

INTERNAL AUDIT REPORT

DATE: July 23, 2020

TO: Linda Gorton, Mayor

CC: Sally Hamilton, Chief Administrative Officer
Glenn Brown, Deputy Chief Administrative Officer
Aldona Valicenti, Chief Information Officer
Kevin Atkins, Chief Development Officer
Nancy Albright, Commissioner of Environmental Quality & Public Works
William O'Mara, Commissioner of Finance and Administration
Susan Speckert, Commissioner of Law
Douglas Burton, Director of Engineering
Phyllis Cooper, Director of Accounting
James Duncan, Director of Planning
Susan Straub, Communications Director
Urban County Council
Internal Audit Board

FROM: Bruce Sahli, CIA, CFE, Director of Internal Audit
Matthew Reid, CPA, Internal Auditor

RE: Exaction Program Audit

Background

In 1996 Council approved the expansion of the Urban Growth Boundary in Fayette County into several Expansion Areas (EA1, EA2A, EA2B, EA2C, and EA3) and addressed the need for the development of infrastructure (e.g. roads, sewer transmission,



sewer treatment, etc.). In an effort to provide a system to finance the development of this infrastructure, Appendix 23C of Article 23 of the Zoning Ordinance established regulations for the Exaction program, implementing the Expansion Area Master Plan (EAMP).

An exaction is a fee calculated based upon zoning, land area, and the cost to provide public facilities. New developments constructed in Expansion Areas are assessed an exaction fee on a lot by lot basis which represents the proportionate fair share cost of installing new infrastructure in that expansion area. Developers can choose to pay exaction fees at the time of building permit and allow LFUCG to construct the improvements, or they can choose to build the infrastructure in the Expansion Area and receive exaction credits in the amount equal to their cost of construction.

If a developer constructs the infrastructure (i.e. roads, sewer lines, storm water, etc.) in an expansion area, they receive exaction credits equal to their cost of construction which can be utilized to offset the exactions owed. Before construction begins, the estimated cost of construction is calculated and approved in a written agreement or memorandum and the developer is granted exaction credits in the amount of the estimated cost. Developers can begin utilizing these exaction credits, which are limited to 80% of the estimated amount awarded, to offset exaction fees before construction is completed. Utilizing these exaction credits will draw down the balance of exaction credits developers have available for future use.

Prior to construction, the developer prepares a plat which reports exaction fees for each lot included in the plat. Exaction fees are calculated and approved by the Division of Planning. An employee in the Division of Planning inputs the amount of the exaction fee into the EAMP Database for each lot included in the plat. In the event a developer utilizes an exaction credit, the application of this credit is also entered into the EAMP Database. We were informed by the Director of Accounting that the EAMP Database contained the complete population of all exaction activity and transactions. This includes the amount of exaction fees due on a lot-by-lot basis as well as the amount of exaction credits utilized on a lot-by-lot basis for all properties located in the Expansion Areas.

In addition, a member of the LFUCG Department of Finance maintains an Exaction Credit Statement for each developer that is granted exaction credits. The Exaction Credit Statement identifies the amount of exaction credits awarded to the developer, the amount of exaction credits utilized by the developer, and the net balance of credits available to be used in the future.



After the construction is completed, the developer submits supporting documentation detailing the actual total cost of construction which will likely differ from the approved cost estimate. The supporting documentation is reviewed by the Exaction Credit Advisory Committee (ECAC) and if approved, the agreement or memorandum is “closed out” and a letter is mailed to the developer notifying them of the amount of exaction credits they were ultimately granted. In the event a developer fails to submit documentation of final costs, the related agreement is closed out at 80% of the estimated credits originally awarded.

Scope and Objectives

The general control objectives for the audit were to provide reasonable assurance that:

- Credit statements exist for every exaction agreement / memorandum
- Exaction credits granted per credit statements agree with the amount of exaction credits approved by the ECAC and awarded in the Close-Out Letter
- Exaction credits utilized by developers as reported in the credit statements agree with the exaction credits utilized as reported in the EAMP Database
- Exaction Credit Net Balances in credit statements are reasonably stated
- Exaction credits reported as transferred-out from one credit statement are being correctly reported as transferred-in on another credit statement
- Exaction credits are being utilized in an appropriate expansion area
- Exaction fees reported on the plat agree with exaction fees reported in the EAMP Database
- Capital assets associated with exaction agreements that have been closed out are capitalized and recorded in the PeopleSoft general ledger

Audit results are based on observations, inquiries, transaction examinations, and the examination of other audit evidence and provide reasonable, but not absolute, assurance controls are in place and are effective. In addition, effective controls in place during an audit may subsequently become ineffective as a result of technology changes or reduced standards of performance on the part of management.

