, and conducting interviews with city management. The purpose of this review was not to provide an opinion on financial statements or activities, but to evaluate whether appropriate processes are in place to provide strong oversight of financial activity and to review specific issues brought to our attention.

Detailed findings and recommendations are attached to this letter to assist all parties involved in the City's governance structure to improve internal controls. Overall, these findings indicate weaknesses in policies and procedures that promote accountability, sound fiscal management, and effective communications within the governance structure. We recognize the City has been working toward making improvements internal controls, and believe further improvements in these areas should assist the City by clarifying responsibilities between management and those charged with governance, and providing reassurance to all parties through an improved system of checks and balances. Since these procedures did not constitute an audit or examination, management's response to specific findings were not requested and, therefore, are not contained in this letter. However, we are requesting a written plan for corrective action be provided within 60 days of the date of this letter.

If you have any questions please contact Libby Carlin, Assistant Auditor of Public Accounts, or me.

Sincerely,

A handwritten signature in black ink, appearing to read "Adam H. Edelen".

Adam H. Edelen
Auditor of Public Accounts

C: Members of the City Council

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FINDINGS AND RECOMMENDATIONS

FINDING 2013-01: Funds Collected From Sanitation Fees Were Not Restricted For The Purposes Identified In City Ordinances

The Auditor of Public Accounts (APA) received concerns that the City of Audubon Park (City) overcharged residents for sanitation fees. Upon reviewing financial detail and city ordinances for FY 2011-2013 provided by the City, auditors noted that sanitation receipts collected did exceed direct sanitation expenses for all three years. Below is presented a summary of the receipts and disbursements for the three years reviewed:

	As of June 30		
	2011	2012	2013
Sanitation Receipts	\$ 346,968	\$ 343,440	\$ 345,600
Sanitation Disbursements	183,550	183,550	183,550
Excess Receipts Over Disbursements	<u>\$ 163,418</u>	<u>\$ 159,890</u>	<u>\$ 162,050</u>

The financial detail identified that the sanitation activity was not accounted for in a separate self-balancing fund, but instead deposited into the General Fund. Because of this commingling of sanitation receipts with other general revenue, the specific use of excess sanitation receipts could not be determined since those funds were not separately identifiable within the accounting system. Therefore, it is likely that sanitation funds were utilized, at least in part, for general operating expenses of the City. This use of sanitation receipts does not appear to comply with City ordinances.

Inquiry with City management indicated sanitation rates are based on “the overall budget and charges from previous years for storm damage”. Although it does not appear sanitation receipts may be used for general expenditures to balance the overall budget of the City, storm damage related expenses impacting sewers may be allowable when approved by the Audubon Park City Council (Council). However, currently City ordinances do not appear to permit these expenses.

Ordinance No. 0003 (Series 2011, 2012 and 2013) establishes the sewer rates for the year. These ordinances indicate sanitation fees are assessed to cover the cost of the City’s contract with a private company for its sanitation and recycling program. Although the assessment rates are clearly outlined, and were approved by the Council, it is not clear whether an analysis of projected revenues compared to planned expenses was provided for decision making purposes.

Recommendation

We acknowledge that City management has contracted with an accounting firm to act as the City’s accountant to help improve internal controls over accounting for the sanitation program, including establishing a separate fund to account for sanitation receipts and disbursements. In addition to those changes, we recommend the City:

- Provide the Council an activity analysis report of projected receipts based on the recommended assessment prior to the Council’s vote on the sanitation rates.

FINDING 2013-01: Funds Collected From Sanitation Fees Were Not Restricted For The Purposes Identified In City Ordinances (Continued)

- With the help of the City Attorney, determine other uses of sanitation receipts permitted by law, such as storm damage clean up. Any expense to be funded with sanitation receipts should be clearly explained in the City's sanitation assessment ordinance.
- Provide the Council with a detail report of the sanitation fund activity at least quarterly.

FINDING 2013-02: City Management Should Make Improvements Toward Better Accountability And Transparency To The City Council

Concerns reported to the APA suggested strained relations and questions regarding whether the appropriate level of accountability and transparency existed between the City's management and its Council. Auditors inquired with city management and others, and reviewed activity within certain accounts to determine whether improvements were warranted by City management to ensure its governance structure was conducive for proper accountability. A summary of specific areas of concern is provided below.

