GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE INSPECTOR GENERAL

AUDIT OF THE FIXED-COSTS ALLOCATION PROCESS

CHARLES J. WILLOUGHBY
INSPECTOR GENERAL

OIG No. 05-2-10MA **September 28, 2006**

GOVERNMENT OF THE DISTRICT OF COLUMBIA
Office of the Inspector General

Inspector General

September 28, 2006

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Dear Mr. Reiskin, Dr. Gandhi, Ms. Mitten, and Ms. Peck:

Enclosed is our final report summarizing the results of the Office of the Inspector General's (OIG) Audit of the Fixed-Costs Allocation Process (OIG No. 05-2-10MA).

Our report contains 17 recommendations for necessary action to correct deficiencies. We received management responses from: (1) the Office of the Chief Technology Officer on June 1, 2006; (2) the Office of the Chief Financial Officer, Government Operations Cluster on July 17, 2006 (OCFO); (3) the Office of the City Administrator on August 1, 2006; and (4) the Office of Property Management on August 21, 2006.

The OCTO response addressed fully three of the four recommendations directed to OCTO. We request that OCTO state specific action planned in addressing the fourth recommendation, Recommendation 8.

The OCFO response addressed Findings 1, 2, 3, and 6 in general rather than specific recommendations. OCFO agreed with Findings 2 and 3. OCFO disagreed with Finding 1 related to moving the date of the memorandum of understanding (MOU) summits. The OCFO also disagreed with Finding 6 but provided us with additional documentation to support its position, which we consider responsive. We request that OCFO reconsider its response to Finding 1.

The OCA response to Recommendations 4 and 5 fully addressed the recommendations.

The OPM response stated agreement with Recommendations 1 through 5. Corrective action taken or planned by OPM in response to Recommendations 13, 14, and 15 fully addresses the need for improvement. OPM's response to Recommendations 11 and 12 partially addressed our concerns. Accordingly, we request that OPM reconsider its response to Recommendations 11 and 12.

Management comments are incorporated where appropriate. The full text of each management response is included at Exhibits B through E.

Generally, audit recommendations should be resolved within 6 months of the date of the final report. Accordingly, we will continue to work with management to reach final agreement on the unresolved issues in this report. Management's final comments on the unresolved issues should be provided within 60 days of the date of this report.

If you have questions or desire an exit conference prior to preparing your response, please contact William J. DiVello, Assistant Inspector General for Audits, at (202) 727-2540.

Sincerely,

Charles J. Willoughby
Inspector General

CJW/rj

The Honorable Anthony A. Williams, Mayor, District of Columbia (1 copy)
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Ms. Sharon Anderson, Deputy Chief of Staff, Policy and Legislative Affairs (1 copy)
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Attention: Johanna Hardy (1 copy)
The Honorable Joseph Lieberman, Ranking Minority Member, Senate Committee on Governmental Affairs, Attention: Patrick J. Hart (1 copy)

AUDIT OF THE FIXED-COSTS ALLOCATION PROCESS

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OVERVIEW

This report summarizes the results of the Office of the Inspector General's (OIG) Audit of Fixed-Costs Allocation (OIG No. 05-2-10MA). The audit was conducted as a result of a request by the City Administrator.

The Office of Finance and Resource Management (OFRM), the Office of the Chief Technology Officer (OCTO), the Office of Property Management (OPM), the Office of Budget and Planning (OBP), and user agencies play major roles in the forecast and budgetary processes for the fixed costs incurred by the District government.

The District government incurs approximately $200 million in fixed costs annually. Fixed costs are general and administrative in nature and include commodities such as rent, occupancy, telecommunications, utilities, security, etc. Although these costs are called "fixed costs," that is somewhat of a misnomer. "Fixed" refers to the costs being necessary rather than non-variable.

District agencies may not always "buy-in" or "take ownership" of their share of these costs because the costs are: (1) mostly procured centrally by OPM and OCTO; (2) not always controllable by the agencies; and (3) not direct program costs. However, during the budget or forecast process, it is imperative that agencies take responsibility for identifying their "fixed costs" needs as accurately as possible so that their share of these costs can be estimated as accurately as possible.

Our audit objectives were to determine whether: (1) adequate policies, guidelines, and procedures for fixed-costs allocation exist; (2) District personnel are complying with prescribed policies and procedures related to fixed-costs allocation; (3) internal controls over fixed-costs allocation are adequate; and (4) fixed-cost allocations were proper and accurate.

CONCLUSIONS

This report contains six findings that detail the conditions found during the audit. The first finding addresses the need for OFRM to improve the Fixed-Costs Memorandum of Understanding (MOU) process by executing the MOU timelier, wording the MOU more exacting, and enhancing the signatory section of the MOU. For fiscal years (FYs) 2004 and 2005, OFRM executed the MOU during a conference between OFRM, seller agencies, and buyer agencies just before the new fiscal year began. However, it was not clear as to what officials should have been the signatories on the MOU. Also, for FYs 2004 and 2005, the signatures on the MOU were not always decipherable and the positions and titles of the signers were not stated. Further, the language in the MOU confused seller, buyer, and payer agencies. As a result, the authority governing the MOU

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was weakened, and the MOU did not have the managerial accounting and budget impact it should and could have had.

The second finding addresses deficiencies relating to the forecast process for telecommunications expenditures. Agency telecommunications coordinators (ATCs) do not always provide OCTO with sufficient information that reflects the telecommunications needs of their respective agencies and should be included in the forecast. As a result, the forecast process may not be as accurate as possible and may lead to spending pressures or under spending. Additionally, agencies' variable telecommunications needs are not fully considered during the forecast and budgetary processes.

The third finding addresses deficiencies in the inventory of telecommunications lines. ATCs do not know the inventory of telecommunications lines and services assigned to their respective agencies. Adequate knowledge of the inventory composition is necessary to perform a meaningful forecast for telecommunications expenditure for any budgetary period. Most agencies believe that because OCTO coordinates and oversees their telecommunications budget, OCTO should take responsibility for every aspect of telecommunications, to include inventory management. As a result, agencies do not perform a proper review of their telecommunications bills prior to payments. Payments have been made for telecommunications lines that were either not needed or not known to exist.

The fourth finding noted that OPM performed minimal monitoring of the operational pass-through component of rental costs, and did not have any written policies and procedures governing the oversight and monitoring of operational costs. The failure to monitor operational expenses prevents the District from identifying excessive overcharges resulting from errors in landlords' statements.

The fifth finding noted that OPM did not properly allocate and certify rental forecasts and expenditures for the Department of Human Services, Department of Health, and the Department of Mental Health. As a result, OFRM allocated and charged rental expenditures to the incorrect agencies. This condition will hinder the Office of Budget and Planning (OBP) in developing correct estimates for agencies' fixed-costs budget.

Lastly, the sixth finding notes that while OFRM was observed to be generally accurate in processing rent payments, the OFRM made duplicate rental payments to one lessor. Duplication of rental payments results in increased expenditures for the District and inefficient use of resources.

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OTHER MATTERS OF INTEREST

Based on the OPM Director's response to the draft report and subsequent discussions held with the Director, we agreed to address additional concerns about the process for allocating and charging fixed costs. While there is agreement that our recommendation for moving the MOU process to coincide with the budget process creates an enhanced budgeting tool, OPM notes that problems remain with the current procedures used to collect fixed costs from individual agency budgets. It should be noted that we did not perform an audit evaluation of fixed-costs collection methodologies and are presenting these comments to highlight the difficulties principle agency stakeholders (OFRM, OPM, DPW, and OCTO) and the District agencies face in allocating and managing fixed costs. In this regard, we are also presenting some potential solutions to the fixed-costs allocation problem that were discussed with OPM and other agency officials.

As the OPM Director noted, at some point in the fiscal year, OFRM collects the fixed-cost amounts reflected in the most recent estimates prepared by OPM. It is our understanding that similar OFRM collection efforts are undertaken with fixed costs managed by DPW and OCTO. These collections from agency fixed-cost budgets are made regardless of whether or not the most recent estimate exceeds the budgeted amount. As currently configured, OFRM is empowered to collect fixed-cost amounts without agency consent (many District agencies refuse to sign the MOUs), which could potentially place the agencies in a temporary deficit position. It is also our understanding that OFRM will initiate several fixed-cost collections in excess of agency fixed-cost budgets to cover the spending pressure generated by increases in fixed costs. In this scenario, the agencies faced with increased fixed-cost charges have few options other than to tap unused operating funds to cover the charges or otherwise operate in a deficit position. As presented to us, we believe that District management officials need to address this problem.

Several ideas were proffered that should be considered in future discussions of how best to remedy or otherwise revise existing fixed-cost allocation methodologies. The suggestions expressed below are intended for District management officials to discuss and consider, but are not intended to limit or restrict the use of other creative or known methodologies for allocating fixed costs.

<u>Global Funding of Excess Fixed Costs</u> – OFRM could track and accumulate unbudgeted, across-the-board increases in fixed costs as a city-wide spending pressure as opposed to the current method of allocating increases in fixed costs to agency budgets. The accumulated fixed-cost spending pressure could be funded globally from unused operating funds or, if needed, from reserves. The actual fixed costs incurred by each agency would be retained for future fixed-cost budgeting purposes.

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Incremental Assessments - OFRM could perform incremental assessments of all agency program costs, including fixed costs, to identify unused agency money that would be available for reallocation to other agencies to cover a spending pressure that arose from increased fixed costs at those agencies.