The scope of the audit included activity from the commencement of the exaction program through June 30, 2019. The audit included the performance of test work to verify exaction fees as reported on the plat were in agreement with exaction fees reported in the EAMP



Database. We verified exaction credit statements were reasonably stated by confirming exaction credits granted as reported in the credit statements agree with the amount of exaction credits approved by the ECAC (Exaction Credit Advisory Committee) and reported in the Close-Out Letter, and also by reconciling exaction credits utilized as reported in the credit statements to the amount of credits utilized as reported in the EAMP Database. We relied upon the exaction fee calculations provided on the related plats as approved by professional engineers in performing our work. Although some discrepancies were identified during our testing, overall it appears the credit statements are reasonably stated.

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 mostly being met. Opportunities to improve controls are included in the Summary of Audit Findings.

Priority Rating Process

To assist management in its evaluation, the findings have been assigned a qualitative assessment of the need for corrective action. Each item is assessed a high, moderate, or low priority as follows:

High - Represents a finding requiring immediate action by management to mitigate risks and/or costs associated with the process being audited.



Moderate – Represents a finding requiring timely action by management to mitigate risks and/or costs associated with the process being audited.

Low - Represents a finding for consideration by management for correction or implementation associated with the process being audited.

SUMMARY OF AUDIT FINDINGS

Finding #1: Management of Exaction Program Should be Assigned to a Single Authority

Priority Rating: High

Condition:

Several employees across multiple Divisions currently play a role in the administration and management of the exaction program, with no one employee or Division taking full ownership of the program. An employee reporting to the Chief Development Officer is overseeing much of the exaction program, exaction credit statements are prepared and maintained by employees in the Department of Finance, and an Administrative Officer Senior in the Division of Planning is responsible for entering exaction data (i.e. exaction fees and exaction credits utilized) into the EAMP Database. As a result, a simple miscommunication or oversight could possibly cause an unintentional error or omission in the administration or management of the exactions program. It is possible this has been a contributing factor in some or perhaps all of the other findings noted in this report.

Effect:

The absence of ownership by a single Division and/or Manager increases the likelihood of errors and omissions in the administration of the exaction program.

Recommendation:

The Chief Administrative Officer should consider assigning formal responsibility for the administration of the exactions program to a specific Division and/or Manager. During the audit, we were informed that a new software system is currently being developed in an attempt to consolidate data functions within the exactions program. If successful, the new software could be a useful tool for the Division and/or Manager who is ultimately assigned ownership of the exactions program.



Chief Administrative Officer Response:

I agree with this recommendation. During a recent Zoom meeting with Bill O'Mara, Jenifer Wuorenmaa, Kevin Atkins, Craig Bencz and Wes Holbrook, we discussed this recommendation in detail. Craig felt that a meaningful job description could not be prepared or a person hired until the RFP was issued and the consultant's work was complete. We also agreed that when it is time to either hire or assign someone to work full time on exactions, the position will be in the CAO's Office. However, until then we will continue as it is now.

Finding #2: Several Credit Statements Report Negative Credit Balances
Priority Rating: High

Condition:

An Administrative Officer Senior in the Department of Finance (referred to hereafter as the credit statement custodian) maintains all exaction credit statements. These credit statements are created when a developer enters into an exaction agreement/memorandum with LFUCG. Each credit statement reports the amount of exaction credits granted to the developer, the amount of exaction credits utilized by the developer, and the net balance of exaction credits remaining to be used in the future for each exaction agreement / memorandum. We obtained all of the credit statements from the credit statement custodian and noted that several of them reported a negative balance, indicating that more exaction credits were utilized by developers than the amount of exaction credits granted.

