

Mayor Jim Newberry

LEXINGTON-FAYETTE URBAN COUNTY GOVERNMENT

Office of Internal Audit

INTERNAL AUDIT REPORT

DATE: January 9, 2009

TO: Jim Newberry, Mayor

CC: Joe Kelly, Senior Advisor for Management

Cheryl Taylor, Commissioner of Environmental Quality

Steve Feese, Director of Waste Management

Urban County Council Members Internal Audit Board Members

FROM: Bruce Sahli, Director of Internal Audit

RE: Division of Waste Management Time Reporting Review

Background

On August 15 2005, the Office of Internal Audit issued an audit report on Division of Waste Management Time Reporting, with a follow-up report issued on June 20, 2006. Those reports identified several time reporting issues within the Division, including significant under-time (defined as employee hours paid for but not worked as authorized by management) and significant increases in overtime (some of which was paid for overtime hours not actually worked). This is a follow-up review to determine if under-time and overtime levels have improved.

Scope & Objectives

The audit was conducted to provide reasonable assurance that:

- Under-time is being effectively managed
- Payroll adjustments are reasonable and appropriate
- Overtime is being effectively managed
- The use of temporary agencies is reasonable and effectively managed

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The period of review was calendar 2000-2008 for detailed overtime activity and calendar November 27, 2005 through September 28, 2008 for under-time. The November 27, 2005 pay period was the first to track under-time in the KRONOS System.

STATEMENT OF AUDITING STANDARDS

We conducted our audit in accordance with the International Standards for the Professional Practice of Internal Auditing. Those standards require that we plan and perform the audit to afford a reasonable basis for our judgments and conclusions regarding the organization, program, activity or function under audit. An audit also includes assessments of applicable internal controls and compliance with requirements of laws and regulations when necessary to satisfy the audit objectives. We believe that our audit provides a reasonable basis for our conclusions.

AUDIT OPINION

In our opinion, the controls and procedures provided reasonable assurance that the general control objectives were being met. Opportunities to enhance controls are included in the Summary of Audit Findings.

SUMMARY OF AUDIT FINDINGS

1. Significant Improvement in the Management of Under-time

Under-time is defined as employee hours paid for but not worked as authorized by management. It is also referred to as incentive pay because it rewards route workers for completing their assigned route before the end of their shift. We conducted a trend analysis of under-time activity occurring during payroll periods November 27, 2005 through September 28, 2008. The results of that analysis are depicted on line graphs contained in Attachments I and II. The Attachment I line graph depicts the overall under-time reduction, while the Attachment II line graph depicts under-time reduction since the last Waste Management time reporting audit conducted in June 2006. Both demonstrate a significant decrease in under-time, which peaked in the pay period ending December 25, 2005 at 5,571 hours and had a minimum under-time of 900 hours for pay period ending January 6, 2008. This represents a highly significant improvement in the management of under-time.

Of particular note is the fact that under-time has decreased 94% from an average of 2,719 hours for the pay period November 27, 2005 through July 22, 2007 to an average of 1,404 hours for the pay period August 5, 2007 through September 28, 2008. Effective July 31, 2007 there was a management change in this Division and two managers assumed joint responsibility as Acting Director. Effective January 21, 2008 one of those managers was subsequently made Director. This new management team amended the under-time program to better align it with industry best practices. Eight-hour day route workers now must actually work a minimum of six hours per day in order to be eligible for two hours of under-time, while ten-hour day route workers now must actually work a minimum of eight

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hours per day to be eligible for two hours of under-time pay. This is a significant improvement in the effective management of under-time.

<u>Director of Waste Management Response:</u> The Division plans to continue the policy of minimum work hours even on the days that the crews complete their routes early because of limited set out or other operational issues.

<u>Commissioner of Environmental Quality Response:</u> I concur with the finding and recommendation of the audit.