Managing Fixed Costs Centrally – As opposed to the current method of budgeting and allocating fixed costs to each agency, OFRM could manage all fixed costs centrally by preparing one budget for all agencies and managing all fixed costs in one place. There is an obvious benefit to this option because it immediately eliminates the problems with allocating fixed costs to individual District agencies. However, unless an accounting adjustment is made at year-end to reallocate each agency's share of fixed costs, the true costs for each District agency would be distorted. Another concern is that centrally managed fixed costs would prove difficult to manage since OFRM would be required to manage a sizeable, complex fixed-cost budget for 60 plus District agencies. Further, the existing incentive agencies now have to monitor and control fixed costs would be weakened if ownership of these costs passes to OFRM.

We presented this *Other Matters of Interest* section to provide District management officials with potential alternatives to the existing fixed-cost allocation methodology. We believe a focused discussion on this issue by the agencies involved in the allocation process (OFRM, OPM, DPW, and OCTO), with the participation of principle District agencies, will help develop the best solution for budgeting and allocating the District's fixed costs.

SUMMARY OF RECOMMENDATIONS

We directed 17 recommendations to the OCFO, OFRM, OCTO, OPM, and the Office of the City Administrator that we believe are necessary to correct the deficiencies noted in this report. The recommendations, in part, center on:

- Executing the Fixed-Costs Memorandum of Understanding (MOU) in a more timely manner, closer to the budget proposal date;

- Improving the language of the MOU so that the parties and their responsibilities as seller agencies, buyer agencies, and payer agency or administrator are accurately identified and described;

- Requiring the MOU to be signed by senior officials of the Office of the Chief Financial Officer, the Office of Property Management, the Office of the Chief Technology Officer, and the user agencies;

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- Enhancing the signatory section of the MOU to include lines for the printed names of the signers, their titles or positions, and their agencies;

- Requesting that a Mayor's Order or directive on fixed costs be issued, which clearly spells out the responsibilities of: (a) agencies that procure commodities categorized as fixed costs for use by other agencies; (b) agencies using these commodities; and (c) the administrative or paying agency;

- Developing uniform policies and procedures for training agency telecommunications coordinators (ATCs) on the forecast and budgetary processes;

- Offering classes to ATCs periodically to inform them of updates, training new ATCs, and developing an ATC operating manual;

- Working with agency heads to ensure that all requests for telecommunications services (RTS), and approvals thereof, are for items that were budgeted for;

- Updating periodically the telecommunications inventory of lines and services;

- Developing guidelines as to adequate telecommunications staffing levels for agencies;

- Developing written policies and operating procedures governing oversight and monitoring of operational costs in order to improve management controls surrounding the operational pass-through component of rental expenditures;

- Improving management oversight and monitoring of lessors' books and records to identify the validity of operating expenses prior to certifying payment;

- Replacing manual worksheets with automated systems to improve management functions;

- Establishing quarterly sessions with Agencies' Area Asset Managers to confirm the proper allocation and assignment of space for District leased facilities as a means of improving agency-related fixed-cost estimates;

- Ensuring that OPM, OFRM, and user agencies have compatible/uniform data systems to accurately and efficiently process forecasts data;

- Performing reconciliations of the OPM monthly rent roll and the OFRM monthly rental summary report in order to identify errors in lessors' accounts.

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This will allow OPM to make adjustments, prior to certifying rental payments in subsequent months; and

- Seeking reimbursement of overpayment of rental expenditures from lessors.

CORRECTIVE ACTIONS

The OCTO response addressed fully three of the four recommendations directed to OCTO. We request that OCTO state specific action planned in addressing the fourth recommendation, Recommendation 8.

The OCFO response addressed Findings 1, 2, 3, and 6 in general rather than specifically. OCFO agreed with Findings 2 and 3. OCFO disagreed with Finding 1 related to moving the date of the memorandum of understanding (MOU) summits. The OCFO also disagreed with Finding 6, but provided us with additional documentation to support its position, which we consider responsive. We request that OCFO reconsider its response to Finding 1.

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The OPM response stated agreement with Recommendations 1 through 5. Corrective action taken or planned by OPM in response to Recommendations 13, 14, and 15 fully addresses the need for improvement. OPM's response to Recommendations 11 and 12 partially addressed our concerns. Accordingly, we request that OPM reconsider its response to Recommendations 11 and 12.

INTRODUCTION

BACKGROUND

On October 1, 1998, as a result of the District's program of management reform, the Department of Administrative Services (DAS) was restructured. Four new agencies were created to provide DAS's shared services and centralized payments within three key program support areas, to include: Procurement, Technology, and Asset Management.
The new agencies included:

- Office of Finance and Resource Management
- Office of the Chief Technology Officer
- Office of Property Management

Office of Finance and Resource Management (OFRM)

OFRM is under the management control of the District's Office of the Chief Financial Officer. Its mission is to provide timely, efficient, and accurate fiscal management of shared financial services, resource management/central payments, and capital management.
In this capacity, OFRM pays utility bills and serves as a liaison among OCTO, OPM, and client agencies.

OFRM uses two models to provide shared financial services to agencies, the shared services model and the centralized payment model. Under the shared services model, OFRM makes sharing of resources possible by providing various financial and budgetary services to user agencies. Currently, about 68 agencies, with a combined fixed-costs annual budget of approximately $200 million, have executed memorandums of understanding (MOU) with OFRM to manage their fixed costs.

Under the centralized payments model, consolidated fixed-costs payments are made to vendors/service providers. Thus, the centralized payments model is conducive to obtaining vendor volume discounts. OFRM tracks historical, monthly fixed-costs usage patterns for each of its client agencies. This information is used in developing subsequent forecasts and budgets.

OFRM is responsible for providing financial oversight of and payment for 11 commodities of fixed costs incurred by District agencies, to include:

1. Rent
2. Telephone
3. Electricity
4. Security
5. Natural Gas
6. Water

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7. Custodial
8. Fuel
9. Occupancy
10. Steam
11. Postage

Table I below gives a breakdown of the expenditures by commodities, amount, and percentage of total costs for FY 2004.

Table I. – Fiscal Year 2004 Fixed-Costs Expenditures by Commodity.

Commodity	Amount	Percent of Total Costs
Custodial	$4,033,811	2%
Electricity	$24,986,312	13%
Fuel	$6,236,021	3%
Natural Gas	$16,518,055	8%
Occupancy	$3,727,566	2%
Phone	$24,344,487	12%
Rent	$83,659,784	43%
Security	$24,430,464	12%
Steam	$1,067,498	1%
Water	$7,223,152	4%
TOTAL	**$196,227,150**	**100%**

The forecast process for the District's fixed costs is a coordinated effort by OFRM, OPM, OCTO, and the user agencies.

Office of Property Management (OPM)

OPM is responsible for facility management, portfolio management, protective services, postal services, facility repairs, capital and constructive services, and energy management. In addition, OPM provides the forecast that is used in estimating and managing the District's fixed costs under OPM's purview, and in receiving, reviewing, and certifying fixed costs to be paid.

To develop fixed-costs estimates, OPM:

a. consults with agency representatives regarding fixed costs,
b. prepares estimates of usage patterns based on historical trends and actual usage, and
c. analyzes historical costs and calculates anticipated costs based on the CPI and projected price level changes.

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For the rent forecast, the Portfolio Management Division of OPM considers the following costs: base rent, annual escalations, and operational pass-through expenses. The annual forecast for the base rent and escalation is predictable because the terms are included in the lease agreement. Operational expense, the variable component of the rental forecast, is not as predictable because it is based on prior year actual expenditures and changes in the consumer price index. In making estimates for operational costs, OPM compares the actual expense for the leased facility with a base rate that is established in the first year of the lease. If the actual expense exceeds the base rate, the difference becomes the basis for forecasting the operating expense.

Operational cost is an expense that the lessor pays or incurs or becomes obligated to pay in connection with the operation, management, repair, and maintenance of the leased property and common areas. Other pass-through costs include real estate taxes, parking, and utilities. Operating costs include:

1. Management fees that include wages, salaries, educational, travel and professional fees, and salaries for lessor executive personnel, and salaries for individuals engaged in the operation, repair, and maintenance or security of District agencies' rented and common areas;
2. Costs of performance by lessor service agreements for HVAC maintenance, trash removal, parking lot cleaning, snow removal, janitorial services, control alarm services, window cleaning, elevator maintenance and landscaping;
3. Utilities including water and sewer;
4. Cost of casualty and liability insurance; and
5. Accounting and legal costs incurred by the lessor.

Office of the Chief Technology Officer (OCTO)

OCTO operates under a centralized model which enables cluster managers to provide customized support at the agency level. OCTO develops guidelines and procedures for use by agencies in the procurement and management of all telecommunications goods and services. OCTO's responsibilities include developing and enforcing policies, procedures, and standards regarding the economic acquisition and effective use of telecommunications technology by agencies, departments and employees of the District government. Further, OCTO assists agencies in forecasting the variable components of their telecommunications needs.

Office of Budget and Planning (OBP)

OBP provides effective budgeting and planning assistance for both buyer and seller agencies. In addition, OBP provides balances of Intra-District funds remaining in the budget.

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OBJECTIVES, SCOPE, AND METHODOLOGY

The audit objectives were to determine whether: (1) adequate policies, guidelines, and procedures for fixed-costs allocation exist; (2) District personnel are complying with prescribed policies and procedures related to fixed-costs allocation; (3) internal controls over fixed-costs allocation are adequate; and (4) fixed-costs allocations were proper and accurate.

We conducted the audit by examining policies, procedures, and processes involving the fixed-costs forecasts at OPM, OCTO, OFRM, OBP, and six selected buyer or user agencies. We interviewed officials and staff, examined invoices and billing, analyzed leases and budgets, and reviewed memorandums of understandings and other documentation.

The six user agencies tested were the:

1. Department of Public Works (DPW);
2. Metropolitan Police Department (MPD);
3. Department of Human Services (DHS);
4. Fire and Emergency Medical Services Department (FEMS);
5. Department of Mental Health (DMH); and
6. Department of Health (DOH).