The credit statement custodian informed us that if a developer utilized more credits than was granted in an agreement resulting in a negative credit balance, and the same developer had available credits to utilize in a second agreement having a positive credit balance, the two credit balances would not be netted together to calculate the amount of "net" credits the developer is allowed to use going forward. The credit statement custodian explained this has been the standard practice when a developer has more than one exaction agreement. For example, if Developer X has an agreement in which exaction credits granted were overspent by \$200,000, and Developer X also has a second agreement which still has \$300,000 of exaction credits available, the standard practice has been to allow Developer X to utilize the full amount of the \$300,000 exaction credits associated with the second agreement even though the first agreement had a negative \$200,000 credit balance. The two amounts would not be netted out to provide a remaining exaction credit balance of \$100,000.



Effect:

The practice of allowing developers to spend existing credits from one exaction agreement when another of the developer's exaction agreement credits are overspent has the result of allowing the developer to utilize more exaction credits than LFUCG granted.

Recommendation:

The Department of Law should determine how to address negative credit balances and whether the netting of exaction agreement/memorandum credit balances involving the same developer is a legally enforceable way to address this matter.

Commissioner of Law Response:

Under Article 23C of the Zoning Ordinance, if a developer elects to construct all or a portion of the required system improvements in an Expansion Area, the developer is required to enter into a development agreement / memorandum with LFUCG. Section 23C-7 of the Zoning Ordinance expressly requires the development agreement / memorandum to provide for verification of costs through documentation required by LFUCG. Following construction of the required system improvement, LFUCG requests documentation for verification of the claimed exaction credit amount. Should the developer fail to provide documentation for verification of the claimed credit amount, the development agreement / memorandum provides that LFUCG shall close the agreement out at 80% of the exaction credit amount granted by the agreement.

However, LFUCG allows developers to begin using exaction credits granted by a development agreement / memorandum to satisfy required exactions and obtain building permits, up to an amount of 80% of the estimated exaction credits (consistent with the 80% close out number). If LFUCG closes out an agreement / memorandum at 80% of the exaction credit amount because the developer has not provided documentation for verification, but has allowed a developer to utilize more than 80% of the exaction credits granted by the agreement / memorandum along the way, a negative balance will be shown on the exaction credit statement maintained by the Department of Finance. The developer "overspent" exaction credits by spending in excess of the 80% closeout threshold.

Legally, the cleanest approach to addressing negative exaction credit statement balances would be to avoid negative balances by limiting the developer to using no more than 80% of the exaction credits granted by the agreement, pending verification of actual costs in excess of that amount – that way, if LFUCG resorts to closing out an agreement at 80% based on a failure to provide documentation for verification, there should be no resulting negative balance on the exaction credit statement, as LFUCG did not allow the developer



to spend credits in excess of the 80% closeout threshold. It is our understanding that this is the current policy and practice of LFUCG, and that this policy and practice will continue to be enforced.

Because exaction credits are awarded and used pursuant to a development agreement / memorandum between LFUCG and the developer, that agreement / memorandum would control the granting of exaction credits. Whether a negative exaction credit statement balance on an existing development agreement / memorandum can be “netted” against a positive exaction credit statement balance on a separate existing development agreement / memorandum would depend on an examination of the respective terms of each agreement and a consideration of Article 23C of the Zoning Ordinance as applied thereto, which would have to be evaluated on a case-by-case basis. Going forward, LFUCG can draft future development agreements to expressly provide that a developer is not authorized to use the exaction credits granted by the agreement in excess of the 80% closeout threshold unless and until the developer verifies actual costs in excess of that threshold, and in the event that the agreement is closed out at 80% and the developer has utilized exaction credits in excess of the 80% threshold, any exaction credits used in excess of the 80% closeout threshold are subject to re-capture in a future development agreement / memorandum. Expressly limiting developers to the use of 80% of estimated exaction credits pending verification under Article 23C of the Zoning Ordinance, coupled with the addition of language to the development agreement / memorandum that expressly authorizes the re-capture of any negative exaction credit balance in a future development agreement / memorandum, would be a legally defensible approach to avoiding and addressing negative exaction credit statement balances.

Chief Administrative Officer Response:

I concur.