2. Significant Growth in Overtime and Temporary Labor Expense

We conducted a trend analysis of gross pay (Attachment III), overtime pay (Attachment IV), temporary labor expense (Attachment V), and headcount (Attachment VI) during calendar years 2000 through 2008 (projected). Gross pay has been relatively flat in 2007 & 2008 (forecast), but the 2007 and 2008 trend in overtime demonstrates an increase of 67% in 2007 and an additional 50% in 2008 (projected). Temporary labor costs have experienced significant growth in FY 2008 and spikes to a projected FY 2009 cost of approximately \$1.5 Million. Headcount is an apparent link to the increasing overtime and temporary labor costs. Staffing has trended down from 217 in 2005 to 199 in both 2007 and 2008 (authorized strength is 234), and overtime and temporary labor cost increases appear to be driven by a shortage of route workers and the extensive use of temporary labor at the recycling center. Management stated they are in the process of developing new, more efficient routes and adding GPS tracking capability to the trucks. Management also informed us that temporary labor is the most efficient method for staffing the recycling center as it experiences high turnover due to the nature of the work.

We also noted that unearned overtime is still an issue. In a judgmental sample of overtime for pay period ended August 17, 2008, we noted that 241.8 hours of the total 887.3 hours of overtime paid (27.3%) was unearned due to the incentive pay system. Unearned overtime primarily occurs when a route worker receives under-time and works on a scheduled day off during the same pay period for training or additional route work. In 2006, the Department of Labor hotline informed Department of Law personnel that LFUCG is required to pay this overtime due to the design of the incentive pay system. Therefore, as long as the under-time program is in place and four-day a week employees train in their unscheduled work days, unearned overtime payments will continue to occur.

We recommend Division management continue to pursue the development of more efficient routes and the installation of GPS tracking devices, and keep staffing at the current level until the impact of these initiatives is determined. Management should then seek to obtain balance between route worker levels and staffing needs in order to reduce overtime and temporary labor expense. From the time management efficiencies gained through these two initiates, management should also evaluate whether some training may then occur during regular route workdays in order to further reduce overtime costs. Senior management should also consider that if unearned overtime is going to be allowed to continue under the incentive system, the Code of Ordinances should be amended to codify this practice.

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<u>Director of Waste Management Response:</u> The Division is taking steps both internally and in conjunction with the Division of Computer Services to improve the routing system to achieve a more even distribution and efficient use of personnel. One of the benefits would be to reduce the level of overtime needed to conduct routine operations. We will also be working with Human Resources to develop a system of maintaining our staffing level of civil service employees to reduce our dependence on overtime and temporary employees.

<u>Commissioner of Environmental Quality Response:</u> I concur with the finding and recommendation of the audit. We have plans to continue to improve the situation with the addition of the new routing software, a project we are working on right now.

RISK OBSERVATION

Standards for the Professional Practice of Internal Audit stipulate that it is the Office of Internal Audit's responsibility to inform management of areas where risk to the organization or those it serves exists. The following observation identifies a risk associated with the incentive pay process not considered an audit finding, but which is considered to be of sufficient importance to deserve mention in this report to ensure senior management's awareness.