The audit covered FYs 2004 and 2005. We conducted the audit in accordance with generally accepted government auditing standards, and included such tests as we considered necessary under the circumstances. We did not review the underlying structures and processes of the computer information systems which generated and maintained the databases under audit nor did we assess the reliability of such data. However, we did examine source and supporting documents, and analyzed and compared accounts to verify the reliability of the data. This final report contains revisions to the draft report that the OIG issued on May 15, 2006. The revisions were based on OPM's initial response to our draft report and subsequent discussions held with the Director of OPM. Accordingly, we address additional concerns about the process for allocating and charging fixed costs. Further, based on additional information provided by OPM, we modified Finding 4 of this report.

PRIOR AUDITS

There are no prior audits of the process for allocating fixed costs incurred by the District government.

FINDINGS AND RECOMMENDATIONS

FINDING 1. FIXED-COSTS MEMORANDUM OF UNDERSTANDING

SYNOPSIS

The OFRM needs to improve the Fixed-Costs Memorandum of Understanding (MOU) process by executing the MOU timelier, wording the MOU properly, and enhancing the signatory section of the MOU. For FYs 2004 and 2005, OFRM executed the MOU during an annual summit between OFRM, seller agencies, and buyer agencies just before the new fiscal year began. It was not clear as to what officials should have been the signatories on the MOU. Also, the signatures were not always decipherable and the positions and titles of the signers were not stated. Further, the language in the MOU was confusing as to the responsibilities of seller, buyer, and paying agencies. As a result, the weight of the MOU was weakened, and the MOU did not have the managerial accounting and budget impact needed to effectively process and manage fixed costs.

DISCUSSION

OFRM designed the MOU as a means to ensure that user agencies were aware of fixed costs to be charged to their agencies and were in agreement with the specific forecasted amounts for various commodities (rent, telecommunications, occupancy, security, utilities, etc.). The purpose of each annual summit was to discuss the terms of the fixed-costs MOU with the various parties to the MOU. Therefore, representatives from OFRM, OCTO, OPM, OBP, and the buyer agencies attended the meetings. An agency's fixed-costs budget was given a final review, the agency was provided the opportunity to ask questions concerning the budget, and attempts were made to resolve discrepancies.

Scheduling the MOU Summit

OFRM schedules MOU summits just before a new fiscal year begins. We believe the MOU process can be improved by scheduling the MOU summit closer to the time that the Mayor submits his final proposed budget to the Council. At that point in time, the seller agencies (primarily OCTO and OPM) and the buyer agencies should be in agreement as to the amount of fixed costs the seller agencies are projecting that the buyer agencies will incur based on: (1) the needs the buyer agencies have identified; 92) the economic and cost factors the seller agencies have assumed; and (3) discussions held between seller and buyer agencies. By the August or September before a new fiscal year begins, the budget has already been approved and fixed costs already set. For example, for the FY 2006 budget, the deadline for the final proposed budget to the Council was March 21, 2005, according to OBP's "FY 2006 Operating Budget Timeline," dated September 9, 2004. However, the MOU summits were not conducted until September 2005, 6 months after the final proposed

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budget. The MOU summit lacked significance then because the agencies should have already identified their fixed-costs needs, given their input into the fixed-costs forecasts, and accepted the budget months before.

The MOUs are key documents in the fixed-costs allocation process because agencies (buyers) and sellers are attesting that these costs are necessary for the operation of the agencies for the fiscal year being budgeted. The MOUs could aid in justifying budgets to the Council by showing that fixed costs have been measured, forecasted, and agreed upon by the responsible entities, well before submission of the proposed budget.

Further, we noted that not all agencies signed MOUs because of discrepancies between fixed-costs amounts included in the MOUs and the actual fixed costs recorded in agency budgets. For example, the fiscal officer for the Office of the Attorney General did not sign the FY 2005 Fixed-Costs MOU because the fixed-costs amounts were greater than the budgeted amounts. Before the agency's fiscal officer signed the MOU, the fiscal officer wanted to discuss with the agency director the spending pressures created by the differences between allocated fixed costs and budgeted fixed costs, and where spending reductions could be made. The MOU's timing prevented adequate discussion of these spending pressures.

Table II below illustrates that some agencies have signed MOUs and others have not.

Table II. - Status of Signed and Unsigned MOUs.

Agency	FY	MOU Signed
Office of Attorney General	2005	No
Department of Human Services	2004	Yes
Department of Human Services	2005	No
D.C. Public Schools	2005	Yes
Metropolitan Police Department	2004	No
Property Management	2005	Yes

If the fixed-costs MOUs are executed close to the time the budget is submitted to the City Council, then the budget amounts and MOU amounts should agree. If fixed-costs amounts are changed by the Council for some unforeseen events outside of the control of the District, then amendments to the MOUs could be made and signed by responsible parties.

Fixed costs as a whole total approximately $200 million and are increasing. These costs are not "fixed" in the sense that they are not variable — because some do vary — but they are fixed in the sense that they are general and administrative or overhead costs which must be incurred if programs are to operate. Hence, the process should provide sufficient time to allow those agencies responsible for these costs to take ownership of them.

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MOU Wording and Signatory Section

We also noted that the MOUs' wording was not clear. For example, OFRM was referred to as the "Seller," as was the OPM. However, OFRM was actually the administrator or payer and OPM was the "Seller." OCTO was not referred to as a "Seller" even though telecommunication services were included among the services being sold. Further, we could not decipher the names of the signatories on most of the MOUs which were signed. In addition, the signature blocks did not indicate the titles of the persons signing the MOUs. Imprecise wording, indecipherable signatures, and the lack of printed names and titles weaken the force and impact of MOUs.

MOU as a Managerial Accounting Tool

OFRM initiated the MOU and the summit so that agencies would: (1) be aware of their fixed costs; (2) take ownership of their fixed costs; and (3) transfer funds to pay fixed costs to OFRM. In order to strengthen the MOU to make it more authoritative, the MOU should be signed by the District's CFO, the District's Chief Technology Officer, the Director of OPM, the Director of OFRM, agency directors, and agency fiscal officers. The signatory blocks should contain lines for printed names and titles, as well as signatures.

The MOUs can be used as a managerial accounting and budget document to attest that fixed costs have been soundly forecasted based on accurate analyses of historical costs and identified needs of the agencies for the year under budget consideration. The MOUs can be presented to the City Council for the Council's consideration in reviewing the budget. The MOU process for FY 2006 has undergone some changes from previous years. The City Administrator is supposed to sign the MOU as the representative for the buyer agencies. However, there needs to be a clear directive (Mayor's Order or Administrative Issuance) spelling out the responsibilities of user agencies, seller agencies, the administrative or paying agency, and the officials who should be the signatories to the MOU.

RECOMMENDATIONS

We recommend that the Chief Financial Officer, the Chief Technology Officer, and the Director, Office of Property Management coordinate efforts to:

1. Execute the Fixed-Costs Memorandum of Understanding closer to the date the Mayor presents the proposed budget to the City Council to make the MOU a more effective managerial accounting and budget tool.

FINDINGS AND RECOMMENDATIONS

We recommend that the Chief Financial Officer:

2. Improve the language of the MOUs so that the parties and their responsibilities as seller agency, buyer agency and paying agency or administrator are accurately and clearly identified and described; and

3. Enhance the signatory section of the MOU to include lines for the printed names of the signers, their titles or positions, and their agencies.

We recommend that the City Administrator:

4. Require the MOU to be signed by top officials of the Office of the Chief Financial Officer, OPM, OCTO, and the user agencies; and

5. Request that a Mayor's Order or directive on fixed costs be issued, which clearly spells out the responsibilities of: (a) agencies that procure commodities (rent, telecommunications, etc.) categorized as fixed costs for use by other agencies; (b) agencies using these commodities; and (c) the administrative or paying agency.

MANAGEMENT RESPONSES

Following are management responses listed by recommendation(s), by agency.

Recommendations 1-3

OCFO

OCFO did not respond specifically to each recommendation. OCFO stated that the MOU "summit" is the third opportunity that agencies have to address fixed-costs forecasts. OCFO stated that it is the responsibility of the Executive Office of the Mayor and the OCFO to ensure that budgets equal forecasts prior to submission to the Council. OFMR further stated that the MOU process has been streamed lined and that the City Administrator signs the fixed-costs MOUs on behalf of the agencies. OCFO also stated that OCFO, OPM, and OCTO sign as well.

OPM

OPM stated that moving the MOU closer to budget submission to Council is a good idea as far as enhancing the MOU as a budget tool. OPM expressed concerns that the recommendation does not address collecting funds when estimated or budgeted amounts are less than actual amounts needed. OPM concurred with Recommendations 2 and 3.

FINDINGS AND RECOMMENDATIONS

OIG COMMENT

In regard to OCFO's response, the OIG still recommends that the fixed-costs MOU agreements be signed prior to submission to the Council, and that the MOUs be signed by agency heads, agency fiscal officers or CFO's, and by the OCFO as well as the OCTO and OPM. If the MOU agreements are signed prior to submission to the Council and are signed by agency heads and fiscal officials, there is a stronger indication that agency personnel have assumed their responsibility in the fixed-costs forecast process, have given their input based on their identified needs, and have been active participants in the process. If the City Administrator signs on behalf of the agencies, an acknowledgement that agency program and fiscal officials are in accord with the forecasts does not exist. Hence, agency personnel could "slip back into their old habits" of not being active participants in the forecasts process, as OCFO states in regard to telecommunications forecasting. Agency personnel should not be of the mindset that it doesn't matter whether they sign the MOUs because OCFO is going to take their funds away regardless.