Finding #3: Lack of Compliance with ECAC Policy Contributed to Negative Balances in Several Credit Statements

Priority Rating: High

Condition:

We were informed by an employee who reports to the Chief Development Officer that the Exaction Credit Advisory Committee (ECAC) approved a policy in August 2004 that dealt with the question of how exaction credits approved under an executed Design and Construction Memorandum or Development Agreement may actually be applied when



the work has not been fully completed. We obtained a copy of this policy and noted it states, “Credits shall not be granted in excess of 80% of the total estimated credits as stated in the Development Agreement or Design and Construction Memorandum unless and until the developer has completed all actions and provided all documentation necessary to verify and finalize all credits due.” Therefore, we were advised that developers should not be allowed to use more than 80% of the estimated exaction credits as stipulated in the Development Agreement or Design and Construction Memorandum unless the project has been closed out.

We obtained a population of all credit statements from the Department of Finance. We noted that there were 14 credit statements that reported a negative balance. A negative balance indicates there were more exaction credits used by the developer than the amount of credits eventually approved by the ECAC per the Close-Out Letter, and the credits were therefore overspent. These agreements eventually closed out in an amount less than initially estimated in the original agreement/memorandum, often times at 80% of the initially awarded amount. By the time these projects closed out, more credits had been utilized by the developer than the amount of credits approved during close-out, resulting in a negative balance.

If the developer’s use of credits had been limited to 80% of the estimated credits in the Agreement/Memorandum as required by policy established by the ECAC in 2004, these 14 negative balances would have been significantly reduced or eliminated entirely. We noted that all 14 of these credit statements applied to several projects that began a number of years ago (some of which reported developer’s use of credits as far back as 2002) and prior to when the current credit statement custodian’s employment began. We also noted there are currently six credit statements that represent projects that are still in progress and have not been issued a Close-Out Letter, and all six of these credit statements limit the credits available for developer use to 80% of the amount awarded in the initial agreement in compliance with ECAC policy.

Effect:

Failure to limit developer’s use of exaction credits to 80% prior to close-out as required by ECAC policy creates the risk that a project may close out in an amount less than initially estimated in the agreement/memorandum, and therefore result in negative credit balances.

Recommendation:

LFUCG should enforce the policy adopted by the ECAC in August 2004 and not allow developers to use more than 80% of the credits estimated in the original contract until the



agreement/memorandum has been closed out or until the developer can “provide all documentation necessary to verify and finalize all credits due” as stipulated by policy. This will reduce the likelihood that developers will use more credits than the amount of credits approved during project Close Out.

Commissioner of Finance and Administration Response:

I concur with Internal Audit. Agreements that haven’t been closed out will be corrected if necessary and all future credit statements will be set up at 80% of estimated credits.

Chief Administrative Officer Response:

I concur.

Finding #4: Some Discrepancies Identified Between EAMP Database and Credit Statements

Priority Rating: High

Condition:

We were informed that the EAMP Database contains the entire population of all exaction transactions and activity, including the reporting of all exaction credits used by developers. We reconciled the amount of exaction credits utilized as reported by the EAMP Database to the amount of exaction credits utilized per the credit statements we obtained from Finance. Our expectation was that all credits reported as utilized in the EAMP Database would be reported as utilized in one of the credit statements. Likewise, we expected all credits reported as utilized in the credit statements to also be reported as utilized in the EAMP Database (i.e., a two-way match).

We noted the EAMP Database reported that developers utilized total exaction credits in the amount of \$38,984,205.08 since the inception of the exaction program. All of the credit statements provided to us reported developers utilized exaction credits in the amount of \$38,791,394.04. The \$192,811.04 difference between these two amounts equals approximately 0.5% of all credits utilized in the EAMP Database. In our opinion, a variance of 0.5% indicates the credits reported as used in the credit statements are reasonable. The discrepancies that make up the difference of \$192,811.04 are broken out below, after adjusting for a \$0.82 rounding difference:



Exaction credits reported as utilized in the EAMP database but not included in a credit statement:

\$310,439.53 Gess Property Development:

We noted that the EAMP Database reported \$310,439.53 of non-sewer credits utilized in the Gess Property Development (related to Plats N-886, N-885, N-884 & N-910), but these credits are not included in any of the developer's credit statements we obtained from Finance. The use of these credits could be included with the credit statement for Agreement R-456-2010 as it was granted \$430,000 of non-sewer credits from a transfer of property. However, the current credit statement custodian advised the credit statement for R-456-2010 has never been created (see additional finding below). Although these non-sewer credits were not included in a credit statement, they were reported in the detail that summarized PeopleSoft General Ledger activity we obtained from Finance. We also noted the assets related to R-456-2010 were capitalized in the PeopleSoft General Ledger.

