



**Audit of Orange County
Utilities Capitalized
Labor Process**



**Phil Diamond, CPA
County Comptroller
Orange County, Florida**

www.occompt.com



Report 473
January 2019

County Audit Division

Christopher J. Dawkins, CPA, CIA
Director

Wendy Kittleson, CISA, CIA
Deputy Director

Audit Team

Sheila M. Roberts, CPA, CFF, CIA
Audit Supervisor

Deborah W. Owens, CPA
Audit Supervisor

Orange County Comptroller's Office

Mission

The mission of the Orange County Comptroller's Office is to serve the citizens of Orange County and our customers by providing responsive, ethical, effective, and efficient protection and management of public funds, assets, and documents, as specified in the Florida Constitution and Florida Statutes.

Vision

The vision of the Orange County Comptroller's Office is to be recognized as a highly competent, cohesive team leading the quest for continuing excellence in the effective safeguarding and ethical management of public funds, assets, and documents.



TABLE OF CONTENTS

TRANSMITTAL LETTER	1
EXECUTIVE SUMMARY	2
INTRODUCTION	4
BACKGROUND	4
AUDIT SCOPE.....	6
AUDIT OBJECTIVE	6
AUDIT METHODOLOGY	6
OVERALL EVALUATION.....	7
RECOMMENDATIONS FOR IMPROVEMENT	8
1. ACCURATE WAGE AND OVERHEAD RATES SHOULD BE UTILIZED IN THE COMPUTATION OF CAPITAL LABOR COSTS	8
2. WATER DISTRIBUTION EMPLOYEES' CAPITALIZED LABOR HOURS SHOULD BE ADEQUATELY SUPPORTED	9
3. UTILITIES SHOULD LIMIT OVERTIME HOURS	11
ACTION PLAN	14



OFFICE OF THE COMPTROLLER

ORANGE
COUNTY
FLORIDA

PHIL DIAMOND, CPA
County Comptroller
County Audit Division
109 East Church Street, Suite 220
Post Office Box 38
Orlando, FL 32802
Telephone: 407-836-5775
www.occompt.com

January 16, 2019

Jerry L. Demings, County Mayor
And
Board of County Commissioners

We have conducted an audit of the Orange County Utilities Department's capitalized labor process. The audit was limited to a review of controls related to the capitalization of employee labor costs allocated to capital asset projects. The period audited was October 2015 through December 2016.

We conducted this audit in accordance with generally accepted government auditing standards. Those standards require that 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 provides a reasonable basis for our findings and conclusions based on our audit objectives.

Responses to our Recommendations for Improvement were received from the Assistant Director of the Utilities Department and are incorporated herein.

We appreciate the cooperation of the personnel of the Utilities Department during the course of the audit.

Phil Diamond, CPA
County Comptroller

c: Byron Brooks, County Administrator
Ray Hanson, Director, Utilities Department
Timothy Armstrong, Assistant Director, Utilities Department



Why This Audit Is Important

The Orange County Utilities Department (Utilities) provides utilities services including water, wastewater, and reclaimed water services to Orange County residents. To provide these services, Utilities builds, acquires, and renovates capital assets. Employee compensation incurred to build and renovate capital assets are typically included in these capitalized costs. During 2017, Utilities capitalized over \$4.1 million of employee labor costs.

The Objective of Our Audit (Page 6)

The objective of the audit was to determine whether controls were adequate to ensure labor costs included in the construction of capital assets were accurate, properly allocated to appropriate capital projects, and sufficiently documented.

What We Found

Inaccurate Wage and Overhead Rates Were Used to Calculate Capital Labor Costs (Page 8)

Our review identified incorrect wage rates used to calculate two employees' capital labor costs. In addition, inaccurate overhead rates for insurance and retirement costs were used for all employees. As a result, capital labor costs were understated by \$26,780.

Employees' Capitalized Labor Hours Were Not Adequately Supported (Page 9)

Some Utilities employees are required to prepare manual timesheets to document their time worked on capital projects. The timesheets are entered into the Capital Labor Timekeeping Program to calculate total costs. Utilities personnel could not locate 14 of the 20 (70%) tested employees' timesheets. In addition, two employees reported a total of 57 hours of capital labor, but only 21 hours were recorded in the system. The hours capitalized also differed from the hours reported in the work order system.