The OIG met with OBP officials about the fixed-costs process. We were informed by OBP that the Council's confidence in fixed-costs projections is undermined by a lack of what the Council considers to be sufficient, competent support and documentation for fixed costs. The OIG agrees with the OCFO's implementation of a new Rationalization Process for telecommunications services. Agencies' rationalization of all their projected fixed costs with a signed MOU before budget submission to the Council should improve the Council's confidence in the projections.

In regard to OPM's response, the OIG opines that collecting fixed-costs funds from agencies, when new estimates exceed budgeted amounts, is a matter that OBP and OFOS should resolve.

Recommendation 4

OCA

OCA concurred and stated that at the start of each budget cycle, it will issue instructions to top agency officials to acknowledge their roles and responsibilities in the fixed-costs allocation and oversight process.

OIG COMMENT

OCA's planned action addresses the recommendation.

FINDINGS AND RECOMMENDATIONS

Recommendation 5

OCA

OCA concurred and stated that at the start of the new administration, it will draft and request that the Mayor issue a directive instructing agencies on their roles in managing fixed costs.

OPM

OPM agrees with the need for a Mayor's Order to address the management of fixed costs. OPM further mentions in its response that the directive should allow fixed-costs surpluses to be carried forward to the next fiscal year, which will thus end the practice of agencies using fixed-costs surpluses to fund deficits in their program areas.

OIG COMMENT

Action to be taken by the OCA addresses fully the recommendation. However, OPM's comment about fixed-costs surpluses highlights the difference in thought among buyer and seller agencies concerning fixed costs, and illustrates the need to have a Mayor's Order addressing fixed costs. In contrast to the OPM, the buyer agencies we talked to were concerned with deficits produced by fixed costs and having to use program costs to cover those deficits. The OCA should include fixed-costs deficits/surpluses in the Mayor's Order.

FINDINGS AND RECOMMENDATIONS

FINDING 2. TELECOMMUNICATIONS FORECAST PROCESS

SYNOPSIS

Agency telecommunications coordinators (ATCs) do not always provide OCTO with sufficient information to reflect agencies' telecommunications needs for inclusion in the agencies' fixed-costs forecasts.

This condition exists because ATCs do not fully understand their responsibilities relating to the forecast process for telecommunications expenditures, and how their inputs affect their respective agencies' telecommunications budgets. Further, ATCs lack sufficient training to effectively participate in the forecasting process.

As a result, the forecasts may not be accurate and may lead to spending pressures and under spending. Agencies' variable telecommunications needs are not fully considered during the forecast and budgetary process.

DISCUSSION

Prior to the start of each budgetary period, the OBP requires every agency within the centralized management system to forward to OCTO the volume and costs of any telecommunications project(s) for the budget year, or a statement which indicates that no telecommunications projects are planned.

Management of Communication Services

The telecommunications division of OCTO manages all aspects of voice communications, such as, landlines, wireless, hand-held devices and services, telephone equipment, telephone systems, and voice messaging services. Serving as a central point of contact for all telecommunications-related products and services, the telecommunications division is also responsible for establishing, monitoring, and maintaining District-wide standards and procedures for services and installations. In that light, OCTO distributes guides and standard operating procedures to agency telecommunications coordinators.

Telecommunications Responsibilities at the Agency Level

ATCs are the agency personnel responsible for the telecommunications needs of their respective agencies. They are OCTO's primary contact point within agencies for all telecommunications, forecasting, and budgeting activities. Because ATCs are typically not

FINDINGS AND RECOMMENDATIONS

at the decision making levels within most agencies, they often lack sufficient knowledge and understanding of the agencies' strategic plans and goals. Not having a full understanding of the agencies' needs makes it difficult for ATCs to provide detailed or accurate input to the forecasting process.

Agency chief financial officers (CFOs) are often invited at the end of the process to sign or approve the final forecast. However, aside from the signatory responsibility, the role of many CFO's in the forecasting process is largely limited to that of an observer.

Telecommunications Payment Responsibilities

OFRM is responsible for paying utility bills and serving as a liaison between OCTO, the Office of Property Management (OPM), and client agencies. OFRM processes and pays telecommunications bills on the behalf of all agencies in the central payment system. In that light, OFRM collects in advance the budgeted amounts after the MOU summit and pays the telecommunications bills as they become due.

Testing the Telecommunications Forecast Process

ATCs do not always provide OCTO with adequate information to reflect the telecommunications needs of their respective agencies. We reached this conclusion based on tests that we performed at five user agencies: DPW, MPD, DHS, FEMS, and DMH.

Our test was to determine:

1. The extent to which the agency ATCs were involved in forecasting and budgeting for their telecommunications expenditures; and
2. Whether the agencies were fairly satisfied with the centralized payment system of fixed costs.

The ATCs' responses to our inquiries varied. ATCs at DPW and MPD indicated that they play a role in the forecast development. The other agency ATCs neither addressed the issues nor showed knowledge on the part of the budgetary and forecast processes. Test results at three of the five user agencies are described below.

DPW

A DPW official indicated that the telecommunications forecast for DPW is developed by OCTO and the DPW's agency CFO. OCTO obtains the information necessary for the forecast from the OFRM. The telecommunications forecast is calculated by averaging the actual telecommunications expenditures for the 3 years preceding the budgetary year and adding an inflation factor (2.9 percent in fiscal year 2004) to come up with the forecasted amount.

FINDINGS AND RECOMMENDATIONS

We inquired as to the specific role that DPW ATCs play in the forecast process. We found that DPW ATCs provide telecommunications services to the DPW administration, such as placing new orders, providing external technical services, and managing the existing telecommunications infrastructure. DPW ATCs also provide the agency CFO information about new telecommunications projects and cost data associated with the new projects, new services, or lines in the event of new hires. This information is used to forecast DPW's telecommunications needs.

We further inquired whether ATCs were aware of any communication from OCTO requesting information on new projects and major moves during the budgetary period. In response to this question, the DPW telecommunications manager acknowledged receipt of a spreadsheet from OCTO through which such details are forwarded back to OCTO.

MPD

MPD's ATC had been the telecommunications coordinator for only six weeks at the time of our inquiry. Therefore, he had not taken part in the forecast and budgetary processes for telecommunications expenditures for fiscal year 2004. However, he stated that despite not taking part in the telecommunications forecast and budgetary processes for the fiscal year under audit, he understood that the forecast process was a coordinated effort of the OFRM, OCTO, and the telecommunications management staff of MPD.

He further explained that once the agency budget is finalized, the budgeted amount for telecommunications services is transferred to OFRM for it to pay bills as they become due, while a certain portion is loaded into the Request for Telecommunications Services (RTS) system to finance various purchases of telecommunications materials and services as needed by the agency. The RTS provides the ATC with "read-only" capability that allows the ATC to determine the amount available for variable spending when orders are placed. The RTS rejects any order for goods or services that lacks the proper funding.

DMH

DMH's ATC indicated that since coming out of receivership status, DMH has continued to handle its telecommunications activities independently of the centralized management system. DMH maintains its RTS independently of that maintained by OCTO for agencies under the centralized system. Nevertheless, the agency contacts OCTO for telecommunications services and support as needs arise.

FINDINGS AND RECOMMENDATIONS

DHS and FEMS

The ATCs at DHS and FEMS did not respond in a manner that allowed us to assess their knowledge of the budgetary and forecast processes.

OCTO Solicits Agency Input into Forecast

OCTO sends out requests to each agency asking the ATCs to identify telecommunications needs for the upcoming budget year. At times, ATCs do not respond to the request and OCTO must issue a memorandum to the agency directors regarding the lack of a response. On other occasions, the information that the ATCs supply is not sufficient or accurate. As a result, an OCTO official stated that OCTO is confronted with a "garbage-in/garbage-out" scenario in regard to agencies' telecommunications forecasts. Hence, if the information that an ATC supplies as input into the forecast is not adequate or accurate, the output or forecast will not be adequate or accurate.

We noted that some ATCs may not be adequately trained in the following areas: (1) identifying agency needs; (2) knowing what their responsibilities are; and (3) understanding the significance their input has on the forecast process. OCTO indicated that it has designed a 2-day course for ATCs. The course deals with the RTS system, Tel-Watch[1], review of billings, etc. But OCTO has not had the funding to offer the course. Further, OCTO has not developed a standard operating procedures manual for ATCs.

OCTO further indicated that it has no role in appointing agency ATCs. Therefore, the skill levels of ATCs vary. In addition, the responsibilities of ATCs vary, since some ATCs are not solely ATCs.

Conclusion

Agencies that do not adequately address their telecommunications needs are prone to budget shortfalls during the fiscal period, a situation that would require emergency measures like reprogramming to cover shortfalls in the fixed cost budgets. ATCs who lack an adequate understanding of the impact of their input to the forecast and budgetary process may furnish budgetary information to OCTO, which is insufficient to develop accurate forecasts. As a result, agency personnel may submit requests for telecommunications services that were never considered when the forecast was developed. Consequently, the forecast will be inaccurate because funds would not have been budgeted for all of the agency's telecommunications needs.

[1] Tel-Watch is an OCTO information system that contains the master telephone bill and is accessible by District agencies.

FINDINGS AND RECOMMENDATIONS

RECOMMENDATION

We recommend that the Chief Financial Officer, OCFO and the Deputy Chief Financial Officer, OFRM:

6. Develop uniform policies and procedures, along with agency directors, for training ATCs on the forecast and budgetary processes.

We recommend that the Chief Technology Officer:

7. Secure funding for and initiate the planned training course for ATCs and develop a written manual with standard operating procedures for ATCs; and

8. Coordinate with agency heads to ensure that all requests for telecommunications services (RTS), and approvals thereof, are for budgeted items.