\$79,561.01 Gess Property Development:

We noted the EAMP Database reported \$79,561.01 of sewer credits utilized in the Gess property Development (related to Plats N-886 & N-885) but these credits are not included in any of the developer's credit statements we obtained from Finance. The utilization of these \$79,561.01 sewer credits need to be added to a sewer credit statement for Gess Property Development. Although these sewer credits were not included in a credit statement, they were reported in the detail that summarized PeopleSoft General Ledger activity obtained from Finance. We also noted the assets related to these credits were capitalized in the PeopleSoft General Ledger.

Exaction credits that are reported in a credit statement but not included in the EAMP database:

(\$90,432.88) Phelps Property Development:

We noted the credit statement for R-282-2002 reported the use of \$90,432.88 of non-sewer credits at the very top of the credit statement; however, we could not locate these credits reported as used in the EAMP Database. We also noted the credit statement was not reduced for the \$90,432.88 of non-sewer credits.



(\$106,757.44) Phelps Property Development:

We noted the credit statement for R-282-2002 reported the use of \$106,757.44 of sewer credits at the very top of the Credit Statement; however, we could not locate these credits reported as used in the EAMP Database. We also noted that the credit statement was not reduced for the \$106,754.44 of sewer credits.

Effect:

Failure to report all utilized exaction credits in the credit statements/EAMP database will result in misreporting the developer's credit statement balance.

Recommendation:

Management should investigate these discrepancies and make any appropriate changes to the credit statements / EAMP Database.

Commissioner of Finance & Administration Response:

I concur with Internal Audit. We will investigate the discrepancies in coordination with the Division of Planning and make appropriate adjustments.

Chief Administrative Officer Response:

I concur.

Finding #5: Missing Credit Statement

Priority Rating: High

Condition:

During the preliminary phase of the audit, we received a population of all written exaction agreements and memoranda. From this population, we performed test work to determine if every written agreement and memorandum in which exaction credits were granted to developers was accompanied by a credit statement, which would report the amount of exaction credits granted, the amount of exaction credits utilized by the developer, and finally a net balance of credits available for future use. Of the 43 agreements/memoranda tested, we identified one agreement in which a credit statement had not been created.

When we informed the Department of Finance, the credit statement custodian advised he was not sure why a credit statement had not been created for this agreement when it became effective in 2010. We were informed this agreement was approved several years



prior to the current credit statement custodian's employment at LFUCG. We also noted that although a credit statement had not been created for this agreement, it was included in the detail that summarized PeopleSoft General Ledger activity obtained from Finance.

Effect:

The absence of a credit statement for every exaction agreement/memorandum could result in misreporting the developer's credit balance.

Recommendation:

Department of Finance management should create a credit statement for this agreement.

Commissioner of Finance & Administration Response:

I concur with Internal Audit. A credit statement will be created and activity recorded. Credit statements will continue to be created at the time of approval of new agreements and memoranda.

Chief Administrative Officer Response:

I concur.

Finding #6: Unable to Locate Developer's Written Requests for Exaction Activity
Priority Rating: High

Condition:

We performed a walkthrough of four credit statements, each representing a different agreement or memorandum. As part of each walkthrough, we requested to see written documentation in which the developer requested to use exaction credits on each lot for which exaction credits were utilized or transferred. According to the language of each agreement, each use, application, or transfer of exaction credits shall be reported in writing to the LFUCG Department of Finance. However, we were unable to obtain many of these requests as the credit statement custodian advised he did not have many of the older written requests. We noted that many of these requests would have been as much as fifteen years old. In many cases, we were able to locate evidence that these requests did exist at one time because they were mentioned in notes in the EAMP Database.



Effect:

The absence of written requests to use or transfer exaction credits reduces the ability to provide evidence of the developer's intent to use or transfer the credits.

Recommendation:

Management should create a procedure requiring written documentation be obtained from the developer every time a request is made to use or transfer exaction credits. These written requests should be permanently retained along with the related credit statements.

Commissioner of Finance & Administration Response:

I concur with Internal Audit. All requests going forward will be retained electronically in the file where the corresponding credit statements are maintained.

Chief Administrative Officer Response:

I concur.