Incentive Pay Program Increases Holiday Pay Expense

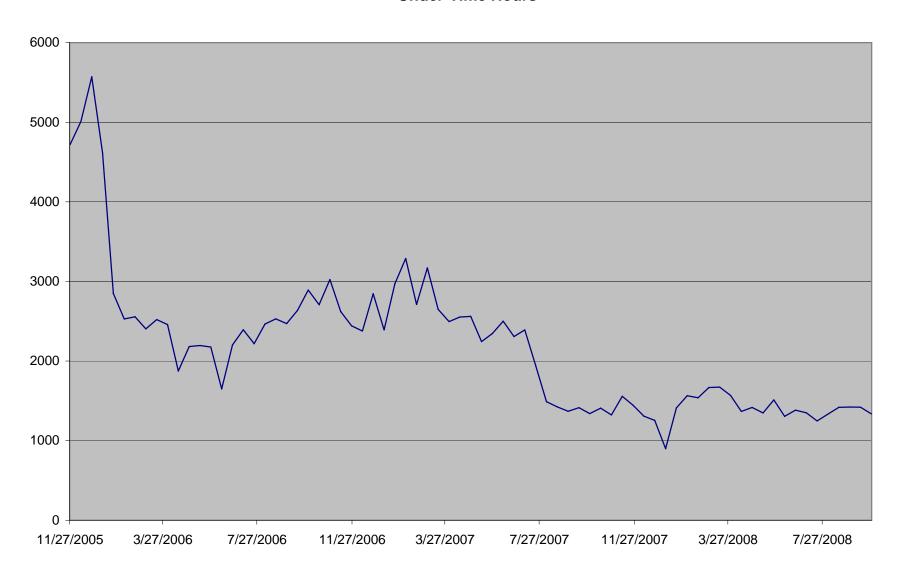
Under the incentive pay program, most Waste Management hourly employees are paid ten hours of holiday pay for designated holidays, rather than eight hours standard to the LFUCG (KRONOS refers to this two hour difference as Holiday Guarantee). In 2007, this practice resulted in 2,492 hours, or approximately \$41,000, of Holiday Guarantee time paid. This is the direct result of the four-day workweek assigned to most route workers. We found no language in the Code of Ordinances specifying whether Holiday Pay is for an eight-hour or ten-hour day.

This item is included in the report to inform senior management of the additional payroll expense the incentive pay system creates during designated Holidays. It is recommended management continue to access the benefits of the incentive pay program against the costs thereof.

<u>Director of Waste Management Response:</u> We have addressed this issue with the Director of Human Resources in the past. He has indicated that the Code of Ordinance requires us to pay the 10 hour employees for the full 10 hours.

<u>Commissioner of Environmental Quality Response:</u> I concur with the finding and recommendation of the audit. In order to remain fiscally responsible, we will request that the Division of Human Resources notify the Department of Environmental Quality of any amendments in the law (should they occur) that would support changing to an eight hour holiday.