MANAGEMENT REPSONSE

Recommendation 6

OCFO

The finding was addressed to the OCFO and Deputy Chief Financial Officer, OFRM. The Deputy Chief Financial Officer, OFRM responded and agreed with the finding in general. However, OCFO/CFRM offered no specific action regarding the recommendation to develop uniform policies and procedures for training ATCs on the forecast and budgetary processes.

OCTO

OCTO also responded to the recommendation. OCTO stated that it will add a Telecommunications Program Director position to "develop programmatic support, tools and training for all telecommunications programs in general…."

OIG COMMENT

Even though OCFO/OFRM agreed with the finding, they offered no specific action to be taken to address the recommendation. Therefore, we reiterate that uniform policies and procedures be developed to train ATC's on the forecast and budgetary forecast. OCFO/OFRM should work with the new OCTO Telecommunications Program Director and agency heads in developing and implementing policies and procedures related to telecommunications forecasting and budget training for ATCs.

FINDINGS AND RECOMMENDATIONS

Recommendation 7

OCTO

OCTO agreed with the findings in general. OCTO stated that it will implement an "Agency Telecommunications (ATC) Training and Certification Program" by the third quarter of this year (2006). The program will provide tools and training on telecommunications manager skills, to include analyzing telecommunications invoices and using available business processes such as the VISION Vendor Portal.

OIG COMMENT

The action planned by OCTO addresses the recommendation.

Recommendation 8

Management did not specifically respond to the recommendation.

OIG Comment

The OIG reiterates the recommendation that OCTO coordinate with agency heads to ensure that agency employees' requests for telecommunications services are for items previously budgeted.

FINDINGS AND RECOMMENDATIONS

FINDING 3. TELECOMMUNICATIONS INVENTORY

SYNOPSIS

ATCs are not aware of the amount of the inventory of telecommunications lines and services subscribed to by their respective agencies. Adequate knowledge of the inventory composition is necessary to perform a meaningful forecast for telecommunications expenditure for any budgetary period. We attribute the cause of this condition to unquestionable reliance by agencies on OCTO for telecommunications management and support. Most agencies believe that because OCTO coordinates and oversees their telecommunications budget, it should take responsibility for most aspects of telecommunications, including inventory management.

As a result, agencies do not perform a proper review of telecommunications invoices prior to the bills being paid. Payments are also made for telecommunications lines that are no longer used or needed.

DISCUSSION

OCTO provides telecommunications management support to those agencies in the centralized management system. All agencies have telecommunications coordinators who are responsible for the telecommunications needs of their respective agencies. As part of our documentation and test of the fixed-cost allocations process, we requested that ATCs from the five agencies listed in the prior finding provide the auditors with a description of the telecommunications services and line inventory for their respective agencies. Except for DHS's ATC, who estimated DHS's telecommunications inventory as being over 5,000 lines, no other ATC had knowledge as to how many lines were subscribed to by their respective agencies. In every instance, ATCs referred us to OCTO for any information related to their agencies' telecommunications inventories.

After receipt of the telecommunications line inventory from OCTO, we performed a test count of DHS's line inventory to authenticate the estimate provided by the DHS ATC.

Table III on the following page reveals the results of our test count by vendor, product/service, and line count:

FINDINGS AND RECOMMENDATIONS

Table III. – Test Count of the DHS Line Inventory.

VENDOR	PRODUCT/SERVICE	TELECOMMUNICATIONS LINE COUNT
Verizon	Dial tone, voice mail, data, Centrex features, etc.	6,380
Sprint	Long Distance, Phone Cards, and Conference Calls.	315
Language Line	Voice Interpretation	3
AT&T GSM	Pricing Plan for discounted Id	17
AT&T Wireless	Cellular	30
Nextel	Cellular	325
Verizon Wireless	Cellular	1
Arch Communications	Pagers and Teletubbies	24
Acquis	Pagers	706
		7801

The inventory count of 7,801 telecommunications lines and services exceeds the 5,000 lines estimated by the DHS ATC. The nearly 3,000 count variance is a significant difference.

One factor attributing to the ATCs lack of knowledge about their agency's telecommunications inventory was the ATCs' workload. The DHS ATC acknowledged not having performed reviews of telecommunications bills on Tel-Watch due to the volume of telecommunications lines. The ATC stated that it was impossible for a staff of two to perform monthly reviews of over 5000 telecommunications lines alongside other responsibilities related to telecommunications.

Not knowing the volume of telecommunications lines and not validating vendor bills for telecommunications services and lines affects the development of accurate telecommunications forecasts, and could possibly result in payment for unused lines.

FINDINGS AND RECOMMENDATIONS

Unused Telephone Lines
Agencies continue to pay for unnecessary telecommunications lines and services. For instance, at the FEMS, three active telephone lines (673-3274, 673-3177 and 673-3129) were recently discovered in an engine house located at 1338 Park Road, N.E that had been abandoned for 12 years. During those 12 years, payments were made to the vendor for those lines because no one at the agency knew of their existence. If ATCs had been regularly monitoring their line inventories, these three lines likely would have been discovered during billing review and terminated in a timely manner.

Also, at the FEMS, 79 unneeded data lines that cost the agency approximately $40.00 each, per month, were recently discovered and terminated. No one knows how long these lines had been unused. The discovery of the data lines only occurred when OCTO informed the FEMS around mid-2005 that Verizon would discontinue its service to the District government, effective December 31, 2005. In response to the notice, the FEMS launched a project to determine which of the data lines would be transferred to the new telephone system (AVL) after December 31, 2005, discovered the unneeded lines, and requested that the lines be terminated.

OCTO's Involvement

Because OCTO itself may not have a complete inventory of lines, the ATCs who rely on OCTO for inventory information also do not have reliable inventory data. According to an OCTO official, no trail or inventory was kept of telephone lines by the agency that handled telecommunications for District agencies prior to OCTO. Verbal orders to connect and disconnect telephone lines were sometimes given; however, no records exist of these verbal orders.

To address previous inventory management problems, OCTO needs to develop and disseminate inventory policies and procedures so that agency ATCs will know what steps to follow in monitoring telephone lines. Further, OCTO should issue guidelines for determining the appropriate number of ATCs to employ, given that the size and complexity of telecommunications inventories vary from agency to agency. In addition, OCTO's guidelines should set forth the minimum qualifications required to serve as an ATC.

RECOMMENDATIONS

We recommend that the Chief Technology Officer:

9. Design and memorialize, in collaboration with agency directors, processes to periodically update agencies' telecommunications inventories and to validate telecommunications invoices; and

FINDINGS AND RECOMMENDATIONS

10. Issue guidelines to agencies as to the number of ATCs needed and skill levels required to adequately manage telecommunications inventories.

MANAGEMENT RESPONSE

Recommendation 9

OCTO

OCTO generally agreed with the recommendation. OCTO stated that OFRM is building databases to address inventory management and that OCTO will help with program implementation. OCTO expects the new system to be in place by the fourth quarter of this year (2006).

OCFO

OCFO agreed with the recommendation and stated that it has started to design inventory management processes which will require active involvement from the agencies. The processes include developing a new fixed-costs management system, developing new rationalization processes, and developing a quality assurance program to conduct selective audits of fixed-costs processes.

OIG COMMENT

The planned action addresses the recommendation. We also note that subsequent to the issuance of the draft report, an official of the OCA informed the OIG that OCFO had recently identified over 7,000 unused lines among the District's telephone inventory. In some cases, these lines had been connected for short-term events or activities but were never disconnected when the events ended. In its written response to the draft, OCA stated that the change in telephone inventory management from OCTO to OCFO had saved the District $5.5 million.

Recommendation 10

OCTO

OCTO stated that its "Business Process Enhancement and Reengineering" procedures will require Billing Resolution Specialist positions to be staffed to analyze activities that affect the telecommunications inventory and budget. Documented business processes for adding, managing, and removing telecommunications inventory will be developed. OCTO will implement "Electronic Signature of Orders" to increase the ease and timeliness of information related to changes in inventory. The planned action should aide

FINDINGS AND RECOMMENDATIONS

telecommunications staff in more effectively accomplishing their tasks. The action is an ongoing, continuous process.

OIG COMMENT

The planned action addresses the recommendation.

FINDINGS AND RECOMMENDATIONS

FINDING 4. RENT ADMINISTRATION AND MONITORING

SYNOPSIS

OPM needs to place more emphasis on monitoring of operational pass-through rental costs. For example, $1.7 million in base rental expenditures for fiscal year 2004 were not sufficiently monitored and $1 million in additional operating rental expenses were unsupported/ questioned costs. The lack of automated leasing systems, the high volume of rental activity, and limited resources resulted in OPM not sufficiently monitoring operational expenses. The OIG questioned costs because they were not recorded in accordance with generally accepted accounting principles (GAAP) and/or in accordance with lease terms which required operating expenses to be based on GAAP. The OIG considered costs to be unsupported if competent, sufficient documents did not exists to verify the charges. If OPM does not adequately monitor operational expenses, it may not identity overcharges and improper charges in lessors' billing statements.

DISCUSSION

For FY 2004, OPM forecasted approximately $85 million in rental expenditures, of which, $11 million represented operational costs. We tested six agencies with rental expenditures totaling nearly $36.7 million, including about $3.8 million in operational costs. We performed an analysis of each agency's leased property to determine whether the forecasted amounts for each lease were reasonable. As part of our analysis, we performed a recalculation of the annual net rental and annual base operating charges based upon our understanding of the lease agreements and any amendments.

Criteria

In testing rental expenses for propriety, we examined documentation to determine whether operating expenses charged to fiscal year 2004 were proper and sufficiently supported. By proper, the OIG means in accordance with terms of the leases and in accordance with GAAP (such as Governmental Accounting Standards Board (GASB) Statement 13)[2]. GAAP generally requires that entities recognize economic events on an accrual or modified accrual basis. Hence, agencies should recognize expenses in the period in which they were incurred or in which services were received. By sufficiently supported, we mean competent documents were available to substantiate the expenses.