Finding #7: Exaction Rate Table Needs to be Updated**Priority Rating: High****Condition:**

Section 23C-5(b) of Article 23 in the LFUCG Code of Ordinances states, "The exactions set forth in this Article are based upon good faith estimates of the costs of acquiring lands for open space, parks, and infrastructure, and the costs of constructing system improvements. The Lexington-Fayette Urban County Government acknowledges that a cost estimate, which as closely as possible approximates the actual construction cost, is in the best interest of the operation of the exaction program. Therefore, beginning four (4) months after the date of the adoption of the resolution establishing the Exaction Schedule, and on a quarterly basis thereafter, the Department of Finance and the Department of Public Works shall review the methodology report and recommend the increase or decrease of all exactions, with the exception of the Open Space Exactions, based upon the actual costs of acquiring properties or interests in properties and the actual costs of constructing system improvements."

The last time the Council was presented a review of the Exaction Rate Table was in 2010. The Exaction Rate Table is used by professional engineers in the Division of Engineering to calculate the exaction fee for each property. We were informed that an employee who reports to the Chief Development Officer is currently working on an Exaction Rate Table update.



Effect:

Failure to update the Exaction Rate Table as required by ordinance can result in exaction fees being calculated using outdated cost estimates.

Recommendation:

An updated Exaction Rate Table should be completed and presented to Council. The requirement that the Exaction Rate Table be reviewed quarterly should also be evaluated to determine if the expected benefit of performing this evaluation every quarter justifies the time and cost to do so. If the estimated costs of acquiring lands for open space, parks, infrastructure, and constructing system improvements is fairly stable, it may be more practical to update the Exaction Rate Table on a semi-annual or annual basis. Whatever update interval is chosen, the update requirement should be complied with on a consistent basis.

Commissioner of Finance & Administration Response:

I concur with Internal Audit. The Council approved the March 1, 2020 Rate Table Update in March. Per discussion with the Office of the Chief Development Officer and as previously presented to Council, the Rate Table will be updated on an annual basis with the next Rate Table update occurring in March 2021. Division of Planning staff is drafting a Zoning Ordinance Text Amendment to formalize the change in the frequency of the Rate Table update requirement from quarterly to annually.

Chief Administrative Officer Response:

I concur.

Finding #8: Two Credit Statements Need to be Updated with Close-Out Amount

Priority Rating: High

Condition:

During the audit, Department of Finance personnel provided us with the population of all credit statements. Of these 52 credit statements, we identified two that had been issued a Close-Out Letter, but the amount of exaction credits granted in the credit statements did not agree with the exaction credits granted in the Close-Out Letters, causing the net balance of the credit statements to be misstated. One credit statement included \$333,049.59 more credits than the Close-Out amount, while the second credit statement reported \$132,510.40 fewer credits than the Close-Out amount.



The credit statement custodian advised this was an oversight as he has not dealt with those particular agreements and their related credit statements since the Close-Out Letters were issued, and therefore these credit statements had not been updated with the Close-Out Amounts. We noted that both of these agreements were included in the General Ledger Summary Schedule obtained from Finance, and the assets related to each agreement were recorded in the PeopleSoft General Ledger in the amount reported in the Close-Out Letter.

Effect:

Failure to update credit statements with close-out amounts could result in misreporting the developer's net balance and/or allowing developer to utilize more credits than allowed.

Recommendation:

Management should update both credit statements for which Close-Out Letters have been issued so they report the amount of exaction credits approved and available for use by the developer.

Commissioner of Finance & Administration Response:

I concur with Internal Audit. The lack of an update was an oversight and the credit statements will be updated with the closeout amount.

Chief Administrative Officer Response:

I concur.

Finding #9: Correcting Journal Entry Needed for a Small Number of Exaction Related Assets

Priority Rating: High

Condition:

We were informed that when an agreement closes out and a Close-Out Letter is issued, the newly constructed infrastructure related to the agreement (e.g. road, sewer, etc.) is capitalized in the PeopleSoft General Ledger in the amount approved by the Exaction Credit Advisory Committee and reported in the Close-Out Letter. We obtained an "Exaction Asset Listing" from the Division of Accounting which listed 43 exaction related assets and their respective values. We performed a test to verify these assets were capitalized in the amount consistent with the amounts reported in the Close-Out Letters. We identified three assets (Asset ID # 94785, 94786, & 94787) where book values did not reflect the amount reported in Close-Out Letters. The three assets combined were



reported in the General Ledger in an amount that was \$213,647.51 less than the amount reported in the Close-Out Letters.