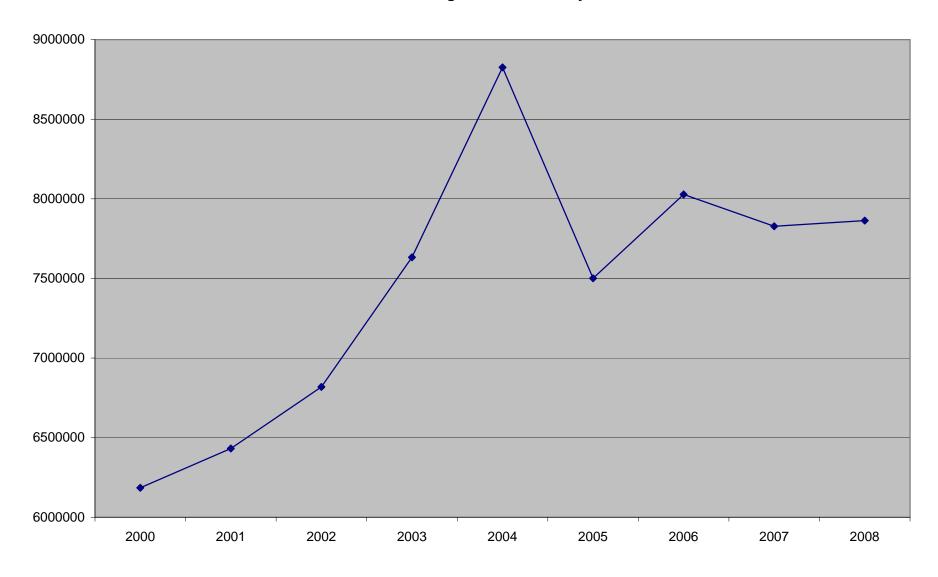
Attachment I Under-Time Hours



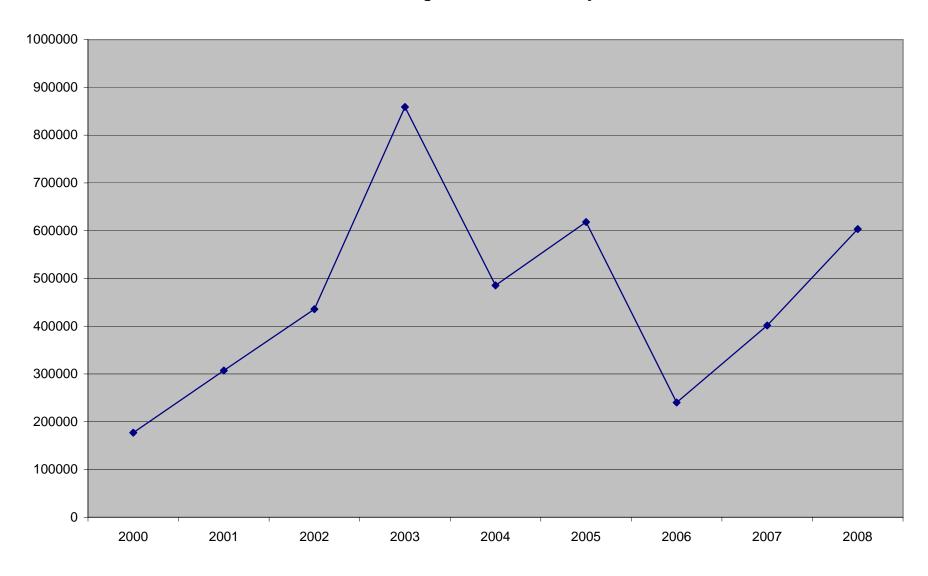
Attachment II
Under-Time Hours Since Last Audit



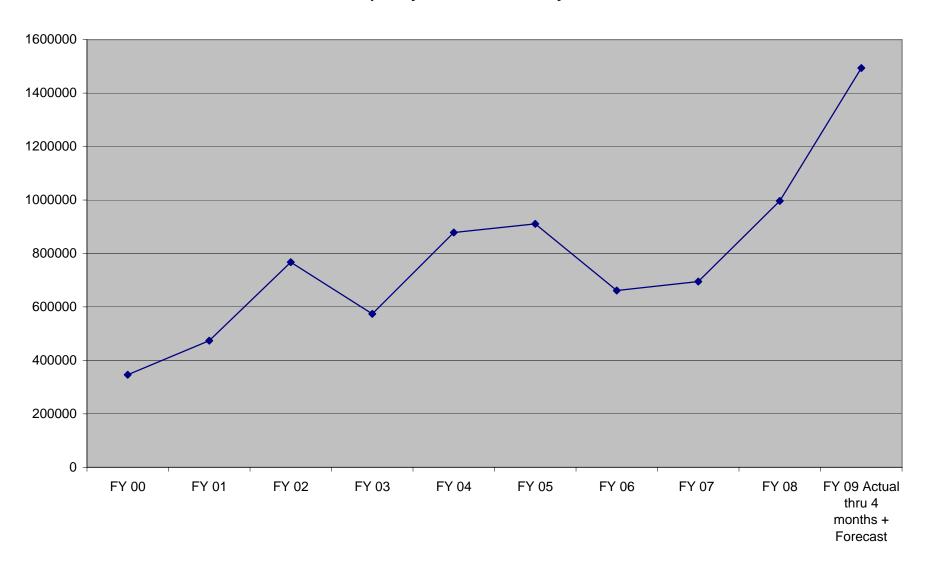
Attachment III
Waste Management Gross Pay



Attachment IV Waste Management Over-Time Pay



Attachment V
Temporary Labor Trend Analysis



Attachment VI Headcount