Utilities Construction Inspectors Capitalized a Significant Amount of Overtime and Should Limit the Amount of Overtime (Page 11)

Construction Inspectors are responsible for inspecting both third-party and in-house construction capital projects. Six Construction Inspectors each recorded, capitalized, and were paid for more than 500 hours of overtime in the 15-month audit period. One inspector was paid for 1,260 hours of overtime during this time.

Overall Evaluation (Page 7 Overall Evaluation)

Based upon the results of our testing, we found that the controls were adequate to ensure employee labor costs included in the construction of capital assets were accurate, allocated to appropriate capital projects, and sufficiently documented.



INTRODUCTION

Background

The Orange County Utilities Department (Utilities) provides utilities services including water, wastewater and reclaimed water services to Orange County residents. In order to effectively, economically, and safely provide these services; Utilities builds, acquires, and renovates capital assets through the Capital Improvement Program (CIP). These projects are needed to accommodate growth; including, expanding, modernizing, and improving existing facilities and infrastructure.

Utilities follows Administrative Regulation 6.01.02 requiring Utilities to capitalize costs. According to the regulation, "...acquisition, construction, installation, and/or renovation of facilities that are expected to be in service for at least ten years and have a value in excess of \$25,000."¹ The bulk of Utilities' project expenditures are capitalized.

Utilities reported employees' capitalized labor costs of \$4,079,172 and \$4,134,440 for fiscal years 2016 and 2017, respectively. The capitalized labor amounts were allocated to 475 different CIP projects in fiscal year 2016 and 364 different CIP projects in fiscal year 2017.

Utilities uses a proprietary software application called "Capital Labor Timekeeping Program" (CLTP) to track and record hours worked on the design, construction, inspection, and installation of CIP projects. This program also calculates the costs and value associated with the employees' time that is tracked and recorded. The labor costs are capitalized and added to the total value of constructed assets as required by the Administrative Regulation. If employees do not have access to CLTP, they are required to prepare manual timesheets (Cap Sheets). The Cap Sheets are used to record the assigned CIP projects with the dates and hours worked. The Cap Sheets are required to be submitted every two weeks. Employees must sign their Cap Sheets and their supervisors must approve the Cap Sheets.

¹ The capitalization of costs adds to the value of Utilities' assets. Additionally, when costs are capitalized, they are not recorded as expenses. This reduces expenses reported by Utilities during the year that funds are spent. The depreciation of the capitalized asset recognizes a corresponding expense each year based on the assets expected useful life.

INTRODUCTION

In addition to the CLTP, Utilities utilizes an enterprise asset management and work order system called MAXIMO. MAXIMO interfaces with numerous County systems for work orders for both CIP projects as well as other service functions within Utilities.

The following chart shows Utilities' employees capitalized labor costs by division for fiscal year 2016.





INTRODUCTION

Audit Scope

The audit scope was limited to Utilities' employee labor costs allocated to capital asset projects. The audit period was from October 2015 through December 2016.

Audit Objective

The objective of the audit was to determine whether controls were adequate to ensure labor costs included in the construction of capital assets were accurate, properly allocated to appropriate capital projects, and sufficiently documented.

Audit Methodology

Our evaluation of the controls included interviews with key personnel and verifying compliance with adopted County regulations and Utilities procedures. We reviewed the projects which included capital labor costs to verify that the nature of the projects met accounting standards for cost capitalization.

To verify that computed capital labor costs were materially accurate, we performed the following:

- Compared the labor wage rates used in the CLTP to the rates recorded in the payroll system;
- Compared the capital labor fringe benefits rates used by the CLTP to the fringe benefit rates calculated by the Utilities Fiscal Division;
- Recomputed capital labor costs for a sample pay period using a blended wage rate according to applicable federal regulations; and,
- Reconciled the amounts calculated by the CLTP to the actual capital labor costs recorded in the general ledger for the audit period.

We verified that the projects listed in the CLTP were also listed as CIP projects in the County's approved fiscal year 2016 budget.

We compared a sample of Field Services Unit employee time listed on manually prepared Cap Sheets to CLTP and MAXIMO time records.



INTRODUCTION

We verified a sample of Construction Inspectors data entered in CLTP to the vehicle tracking system address locations to daily project reports and Kronos time entries.

Overall Evaluation

Based upon the results of our testing, we found that the controls were adequate to ensure employee labor costs included in the construction of capital assets were accurate, allocated to appropriate capital projects, and sufficiently documented.