With regard to GAAP, specifically we considered GASB Statement 13 which states that:

[2] Note: GASB issues generally accepted accounting principles applicable to state and local governments.

FINDINGS AND RECOMMENDATIONS

> Transactions arising from operating leases with scheduled rent increases should be measured based on the terms of the lease contract when the pattern of the payment requirements, including the increases, is systematic and rational.

ACCOUNTING FOR OPERATING LEASES WITH SCHEDULED RENT INCREASES, Statement No. 13, § 5 (Government Accounting Standards Bd. 1990).

Questioned/Unsupported Costs

The OIG noted that increases in operating payments which OPM incurred did not always appear to be systematic and rational or in accordance with terms of the leases. For example, operating expenses, which generally included items such as utilities, general and administrative expenses, property taxes, management fees, etc., consisted of base operating expenses plus increases for the current year. The increase for the current year should have been based on the total of operating expense for the current year less the base amount of operating expenses. OPM performed a reconciliation of the current year costs submitted by the lessor and base year costs to determine the increase or additional payment due the lessor. However, sometimes the increases did not appear to be rational or systematic. We noted: (1) expenses charged or recognized years after they were incurred; (2) overpayment of operating expenses not credited to the District; and (3) capital expenditures recognized as operating expenses.

Table IV lists the leases which had questioned/unsupported costs. We also list the criteria we used to determine that the costs were questioned or unsupported. For example, in Table IV (at the end of this finding), additional rent for lease number 87-08 for fiscal year 2004, included numerous costs the lessor incurred in 2001 or 2002. The OIG opines that it is not systematic or rational for costs incurred in 2001 or 2002 not to be recorded until 2004. Those payments did not represent "the time pattern in which the leased property [was] available for use of the lessee," as required by GASB 13. *Id.* § 5b. Because OPM did not recognize the expenses until 2 or 3 years after the District had use of the leased facility or received the services, there were unrecorded liabilities for 2001 and 2002.

Furthermore the lease itself states:

> The District shall monthly pay to the Lessor an amount equal to actual charges for the servicing, operating, managing, maintenance and repair .… Lessor shall provide Lessee monthly with a bill for the above services and utilities which shall include copies of all actual invoices paid by the Lessor which are including (sic) in said billing.

In addition, the OIG noted that most of the utility bills had late fees and there were some disconnect threats. The fact that nearly every monthly electric bill had such a

FINDINGS AND RECOMMENDATIONS

fee indicated that OPM was not properly monitoring the lease. If adequate monitoring was taking place, then OPM should have informed the lessor to pay its bills timely and to remit bills timely to OPM. It was not rational for the lessor not to submit bills timely.

We also noted for lease number 87-38 that capital expenditures had been incurred but were treated as operating expenses. The $84,948 listed in Table IV included approximately $50,000 for carpet, which has a useful life of more than 1 year. The $50,000 should have spread out over the useful life of the carpet. The remainder of the $84,948 covered the cost of painting. Even though painting may be viewed as an operating expense, the painting possibly could have been done for free under the terms of the lease according to an OPM staffer. The OPM employee informed the OIG that the tenant requested the lessor to install the carpet and to paint. Therefore, the $84, 948 represents costs that possibly could have been avoided, as well as costs that should have been capitalized and amortized.

For lease number 98-06, we noted that $86,506 in questioned/unsupported costs included periods for which the base-year operating expenses were less than the current-year operating expenses. However, the lessor did not give the District credits for overpayment of operating expenses as stipulated in the lease agreement.

In FY 2004, the District leased a building located in the 3200 block of Pennsylvania Avenue, S.E. for MPD. This facility's annual rent expenditure was $346,954 in base rent, plus $155,704 in operational costs. The operational costs represented 45 percent of the base rent. The DPW also occupied space at the same location and incurred $243,311 in base rent expenditures, plus $103,233 in operational costs, which represented 43 percent of the base rent. Subsequent to our review, OPM stated that a court settlement validated that the landlord had duplicated some of these expenses.

Questioned/unsupported costs exist because of the high volume of rental activity and the lack of resources to properly monitor operational costs. The lack of proper monitoring prevents OPM from identifying 1) overcharges, 2) errors in lessors' billing statements and books, and 3) services not timely billed. Inadequate monitoring can result in waste of the District's resources. In the event the landlord overstated the District's pro rata share of operating expenses, the District may be entitled to a refund based on the terms of most of the lease agreements we reviewed.

Additionally, we note that OPM, in its original response to the draft report, stated that OPM had identified about a dozen instances where lessors are suspected of overcharging the District. OPM is working with the Office of the Attorney General to recover overcharges. Alleged overcharges would also fall into the category of questioned costs.

FINDINGS AND RECOMMENDATIONS

Policies and Procedures for Monitoring Operational Costs

OPM has no written polices and operating procedures regarding the governing monitoring and oversight of operational costs. However, various lease agreements state:

> For a period of three years after receiving the statement of operating expenses], the District shall have the right to examine copy and audit Landlord's books and records (i.e., original invoices, originals, if any, of executed contracts and original canceled checks) pertaining to the operating expenses … for the purpose of verifying the accuracy of the statement ….
>
> If it is determined, under Section II or otherwise, that the correct amount owing was greater than 2% less than the increase shown on the statement, then Landlord shall, in addition to refunding any amounts erroneously paid by the District, reimburse the district for the District's reasonable cost of conducting the audit ….

OPM uses spreadsheets, rather than automated systems, to maintain and track operational costs data. Given the volume of lease data, having automated databases would enable OPM to more efficiently monitor operational costs.

Table IV on the following page lists a summary of operational costs not monitored and unsupported operational costs and questioned costs included in the costs of various leased properties.

FINDINGS AND RECOMMENDATIONS

Table IV. - Summary of Operational Costs Not Monitored and/or without Supporting documentation and Questioned Costs.

AGENCY	LEASE #	LESSOR ADDRESS	Base Opr. Exp. Not Monitored	Additional Rent No Support/ Questioned Cost	CRITERIA
Health Department	87-38	2100 Martin Luther King Jr, Ave., S.E.	106,776	$84,948	(1) Capital expenditure pass through as operating expense, amounts not amortized. (2) Not in accordance with GAAP. (3) Addendum H states that any other expenses or charges should be in accordance with sound accounting management practices.
Mental Health	87-08	1536 U Street, N.W.	122,675	$200,738	(1) FY 02, FY 01 operating expenses duplicated $39,445. (2) Annual rent overpaid by $23,232.19. (3) Unrecorded liabilities. (4) Incorrect fiscal year. (5) Utilities late fees paid by District. (6) Lessor not monitored. (7) Addendum E of the approved lease states that the District shall pay monthly lessor an amount equal to the actual charges. (8) Lease terminated in June 2004; however, rent was paid for the full year.
Health Department	88-20	2146 24th Pl.., N.E.	125,075	57,941	(1) FY 02 expenses. (2) Management fees in excess of 3% stipulated in lease. (3) Unallowed fees to lessor for Services and Management Contract in amount of $96,000; Addendum I of the approved lease states Services and Management Contract, including energy management services, should be with independent contractor. (4) Unrecorded liabilities. (5) Addendum H of lease states the District has the right to examine documents in landlord's possession which evidence expenses paid by the landlord during a particular lease year.
Human Services	85-17B	645 H Street, N.E.	289,716	281,974	(1) No supporting documentation.
Human Services	98-11	3917-19 Minnesota Ave., S.E.	72,500	40,631	(1) Expenses duplicated in the amount of $21,020. (2 No supporting documentation. (3) Expenses not in accordance with GAAP. Sec. 2.02 (f) states landlord may give the District notice of landlord's estimate of amounts payable under this paragraph on account of increases in operating expenses for each adjustment period. Landlord's estimate shall be reasonable and based upon GAAP. If the District requests, landlord shall give the District reasonably detailed documentation to support landlord's estimate.
Metropolitan Police Department	98-03	3220 Penn. Ave., S.E.	-	155,704	(1) FY02 expense duplicated. (2) Sec. 2.02 states the District shall reimburse the sub landlord 100% of any excess over base sublease operational expense as additional rent.
Department of Public Works	98-03	3220 Penn. Ave., S.E.	-	103,233	(1) FY02 expense duplicated per OPM audit. (2) Sec. 2.02 states the District shall reimburse the sub landlord 100% of any excess over base sublease operational expense as additional rent.
Health Department	89-36	3720 Martin Luther King Jr. Ave., S.E.	234,653	3,650	(1) No supporting documentation; Addendum I of the approved leases states that the District shall have the right to examine documents in landlord's possession, which evidence the operational expenses paid by the landlord during a particular lease year.

