

OFFICE OF AUDITS & ADVISORY SERVICES



CAPITAL PROJECTS COST CLASSIFICATION AUDIT

FINAL REPORT

Chief of Audits: Juan R. Perez
Audit Manager: Lynne Prizzia, CISA, CRISC
Senior Auditor: Ida Miclat, CPA
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County of San Diego

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AUDITOR AND CONTROLLER

AUDITOR AND CONTROLLER
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JUAN R. PEREZ
CHIEF OF AUDITS

July 23, 2019

TO: Tracy Drager
Auditor and Controller

FROM: Juan R. Perez
Chief of Audits

FINAL REPORT: CAPITAL PROJECTS COST CLASSIFICATION AUDIT

Enclosed is our report on the Capital Projects Cost Classification Audit. We have reviewed your response to our recommendations and have attached it to the audit report.

The actions taken and/or planned, in general, are responsive to the recommendations in the report. As required under Board of Supervisors Policy B-44, we respectfully request that you provide quarterly status reports on the implementation progress of the recommendations. You or your designee will receive email notifications when these quarterly updates are due, and these notifications will continue until all actions have been implemented.

If you have any questions, please contact me at (858) 495-5661.

A handwritten signature in blue ink, appearing to read "Juan R. Perez".

JUAN R. PEREZ
Chief of Audits

AUD:IM:nb

Enclosure

c: Tracy M. Sandoval, Deputy Chief Administrative Officer/Chief Financial Officer
Damien Quinn, Group Finance Director, Finance and General Government Group



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JUAN R. PEREZ
CHIEF OF AUDITS

July 23, 2019

TO: Marko Medved, Director
Department of General Services

FROM: Juan R. Perez
Chief of Audits

FINAL REPORT: CAPITAL PROJECTS COST CLASSIFICATION AUDIT

Enclosed is our report on the Capital Projects Cost Classification Audit. We have reviewed your response to our recommendations and have attached it to the audit report.

The actions taken and/or planned, in general, are responsive to the recommendations in the report. As required under Board of Supervisors Policy B-44, we respectfully request that you provide quarterly status reports on the implementation progress of the recommendations. You or your designee will receive email notifications when these quarterly updates are due, and these notifications will continue until all actions have been implemented.

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Chief of Audits

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c: Tracy M. Sandoval, Deputy Chief Administrative Officer/Chief Financial Officer
Tracy Drager, Auditor and Controller
Damien Quinn, Group Finance Director, Finance and General Government Group

INTRODUCTION

Audit Objective The Office of Audits & Advisory Services (OAAS) completed an audit of the Capital Projects Cost Classification. The objective of the audit was to evaluate adequacy of procedures in place to ensure capital costs are accurately classified and reported.

Background Capital projects are acquisitions or construction of new public improvements including buildings, initial furnishings and equipment. These could also include land and off-site improvements, replacement or reconstruction of permanent public improvements which extend the useful life, increase the ability to provide service or change the functionality of an existing capital asset. Capital projects may also include acquisition of assets that are tangible or intangible for use in operations that will benefit more than one fiscal year and meet the capitalization threshold.

The Capital Program Funds (CPF) were established by the County of San Diego Board of Supervisors (BOS) to provide centralized budgeting and accounting for the County's capital projects. These include the Capital Outlay Fund, County Health Complex, Capital Multiple Species Conservation Program Acquisition Fund, Justice Facility Construction Fund, Library Projects Capital Outlay Fund, and Major Maintenance Capital Outlay Fund. The Auditor and Controller through the Projects, Revenue and Grant Accounting division manages the CPF.

Capital projects are presented for approval to the BOS through the Capital Improvement Needs Assessment (CINA) included in the Annual Operating Plan. The CINA is a planning document developed each year by the Department of General Services (DGS) pursuant to BOS Policy G-16 Capital Facilities and Space Planning which identifies proposed projects for a five-year timeframe.

DGS, on behalf of the Facilities Planning Board (FPB) and pursuant to BOS Policy G-16, oversees the framework for the CINA. They prepare a consolidated and prioritized CINA in conformance with the County's General Management System. It is designed to align capital projects planning with the County's strategic initiatives and five-year financial forecast.