- **Municipal Road Aid:** Concerns were noted regarding whether City management properly expended Municipal Road Aid funds. A general review of Road Fund activity for fiscal years 2011-2013 indicated instances in which expenditures appear to be for items other than road maintenance and paving. For instance, auditors noted:
 - FY 2011: ledger detail included expenses for beautification purchases, such as flowers, mulch, etc., as well as transfers reclassifying general public safety expenses to the Road Fund.
 - FY 2012: ledger detail included expenditures for emergency equipment graphics, credit card payments, and sanitation bills payable.
 - FY 2011-2013: ledger detail included significant expenditures for utility payments. Inquiries with City management indicated these payments are street light maintenance, and acknowledged that the utility bill does not separately identify the portion of the bill associated with the lease payment, but instead combined the lease payment with usage charges on the billing statement. The City provided supporting documentation as to how utility usage payments were estimated by the City's external auditor, and indicated these costs were covered by the General Fund. However, the ledger detail indicates utility payments charged to the Road Fund in all three fiscal years reviewed exceeded the lighting maintenance lease payment. For example, in 2012, the utility payments were \$17,750 more than the lease payment stated by City management. Furthermore, a copy of the utility lease was not available for inspection, likely due to the long period of time passed since the inception of the lease.
- **Financial Reporting:** During inquiries with City management, there was acknowledgement that financial reporting provided to Council members in recent years has been confusing, and the reports may not have been conducive to providing the members with sufficient information for proper accountability and oversight. Auditors were further informed that City management, with the help of the recently contracted accountant for the City, has started making improvements in the financial reports provided to the Council each month.
- **Policies and Procedures:** Auditors inquired with City management regarding the existence of an administrative code, or other written policies, to provide details of policies for areas such as fiscal administration, purchasing, delivery of services, and personnel administration.

FINDING 2013-02: City Management Should Make Improvements Toward Better Accountability And Transparency To The City Council (Continued)

City management was able to provide an employee handbook with personnel related policies which is reviewed and approved by the Council, and also policies regarding fiscal administration and purchasing that are approved through executive order. Auditors believe it is important for fiscal policies to not only have executive approval, but also be reviewed and authorized by those charged with governance to ensure proper checks and balances are in place for effective fiscal management. Also, a review of these policies noted weaknesses in that supporting documentation requirements were not always clear to justify procurement decisions, such as in the case for emergency purchases or sole source vendors.

Also, auditors became aware of a weakness in the procedures for updating the City's employee handbook. There does not appear to have been procedures in place for safeguarding the handbook to prevent unauthorized modification to policies. Whereas City management may have authority to modify the employee handbook for certain administrative type functions, other policies required Council approval, such as those related to employee benefits. However, it appears a modification was made to the handbook related to employee retirement benefits beyond what was approved by Council. Inquiry with City management acknowledged that an employee had physical access to the employee handbook, and could have made modifications without proper approval. Further discussion indicated the modification may be related to the Retirement Plan section (4), stating "If an employee continues retirement after twenty (20) consecutive years he or she shall be entitled to receive six (6) months of added retirement for every year employed after the twenty (2) years for up to a maximum of fifteen (15) years." City management was not certain that this language was approved by the Council, and expressed concern as to how this language was inserted into the employee handbook. During our limited procedures, auditors were not able to determine who made the modifications, and did not find sufficient evidence that the Council did or did not approve this policy. However, the lack of controls over modifications to written policy should be improved.

Finally, during inquiry with City management, it was determined that the City did not traditionally have good procedures in maintaining documentation of City Ordinances other than the record of Council meeting minutes. Furthermore, other documents impacting City policies, such as Executive Orders, were not always maintained and easily accessible. However, City management indicated improvement is underway to address at least part of this weakness, and that a plan to codify the city ordinances was under way.

Recommendations

We recommend the following:

- City management and Council develop procedures for an annual plan for the use of Municipal Road Aid funds. Management should follow this approved plan and provide reports to Council detailing actual expenditures. Both parties should familiarize themselves with allowable expenditures for these funds, including clarifications made in opinions of the Office of the Attorney General.