1. Accurate Wage and Overhead Rates Should Be Utilized in the Computation of Capital Labor Costs

Our review of the Capital Labor Timekeeping Program (CLTP) identified instances where incorrect wage and overhead rates for insurance and retirement costs were used in the computation of capital labor costs. Specifically, we noted the following:

- A) Two employees had multiple active CLTP user accounts. Although each user had one account that included current rate information, the duplicate accounts contained incorrect rates. The incorrect accounts were used for those two employees. This error caused approximately \$4,500 of capitalized labor wages to be excluded.
- B) The rates used to calculate the insurance and retirement amounts in the CLTP were not accurate. We were informed that the Utilities Fiscal Unit staff responsible for entering updated rates did not save the updated rates. This resulted in an understatement of approximately \$22,280 of capitalized labor costs for fiscal year 2016.

The combined understatement of capital costs from the use of the incorrect wage, insurance, and retirement rates totals approximately \$26,780. Although the understatements of capital labor costs noted above is not material, Department procedures should include periodic reviews of user accounts and the rates used to calculate overhead costs.

Recommendation No. 1:

The Utilities Fiscal Unit should:

- A) Periodically review user accounts to identify and de-activate duplicate accounts; and,
 - B) Ensure departmental overhead rates are accurately updated in the CLTP.
-



Management's Response:

- A) *We concur. When we became aware of this issue, Utilities IT removed the duplicate accounts, and has instituted periodic reviews of all user accounts to ensure that no duplicate accounts are created. Utilities IT is in the process of creating an automated report to perform this task monthly.*
- B) *We concur. Utilities Fiscal staff is in the process of preparing a two-part procedure to address updating overhead rates in the CL TP. By providing two points of accountability, this process will ensure that the internal overhead rates are entered into the CL TP at the beginning of each fiscal year.*

2. Water Distribution Employees' Capitalized Labor Hours Should Be Adequately Supported

Some employees, such as Field Services Specialists, do not have access to the CLTP. If employees do not have access to CLTP, they are required to prepare manual timesheets (Cap Sheets). Cap Sheets are used to record dates and hours worked for assigned CIP projects. Employees must sign their Cap Sheets and their division representatives or supervisors must approve the Cap Sheets. The Cap Sheets are submitted every two weeks and recorded in CLTP by the section representative. Our review of the Cap Sheets noted the following:

- A) As part of our testing, we reviewed Water Distribution employee Cap Sheets recorded in the CLTP. We selected the two-week period ending July 2, 2016 for review. This period represented \$15,059 of the \$519,636 of capital labor charged to Water Distribution projects in the 2016 fiscal year. The CLTP included 49 weekly project time entries—related to 20 different employees—for the two-week period. Our testing noted the following concerns:
- Utilities personnel could not locate 14 of the 20 (70%) tested employees' Cap Sheets. As a result, there is no support to substantiate the capitalized hours relating to those 14 employees.



- The six Cap Sheets provided for review did not include the required initials or signatures of either the employee or supervisor. While supervisors may also electronically approve Cap Sheets in the CLTP, four of the 49 weekly project time entries (approximately 8%) were not approved.
- Two employees' Cap Sheets reported a total of 57 hours of capital labor, but only 21 hours were recorded in the CLTP.

To ascertain whether this problem was indicative of a larger problem, we expanded our review to include a comparison of the employees hours tested above to hours recorded in MAXIMO for the two-week period. This additional review found that the hours capitalized for 3 of the 20 employees exceeded the total hours of work recorded in MAXIMO for all projects. However, the total hours recorded for all 20 employees in the CLTP was approximately seven percent² less than the total hours recorded in MAXIMO for capital project tasks.

- B) As a result of further testing, we identified 11 additional employees who collectively reported a total of 241 hours attributable to capital projects in MAXIMO during the two-week test period. Cap Sheets were not completed with respect to the two-week period. Therefore, none of these hours were recorded in the CLTP.

We were informed by management that MAXIMO reports provide a summary of time recorded by employee of all work orders, field activities, and projects. These electronic records may provide a more efficient and effective means of capturing hours worked on capital projects. An effective control system should include monitoring of compliance with the procedures and taking corrective action in instances of non-compliance. Compliance with existing procedures helps ensure that the controls are working and all capital labor hours are appropriately capitalized.

² 500.6 hours recorded in CLTP versus 536.7 hours recorded in MAXIMO

Recommendation No. 2:

Utilities management personnel should consider utilizing MAXIMO reports to enter capitalized labor hours in the CLTP. If MAXIMO reports are not used, procedures should ensure all Cap Sheets are completed, signed, approved, and accurately entered into the CLTP.