FINDINGS AND RECOMMENDATIONS

Health Department	93-01	33 N Street, N.W.	200,000	-	Sec. 2.02(g) states that the landlord shall give the District reasonable detailed documents to support landlord's estimate.
Mental Health	87-25	6135 Kansas Ave., N.W.	30,839	-	(1) Not on FY 04 rental forecast.
Mental Health	98-06	3841-45 Alabama Ave., S.E.	86,985	86,506	(1) No supporting documentation. (2) Expense statement overstated by $8,907. (3) Paragraph (2.02) (iii) states that if the statement shows that the actual amount the District owes for the adjustment period is less than the estimated amounts paid by the District during the adjustment period, landlord shall refund the difference (overpayment) to the District. (4) Sec. 2.02(g) states that the books and records should be in kept in accordance with generally accepted accounting principles.
Human Services	98-07	810 First Street, N.E.	121,428	22,340	(1) No supporting documentation (2) Sec. 2.02(g) states that the landlord shall give the District reasonable detailed documentation to support landlord's estimate.
Human Services	91-09	508 Kennedy Street, N.W.	69,683	35,099	(1) Base amount calculated incorrectly (2) Addendum F states that should operating costs be less than the base amount in succeeding years, then the lessor shall refund such excessive payments to the District without request from the District. The District has the right to audit the lessor's books if it so desires.
Human Services	87-38	2100 Martin Luther King, Jr., Ave., S.E.	261,597	$9,470	(1) No supporting documentation. (3) Sec. 2.02(g) states that the landlord shall give the District reasonable detailed documentation to support landlord's estimate.
Mental Health	93-01	33 N Street, N.E.	50,000	-	Sec. 2.02(g) states that the landlord shall give the District reasonable detailed documentation to support landlord's estimate.
Mental Health	99-05	51 N Street, N.E.	79,775	-	Sec. 2.02(g) states that the landlord shall give the District reasonable detailed documentation to support landlord's estimate.
TOTALS			**$1,836,282**	**$1,082.233**	

FINDINGS AND RECOMMENDATIONS

RECOMMENDATIONS:

We recommend the Director, OPM:

11. Develop written policies and operating procedures governing oversight and monitoring of operational costs, to include the verification of invoices and other billing documentation for operational expenses charged by the lessor;

12. Establish a process to periodically monitor lessors' books and records in order to identify whether operating expenses are reasonable and directly related to the operation, maintenance, and management of the property under lease; and

13. Automate systems that are now recorded on Excel worksheets to accommodate the vast amount of data that is presently stored on the worksheets and to minimize mistakes.

MANAGEMENT RESPONSE

Recommendations 11 – 13

OPM did not separately address each finding in its revised response to the draft report. OPM stated that it agreed with the general conclusion of the report that "the lack of automated leasing systems, the high volume of rental activity and limited resources resulted in OPM not sufficiently monitoring operational expenses." However, OPM stated that in older leases, base operating expenses are fixed and no monitoring can change the amount due. OPM also stated that it disagrees with a requirement to follow generally accepted accounting principles when the leases allow cash or accrual accounting.

OIG COMMENT

The OIG maintains its position that base operating expenses should be monitored in order to ensure that base expenses being charged to the District are in accordance with terms of the lease. The OIG disagrees with OPM's comments that GAAP does not have to be followed if leases allow a cash basis of accounting. The District's Comprehensive Annual Financial Report (CAFR) states:

> The District's financial statements are prepared in accordance with generally accepted accounting principles (GAAP) applicable to governmental entities established by GASB.

Because the District's financial statements are government-wide financial statements composed of transactions of individual agencies, the OIG opines that it is not within an agency's purview to decide what accounting principles to follow. That authority rests with

FINDINGS AND RECOMMENDATIONS

the OCFO. Agencies need to have controls in place such that financial transactions are initiated, authorized, processed, and reported in accordance with GAAP. Therefore, leases and contracts should not specify that accounting principles other than GAAP may be followed.

The OIG notes that OPM has hired an asset manager to help conduct audits or reviews of the leases to protect the District's interests. This action partially addresses Recommendations 11 and 12. We continue to suggest that OPM develop formal written policies to monitor and review lessors' books.

OPM further stated that it has referred a dozen rent cases to the Office of the Attorney General, where it was suspected that the District was overcharged. Such action may help recover some questioned costs.

In regard to Recommendation 13, we additionally note that OPM stated that it has received approval from OCTO to purchase software to automate its processes related to lease administration. Action taken and planned by OPM addresses fully Recommendation 13.

FINDINGS AND RECOMMENDATIONS

FINDING 5: ALLOCATION OF RENTAL EXPENDITURES

SYNOPSIS

OPM did not properly allocate and certify rental expenditures for DHS, DOH, and DMH. This condition resulted from the lack of a proper due diligence review of the rent rolls by OPM prior to certification for payment. As a result, OFRM allocated and charged rental payments to the incorrect agencies.

DISCUSSION

In accordance with OPM procedures for the certification of rental payments, a monthly due diligence review and analysis of lease payments is performed to ascertain whether rental expenditures are properly allocated and certified based on space that agencies occupy. In addition, OFRM's manual, "Operations Overview Making Government Work," states that the OPM fixed cost manager coordinates with the agency area asset manager for review and approval of the rent roll prior to certification for payment. However, we found that OPM did not always coordinate with the agency area asset manager to determine the correct allocation and assignment of space prior to certification of payment.

Certifying and Allocating Costs of Multi-Tenant Leased Space

In multi-tenant government leased buildings, OPM rental estimates are based on the rentable area each agency occupies. Each agency is charged a proportionate percentage for the annual estimated cost of the facility. During our review, we found that OPM erroneously certified $606,166 of rental expenditures tested. For FY 2004, DMH occupied 12 percent of the space at 51 N Street, N.E., a multi-tenant building. However, for 2 months, OPM incorrectly over-allocated rental costs to DMH at 47 percent or $137,142, rather than at the 12 percent rate or $43,561. Conversely, OPM under-allocated rental costs to DOH at the 12 percent rate or $43,561, rather than at the 47 percent rate or $137,142.

In addition, for 12 months OPM over-allocated rental costs of $108,407 to DHS for rental expenditures for a building in the 3300 block of V Street, which DHS did not occupy. The allocation was based on an OPM Summary of Square Footage that showed that DHS occupied 100 percent of the building.

We believe rental costs misallocation was due, in part, to a lack of collaboration between OPM and the agencies' area asset managers. To facilitate collaboration, the OPM fixed-

FINDINGS AND RECOMMENDATIONS

costs manager and the agency area asset managers need to coordinate on a quarterly basis to ensure that expenditures and space are allocated to the correct agencies.

In addition, OPM, OFRM, and buyer agencies need to ensure the uniformity and compatibility of policies, procedures, and data systems that will be used in the fixed-costs allocation process.

Table V lists the facility locations for which rental expenses were allocated in error.

Table V. - Summary of Rental Expenditures Allocated to the Wrong Agencies.

Address	AGENCY	Lease Number	Amount Certified by OPM	Auditor's Calculation Based on % of space occupied.	Date
51 N Street, N.E.	Dept. of Health	99-05	$43,561	$137,142	08/04
51 N Street, N.E.	Dept. of Mental Health	99-05	$137,142	$43,561	08/04
51 N Street, N.E.	Dept. of Health	99-05	$40,132	$114,313	09/04
51 N Street, N.E.	Dept. of Mental Health	99-05	$114,313	$40,132	09/04
3330 V Street, N.E.	Dept. of Human Services	88-32	$108,407	$ 0	10/03 to 09/04
3330 V Street, N.E.	Dept. of Health	88-32	$162,611	$271,018	10/03 to 09/04
TOTAL			$606,166	$606,166	

RECOMMENDATIONS

We recommend that the Director, OPM:

14. Establish quarterly sessions with agency area asset managers to confirm the proper allocation and assignment of space of District leased facilities to ensure the accurate allocation of rental expenditures.

We recommend that the Chief Financial Officer, OCFO:

15. Collaborate with OPM, OBP, and the user agencies to address the uniformity and compatibility of policies, procedures, and data systems that will be used in the fixed-costs process.

FINDINGS AND RECOMMENDATIONS

MANAGEMENT REPSONSES

Recommendation 14

OPM opines that it is an ongoing responsibility of agencies and OPM to confer as to their space needs. OPM also prefers a policy where agencies inform OPM when they contemplate space alterations.

OIG COMMENTS

The OIG agrees that it would be better to have ongoing communication between agencies and OPM concerning agencies' space needs. OPM needs to take action to issue a directive or administrative guidance to that effect.

Recommendation 15

OPM agrees and is having on-going communications with OBP in regards to enhancing information shared with user agencies.

OIG COMMENTS

Action taken and planned by OPM fully addresses the recommendation.

FINDINGS AND RECOMMENDATIONS

FINDING 6: DUPLICATE RENT PAYMENTS

SYNOPSIS

While OFRM was observed to be generally accurate in processing rent payments, we found that OFRM made duplicate rental payments to one lessor. This condition occurred when OFRM issued duplicate wire transfers for eight payments to the lessor. OFRM issued adjustments for four of the duplicate payments, but failed to adjust the remaining four duplicate payments, which resulted in a loss of use of District funds.

DISCUSSION

In FY 2004, actual rental expenditures amounted to $83,659,784 and represented 43 percent of the total fixed-costs expenditures. We examined six agencies with rental costs totaling $36,672,256, or 44 percent of rental expenditures, and found duplicate rental payments totaling $161,610. The duplicate payments represented four-tenths of one percent of the rental costs we examined.

Duplicate Payments

A total of eight duplicate payments were made to one lessor. The duplication occurred when OFRM made two extra payments (14 payments, instead of 12 payments) of four monthly billed amounts, $113,723, $35, $46,417, and $1,435, respectively. These billings were for rented premises in the 2100 block of Martin Luther King Avenue, Jr., S.E.

Adjustments to Cancel Duplicate Wire Transfers

OFRM made several adjustments to cancel some of the duplicate wire transfers. However, OFRM did not make adjustments for all duplicate payments. We found that OFRM failed to cancel four duplicate payments totaling $161,610. (See Table VI on the following page.)

Although the number of duplicate payments is not excessive, all duplicate payments could be avoided if OFRM heightened its due diligence review of rental expenditures prior to posting to the general ledger. Duplication of rental payments results in increased expenditures for the District and a waste of limited resources.

Duplicate payments can also affect the ability of the OPM fixed-costs manager to provide OFRM with an accurate forecast, since historical costs are used as the basis in the

FINDINGS AND RECOMMENDATIONS

projection of rental forecasts. In addition, the OBP estimates can be affected since OBP relies on OFRM fixed-costs forecasts in the preparation of agencies fixed-costs budgets.