Audit Scope & Limitations The scope of the audit included review of the management controls and processes related to capital costs for fiscal year 2015-16 to current. OAAS selected the following three departments that handle capital projects to conduct the audit testing:

- Auditor and Controller (A&C) - Projects, Revenue and Grant Accounting (PRGA)
- Department of General Services (DGS)

- Department of Parks and Recreation (DPR)

This audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing prescribed by the Institute of Internal Auditors as required by California Government Code, Section 1236.

Methodology

OAAS performed the audit using the following methods:

- Reviewed policies and procedures related to capital projects.
- Reviewed and evaluated the methodology used for prioritization of capital projects.
- Identified and evaluated controls over the approval process and budget set up of capital projects.
- Assessed internal controls in place to ensure capital expenditures are properly reported.
- On a sample basis, conducted specific audit procedures such as inquiry, document inspection and analysis to determine proper classification and reporting of capital assets.

AUDIT RESULTS

Summary

Within the scope of the audit, there is reasonable assurance that adequate procedures are in place to ensure capital costs are accurately classified and reported. However, OAAS identified opportunities for improvement.

Finding I:

Prioritization of Requests for Capital Projects

From the CINA plan fiscal years 2015-16 through 2018-19, OAAS reviewed a sample of 30 capital projects and determined that DGS did not perform the evaluation process to prioritize requests for capital projects with an estimated cost of under \$10 million. Specifically, capital projects with less than \$10 million in cost did not have any scoring matrix, a form designed by DGS to evaluate the project priority. This is not in compliance with BOS Policy G-16 (Capital Facilities and Space Planning) and Admin Manual 0050-01-06 (Capital, Space and Maintenance Requests) prioritization requirements.

According to DGS management, the FPB did not require a scoring matrix for capital projects under \$10 million previous to fiscal year 2018-19.

The BOS Policy G-16 and Admin Manual 0050-01-06 both require that capital projects shall be prioritized using specific criteria provided in the Policy for evaluation of capital project requests during the CINA process.

OAAS further noted that capital projects were addressed in the Admin Manual 0050-01-06 as “major capital projects” which is not consistent with the wording in BOS Policy G-16. According to A&C, the Admin Manual 0050-01-06 was developed by both A&C and DGS.

The use of the limited County resources may not be optimized as a result of the lack of an evaluation process to prioritize requests for capital projects.

Recommendation: To make the most efficient use of the County resources, DGS should:

1. Document the process to prioritize all capital projects using criteria specified in BOS Policy G-16.
2. Continue to communicate to departments the implementation of the prioritization process for all capital projects.

To provide clear guidance to County departments, A&C should:

3. Review the use of the term 'Major capital projects' in Admin Manual 0050-01-06 and revise as appropriate to be consistent with BOS Policy G-16.

Finding II: Reclassification of Major Maintenance Projects

From the list of 248 major maintenance projects, OAAS reviewed a sample of 19 projects selected for testing and determined that 2 projects with total costs of \$147,297 should be reclassified to Major Maintenance Capital Outlay Fund (MMCOF) projects.

Although A&C reviewed all major maintenance projects and made the determination whether a project should be classified as MMCOF; according to A&C, the determination was made based on limited project information available at the time of the review.

The Admin Manual 0050-02-01 (Control of Capital Assets and Minor Equipment) requires that costs of construction of capital assets be budgeted and expended in the Capital Outlay Fund.

As a result of not capitalizing the project costs, the capital assets on the financial statements may be understated and major maintenance expenditures may be overstated. In addition, depreciation related to the projects may not be recorded.

Recommendation: To properly report capital costs:

1. DGS should reclassify projects that were incorrectly identified as major maintenance to capital projects.
2. A&C should collaborate with DGS to develop a list of sample capital projects to be used as reference or guide to determine the proper

project classification, in addition to the examples provided in the Managing Capital Projects Guidebook.