Management's Response:

We concur. Field Services will work with Utilities IT to investigate new reporting functionality in MAXIMO in order to capture the hours of each employee working on a CIP project. If that does not prove to be a feasible solution, Utilities management will update the Utilities Department Operating Procedure for Capital Labor to assign responsibility to verify that Cap Sheets are completed, signed, approved, and accurately entered into the CLTP.

3. Utilities Should Limit Overtime Hours

The Water, Water Reclamation, and Field Services Divisions capitalized the majority of overtime labor. We noted that the Field Services Construction Inspectors reported more overtime hours per employee than any other department. Six Construction Inspectors each recorded, capitalized, and were paid for more than 500 hours of overtime in the 15-month audit period. One of the inspectors recorded, capitalized, and was paid for 1,260 hours of overtime during this time. Management reported they had several unfilled positions during the audit period which led to this significant amount of overtime.

The Construction Inspectors are responsible for inspecting both third-party constructed CIP projects and in-house construction. Often third-party contractors work late nights and weekends due to life/safety aspects of water and wastewater distribution/treatment. They also might work late due to contractual deadlines or traffic safety concerns.



Field Services personnel provided us with an internal procedure document titled “Maximum Work Day Limits (a.k.a. 16 Hour Rule).” The document states, “If an employee works more than 16 hours in a 24-hour period, the employee must be scheduled to be off at least 14 hours within the next 24-hour period. The scheduled time off does not have to be in one workday or consecutive hours.” However, the policy also provides that exceptions to the “Extended Work Hours Divisional Guideline” must be approved by the Division Manager or Assistant Divisional Manager.

During the two-week pay period ending July 2, 2016, five inspectors recorded between 99.5 hours to 114.2 hours each. Four inspectors recorded working more than 16 hours in a 24-hour period. One inspector worked 33.3 hours of overtime during a six-day period, recording three consecutive days of working 15.3 hours, 11.5 hours and 17.5 hours.

Another inspector reported working 17.2 hours on the first day of the week and 11.2 hours each of the remaining three work days. Therefore, this inspector exceeded the number of hours allowed under the policy. Utilities management stated that the manager approved the overtime. However, no evidence of this approval was recorded.

The Federal Transportation Safety Board recognizes fatigue and insufficient sleep as a leading cause of vehicle accidents. County owned vehicles are assigned and driven by these inspectors. According to an FBI Law Enforcement Bulletin, “Long work hours can lead to fatigue and result in negative effects on personal safety, performance, and health. Fatigue increases the risk of accidents and other safety incidents, such as decreasing alertness, impairing decision-making ability, and slowing down reaction time. Fatigue also harms work performance by weakening memory, lowering frustration tolerance, and increasing stress, burnout, and absenteeism. Finally, fatigue can have long-term health implications, including increased blood pressure, hypertension, metabolic syndrome, and obesity.”³

³ Lindsey, D. (2007). Police Fatigue: an Accident waiting to happen. *FBI Law Enforcement Bullitan*.



Recommendation No 3:

Utilities management should work to reduce the number of overtime hours worked by the Division.

Management's Response:

We concur. Utilities is working with Human Resources to expedite hiring to fill vacant positions. This has been a challenge with historically low unemployment and the amount of construction activity in Central Florida, competing for skilled trades positions. We are evaluating the need for additional budgeted positions however we are mindful that the economy and construction activity are cyclical and we don't want to staff for peak demand with permanent positions. We will explore the potential for contract labor to assist with inspection activities and evaluate the cost of doing so against the incremental cost of using overtime.



ACTION PLAN

NO.	RECOMMENDATIONS	MANAGEMENT'S RESPONSE		
		CONCUR	PARTIALLY CONCUR	DO NOT CONCUR
1.	The Utilities Fiscal Unit should:			
A)	Periodically review user accounts to identify and de-activate duplicate accounts; and,	✓		
B)	Ensure departmental overhead rates are accurately updated in the CLTP.	✓		
2.	Utilities management personnel should consider utilizing MAXIMO reports to enter capitalized labor hours in the CLTP. If MAXIMO reports are not used, procedures should ensure all Cap Sheets are completed, signed, approved, and accurately entered into the CLTP.	✓		
3.	Utilities management should work to reduce the number of overtime hours worked by the Division.	✓		