Accounting personnel advised that LFUCG issued Close-Out Letters for several agreements in July 2018 and they had recorded the accounting entries for all of those agreements that were closed out during Fiscal Year 2019. However, Division of Accounting personnel advised these particular three assets were related to agreements that closed out in October 2008 and no accounting adjustments were made to them since they closed out years ago. Accounting personnel advised they would record a journal entry to correct this oversight in January 2020 so that the book value of these assets are consistent with the amount reported in the corresponding Close-Out Letters.

We also identified one additional Memorandum which was closed out but no assets were capitalized for this project. We brought this to the attention of an Accountant Senior in the Division of Accounting, who researched the issue and informed us that an adjusting entry in the amount of \$196,963.34 would be posted in the month of February 2020 to correct this oversight.

Effect:

Recording exaction assets in amounts less than reported in Close-Out Letters will result in the undervaluing of assets.

Recommendation:

The Division of Accounting should post correcting journal entries to adjust the book values of exaction assets identified above to agree with the amount reported in the Close-Out Letters.

Commissioner of Finance & Administration Response:

I concur with Internal Audit. The corresponding entries have been made.

Chief Administrative Officer Response:

I concur.



Finding #10: Land Included in Some Closed Agreements Has Not Been Transferred to LFUCG
Priority Rating: High

Condition:

We noted eight instances where exaction agreements that included land had been closed out, but the land had not been transferred to the LFUCG. We were advised by various management personnel that LFUCG will not take ownership of the land and the land will not be transferred into LFUCG's name until the developer requests LFUCG take ownership. Discussions with management indicated there may also be some question about the condition of these parcels of land, and whether they were greenspace that could not be developed. Our audit did not include an evaluation of the condition of the land.

Effect:

LFUCG has not taken ownership of land available to it via closed out exaction agreements.

Recommendation:

Senior management should pursue transferring ownership of the land to the LFUCG and adjusting land book values in the General Ledger.

Commissioner of Finance & Administration Response:

I concur with Internal Audit. The Division of Engineering is coordinating with the Division of Finance to identify these parcels of land and develop a schedule to transfer ownership to the LFUCG.

Chief Administrative Officer Response:

I concur.

Finding #11: Five Close-Out Letters Could not be Located
Priority Rating: High

Condition:

When projects are completed, the developer will submit supporting documentation detailing the actual cost of construction which will likely differ from the initial approved cost estimate. The supporting documentation is reviewed by the Exaction Credit Advisory Committee (ECAC) and if approved, the agreement or memoranda is "closed out" and a Close-Out Letter is mailed to the developer notifying them of the final amount of exaction credits they were awarded.



We were informed by an employee reporting to the Chief Development Officer that there were five agreements that had been closed out for which Close-Out Letters did not exist. We noted each of these agreements were at least twelve years old. The employee advised these projects were closed prior to his employment and he was unable to locate the Close-Out Letters for the related agreements. He also informed us he could not find any reference to closeouts for these agreements in the ECAC Minutes. This employee explained that he obtained close-out amounts for these agreements from other sources (financial records, discussion with developer, etc.).

Effect:

The Office of Internal Audit acknowledges that these agreements were closed out at least twelve years ago, before employees currently assigned to exactions were responsible for them. However, it is apparent based on the evidence that the process to close out exactions was not complied with at the time these five agreements were closed out.

Recommendation:

The process of having agreements closed out by the ECAC and the issuance of a Close-Out Letter to the developer should be documented in an exactions procedure and consistently complied with.

Commissioner of Finance & Administration Response:

I concur with Internal Audit. We will discuss the documentation of the procedure with the Office of the Chief Development Officer where that process is managed.

The process of closing out agreements/memoranda is outlined in each approved agreement/memorandum, which generally requires completion of improvements, which is followed by adjustment of final costs verified by the Developer to the satisfaction of the LFUCG.

In addition to the close out process above, staff will coordinate with the Exaction Credit Advisory Committee to develop a procedure requiring the annual review of all agreements / memoranda to identify projects that are completed but not yet closed out. The annual review will take place in the 4th quarter of each calendar year to provide adequate time for close outs to be completed prior to the Rate Table update adoption each March.

Chief Administrative Officer Response:

I concur.