Office of Audits & Advisory Services

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VALUE

DEPARTMENT'S RESPONSE
(AUDITOR AND CONTROLLER)



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RECEIVED

JUL 17 2019

OFFICE OF AUDITS &
ADVISORY SERVICES

July 16, 2019

TO: Juan R. Perez
Chief of Audits

FROM: Tracy Drager
Auditor and Controller

DEPARTMENT RESPONSE TO AUDIT RECOMMENDATIONS: CAPITAL PROJECTS COST CLASSIFICATION AUDIT

Finding I: Prioritization of Requests for Capital Projects

OAAS Recommendation: To provide clear guidance to County departments, A&C should review the use of the term 'Major capital projects' in Admin Manual 0050-01-06 and revise as appropriate to be consistent with BOS Policy G-16.

Action Plan: A&C agrees with the audit recommendation. A&C will review the use of the term 'Major capital projects' in Admin Manual 0050-01-06 and revise as appropriate to be consistent with BOS Policy G-16.

Planned Completion Date: December 31, 2019

Contact Information for Implementation: Babette Baltazar
Manager, Auditor and Controller

Finding II: Reclassification of Major Maintenance Projects

OAAS Recommendation: To properly report capital assets, A&C should collaborate with DGS to develop a list of sample capital projects to be used as reference or guide to determine the proper project classification, in addition to the examples provided in the Managing Capital Projects Guidebook.

Department Response to Audit Recommendations: Capital Projects Cost Classification Audit
Page Two
July 16, 2019

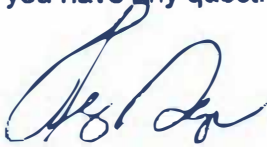
Action Plan: A&C agrees with the audit recommendation.

A&C will collaborate with DGS to add sample major maintenance capital projects to the list provided in the County of San Diego Capital Assets Guide.

Planned Completion Date: December 31, 2019

Contact Information for Implementation: Babette Baltazar
Manager, Auditor and Controller

If you have any question, please contact me at (858) 694-2324.



TRACY DRAGER
Auditor and Controller

A&C:TD:tw

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(DEPARTMENT OF GENERAL SERVICES)



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July 19, 2019

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JUL 23 2019

OFFICE OF AUDITS &
ADVISORY SERVICES

TO: JUAN R. PEREZ, Chief of Audits
Office of Audits and Advisory Services

FROM: MARKO MEDVED, Director
Department of General Services

DEPARTMENT RESPONSE TO AUDIT RECOMMENDATION: CAPITAL PROJECTS COST CLASSIFICATION AUDIT

Finding I: Prioritization of Requests for Capital Projects

OAAS Recommendation: To make the most efficient use of the County resources, DGS should:

1. Document the process to prioritize all capital projects using criteria specified in BOS Policy G-16.
2. Continue to communicate to departments the implementation of the prioritization process for all capital projects.

Action Plan: The Department of General Services (DGS) agrees with this audit recommendation. DGS will document the process to prioritize all capital projects using criteria specified in BOS Policy G-16 and communicate the process to departments.

Planned Completion Date: October 31, 2019

Contact Information for Implementation: Tom Fincher, Chief of Strategic Planning, at thomas.fincher@sdcount.ca.gov or (858) 694-2153.

Finding II: Reclassification of Major Maintenance Projects

OAAS Recommendation: To properly report capital costs:

1. DGS should reclassify projects that were incorrectly identified as major maintenance to capital projects.
2. A&C should collaborate with DGS to develop a list of sample capital projects to be used as a reference or guide to determine the proper project classification, in addition to the examples provided in the Managing Capital Projects Guidebook.



Action Plan: The Department of General Services (DGS) agrees with this audit recommendation. DGS will reclassify projects that were incorrectly identified as major maintenance to capital projects and collaborate with A&C to develop a list of sample projects that qualify to be capital projects.

Planned Completion Date: December 31, 2019

Contact Information for Implementation: Tom Fincher, Chief of Strategic Planning, at thomas.fischer@sdcount.ca.gov or (858) 694-2153.

If you have any questions, please contact me at marko.medved@sdcounty.ca.gov or (858) 694-2527.