FINDING 2013-02: City Management Should Make Improvements Toward Better Accountability And Transparency To The City Council (Continued)

Recommendations (Continued)

- City management should cease using Road Funds for general operating expenses of the City. If cash shortfalls necessitate inter-fund borrowing for budgetary purposes, policies should be in place to establish the level of approvals required, and procedures should ensure that any such inter-fund borrowing is properly reflected in the City's financial statements and the funds are repaid from the appropriate fund as soon as possible.
- City management should contact its utility provider to renew its lighting maintenance lease so both parties have a current understanding of the terms of the agreement, and also to permit the City management and Council to determine whether the lease is still the best option for the City. Furthermore, if the lease continues, City management should work with the utility provider to ensure the lease payment is segregated from usage charges in its bill.
- We acknowledge City management has hired a contract accountant to provide additional expertise to the City's fiscal management, and that improvements have already been made to the financial reporting provided to the Council. We encourage these improvements to continue, and for the Council to provide feedback to City management if additional information or clarification is needed.
- City management and Council should consider appointing a work group or subcommittee to review the accounting and financial policies. The work group should ensure these administrative policies reflect current policies in place, and should consider whether additional policies are needed for effective accountability and oversight. If so, the work group should make such recommendations to the Council.
- City management should immediately establish procedures for the physical security of the employee handbook and other written policy documents to avoid unauthorized modifications. Policies should be implemented by which certain individual(s) given authorization to make modifications do so only with appropriate written authorization in hand, such as a signed City ordinance or executive order. Modification dates of the document should be identified within the document to permit easy determination of the policy in place at a specific moment in time. Draft documents, such as proposals to Council, should be maintained separately from the enacted handbook, and should be clearly labeled "Draft" to avoid confusion.
- City management and Council should work with a City attorney to identify and remove all unauthorized language in the employee handbook. Changes to the handbook resulting from this review should be communicated to all employees.

FINDING 2013-02: City Management Should Make Improvements Toward Better Accountability And Transparency To The City Council (Continued)

Recommendations (Continued)

- We recognize the City has plans to codify City ordinances. We further recommend policies be implemented to improve maintenance, accessibility, and communication of all executive orders to those charged with governance and employees impacted.

FINDING 2013-03: The City Should Work With The City Attorney To Make A Final Determination Of Retirement Related Liabilities

The APA received concerns that City management entered into a retirement agreement with a former employee that may have violated City policies. Auditors were provided the retirement agreement for the former employee, and compared it to the City employee handbook provided as being the one in effect at the time the retirement contract was signed. Based on this review, we noted the following:

- The employee handbook indicates the employee is entitled to retirement benefits of 60% of gross salary during his last full calendar year of employment for a 10-year period. The employee's retirement contract contains similar language, although it has a typo in which it states the employee is to receive "fifty percent (60%)" of his or her gross salary during the last full calendar year of employment.
- The employee handbook states, "If an employee continues employment after twenty (20) consecutive years he or she shall be entitled to receive six (6) months of added retirement for every year employed after the twenty (20) years for up to a maximum of fifteen (15) years." The contract does not contain such language. Furthermore, as noted in Finding 2013-02, City management expressed concerns that this language in the employee handbook may have not been authorized by the Council. Auditors were not able to determine who made the modification to the employee handbook, but City management acknowledged that more than one person had the ability to make this change, including the former employee.
- Auditors also obtained a memo from the City Mayor notifying the City clerk of the retirement of the former employee. The memo states that the former employee should receive retirement benefits for 15 years, instead of the 10 years identified in the employee handbook. The Mayor acknowledged the memo is in error, and that the employee contract does have the accurate timeframe per the Council's intention. The Mayor further acknowledged that although he signed the memo, he was not its author, and that the questionable language from the employee handbook may have led to confusion. Auditors noted that even under the terms of the language in question, the former employee would not be entitled to 15 years of retirement, but instead 12.5 years. The Mayor acknowledged this error.

Recommendations

Due to the circumstances of this situation, auditors were unable to make a determination as to the appropriate retirement benefit calculation for the former employer. Although the memo from the Mayor does not appear to be a binding document but only administrative instruction, the question outstanding is in regards to the employee benefit policies in effect at the time of the former employee's retirement. As noted above, it appears that the contract in place with the employee is for a 10 year retirement benefit, but the impact of the other circumstances of this situation should be considered. We recommend the City work with its attorney to make a final determination.