During our review, we also found that OPM and OFRM do not perform a monthly reconciliation of rental expenditures. OFRM's monthly billing summary report for rental expenditures should be reconciled with the OPM monthly rent roll. This will identify discrepancies in the summary of monthly expenditures and the rent roll prior to posting to the general ledger.

Table VI lists the locations, agencies, and amount of duplicate rental payments.

TABLE VI. - Summary of Duplication of Rental Expenditures.

Address	Lease No.	Agency	Transaction Amount	Document No.	Cancelled Wire Transfers/ Adjust-ments	Doc. No.	Duplicate Payment
2100 Martin Luther King, Jr. Ave., S.E.	87-38	Department of Health	$46,417	ZE007434	$46,417	CN013009	-0-
2100 Martin Luther King, Jr. Ave., S.E.	87-38	Department of Health	$46,417	ZE008043	-0-		$46,417
2100 Martin Luther King, Jr. Ave., S.E.	87-38	Department of Health	$1,435	ZE007442	$1,435	CN013009	-0-
2100 Martin Luther King, Jr. Ave., S.E.	87-38	Department of Health	$1,435	ZE008045	-0-		$1,435
2100 Martin Luther King, Jr. Ave., S.E.	87-38	Department of Human Services	$113,723	ZE007434	$113,723	CN013009	-0-
2100 Martin Luther King Jr. Ave., S.E.	87-38	Department of Human Services	$113,723	ZE008043	-0-		$113,723
2100 Martin Luther King Jr. Ave., S.E.	87-38	Department of Human Services	$35	ZE007441	$35	CN013009	-0-
2100 Martin Luther King Jr. Ave., S.E.	87-38	Department of Human Services	$35	ZE008044	-0-		$35
TOTAL			$323,220		$161,610		$161,610

FINDINGS AND RECOMMENDATIONS

RECOMMENDATIONS

We recommend that the Chief Financial Officer, OCFO:

16. Ensure that OCFO officials reconcile monthly summary rental reports to OPM monthly rent rolls to identify any overpayments of rental expense; and

17. Seek reimbursement of overpayment of rental expenditures in the amount of $161,610.

Management Response

Recommendations 16 and 17

OCFO stated that it did not concur with the finding as outlined by the OIG. OCFO stated that three payments were made to the vendor for August 2004 rent. One payment was cancelled because it was lost in the mail and a second payment, a wire transfer, was cancelled because it had been given the wrong routing number. Therefore, the vendor only received the third payment.

OIG COMMENT

On an Executive Information Summary Report (EIS), provided by OCFO, which listed rental payments to the vendor for FY 04, the OIG saw 14 payments but only one cancellation. We did not see a cancellation for the wire transfer on the EIS report. However, OCFO did provide another document showing the cancellation. Therefore, we consider Recommendations 16 and 17 closed.

EXHIBIT A. SUMMARY OF POTENTIAL BENEFITS RESULTING FROM AUDIT

Recommendation	Description of Benefit	Amount and/or Type of Monetary Benefit	Status[3]
1	**Internal Control.** Executes the Fixed-Costs Memorandum of Understanding near the date the proposed budget is presented to the City.	Non-Monetary	Unresolved
2	**Internal Control.** Improves the language of the MOUs to more clearly identify responsibilities of the seller, buyer and payer agencies.	Non-Monetary	Unresolved
3	**Internal Control.** Requires the MOU to be signed by senior officials of OCFO, OPM, OCTO, and the user or buyer agencies.	Non-Monetary	Unresolved
4	**Internal Control and Compliance.** Enhances the signatory section of the MOU for added clarity of signers.	Non-Monetary	Closed
5	**Internal Control and Compliance.** Issues a Mayor's Order or directive clearly spelling out the responsibilities of user and buyer agencies.	Non-Monetary	Closed
6	**Internal Control.** Develops uniform policies and procedures for training ATCs.	Non-Monetary	Closed
7	**Economy and Efficiency.** Initiates training sessions for ATCs for updates and provides training for new ATCs.	Non-Monetary	Closed
8	**Internal Control.** Ensures that all requests for telecommunications services and approvals are budgeted.	Non-Monetary	Unresolved

[3]This column provides the status of a recommendation as of the report date. For final reports, "**Open**" means management and the OIG are in agreement on the action to be taken, but action is not complete. "**Closed**" means management has advised that the action necessary to correct the condition is complete. "**Unresolved**" means that management has neither agreed to take the recommended action nor proposed satisfactory alternative actions to correct the condition.

EXHIBIT A. SUMMARY OF POTENTIAL BENEFITS RESULTING FROM AUDIT

Recommendation	Description of Benefit	Amount and/or Type of Monetary Benefit	Status[3]
9	**Internal Control.** Designs a process to periodically update agencies' inventories of telecommunications lines and services.	Non-Monetary	Closed
10	**Economy and Efficiency.** Provides guidelines for agencies to follow in employing staff to handle their telecommunications functions.	Non-Monetary	Closed
11	**Compliance and Internal Control.** Improves the administration and monitoring of operational rental costs.	Non-Monetary	Unresolved
12	**Economy and Efficiency.** Improves monitoring of lessors' books and records to identify valid operating expenses directly related to the operation, maintenance, and management of the property under lease.	Monetary Estimated $1 million	Unresolved
13	**Economy and Efficiency.** Automates systems to accommodate the vast amount of data needed to review operational expenses for sixty eight agencies.	Non-Monetary	Closed
14	**Internal Control.** Provides reasonable assurance that vendor billings and space allocations are accurate and ensures accurate allocation of rental expenditures.	Non-Monetary	Closed
15	**Management Controls.** Establishes uniform standards, policies, procedures, databases, and systems to track and manage fixed costs.	Non-Monetary	Closed
16	**Internal Control.** Decreases the possibility of overpayment to lessors.	Non-Monetary	Closed
17	**Economy and Efficiency.** Seeks reimbursement of rent overpayments.	Non-Monetary	Closed

EXHIBIT B. MANAGEMENT RESPONSE - OCTO

GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF TECHNOLOGY OFFICER

RECEIVED
6/25

06 JUN -2 PM 2:46

June 1, 2006

Mr. Charles J. Willoughby
Inspector General
Office of the Inspector General
717 14th Street, NW, 5th Floor
Washington, DC 20005

RE: Audit of the Fixed-Costs Allocation Process (OIG No. 05-2-10MA)

Dear Mr. Willoughby:

I am responding to the Office of Inspector General's (OIG) audit of the Fixed-Costs Allocation Process.

We have provided responses to the OCTO recommendations in the attached document. Please contact me at (202) 741-5020 if you need any additional information.

Thank you for your consideration.

Sincerely,

Chris Peabody
Deputy CTO, Network and Communication Services
Office of the Chief Technology Officer

Attachment

cc: Robert C. Bobb
Natwar M. Gandhi
Carol J. Mitten

441 4th Street, N.W., Washington, DC 20001 (202) 727-2277, Facsimile (202) 727-6857

EXHIBIT B. MANAGEMENT RESPONSE - OCTO

<u>OCTO Response to OIG Audit of Fixed Cost Allocation Process (Dated May 15th, 2006)</u>

I. General Feedback

OCTO agrees with the findings and supports the recommendations of the OIG in general. In fact prior to receiving the draft report on May 16, 2006 OCTO had begun implementation and / or planning of actions to address issues identified by the audit. In particular OCTO notes an opportunity to enhance the OIG findings by providing guidance on the magnitude of the situations identified. For example, knowing the OIG's findings on the line inventory and the "baseline" used would be valuable. Then OCTO can focus first on agencies that have the greatest need. This information would inform decision(s) taken on actions and priorities.

II. Specific OCTO Action(s) taken and Target Dates for Completion

OCTO has made, and is making, structural changes in its Telecommunications Organization which address the need(s) identified by the OIG. The specific action(s) and their implementation schedule follow:

<u>OIG CONCLUSION #2</u> " *....programs will include assistance with the "...forecast process for telecommunications expenditures."*

OCTO RESPONSE: OCTO is adding a Telecommunications Program Director Position (starts June 12th, 2006) - added to develop programmatic support, tools and training for all telecommunications programs in general and for ATCs in particular VISION Vendor Portal – secure portal to manage and to share information on contact / contract / escalation information for all approved OCTO Telecom vendors (*vendors can assist with the "... inventory of telecommunications lines*")

<u>OIG CONCLUSION #2</u> : *"ATC training will address basic skills such as "... forecast process for telecommunications expenditures" and "... inventory...."*

OCTO RESPONSE : Agency Telecommunications Coordinator (ATC) Training & Certification Program – tools and training on a standards set of telecommunications manager skills, including analyzing / reviewing telecommunications bills and on using available business processes, e.g., the VISION Vendor Portal which is available via the DC Government intranet

EXHIBIT B. MANAGEMENT RESPONSE - OCTO

OIG CONCLUSION #3: (*directly addresses the "… inventory of telecommunications…" matter for OCTO and facilitates the work of OFRM*)

OCTO RESPONSE : Enhanced Telecommunications Inventory Management – OFRM is building databases to address inventory management and OCTO is charged with programmatic implementation, as stated above

OIG CONCLUSION #3: (*directly addresses telecommunications services moves, adds, changes and deletions that impact "…inventory of telecommunications….")*

OCTO RESPONSE: Business Process Enhancement & Reengineering of the agency client and program activities that comprise the telecommunications inventory, including but not limited to:

1. Billing Resolution Specialist positions staffed to "investigate" activities that affect the telecommunications budget / compliance / inventory / management / other areas of DC Government agency and / or program operations
2. Documented business processes for adding, managing and removing telecommunications inventory, e.g., adding and / or transferring lines on the DC-Net asset and service, whether new or moved to DC-Net from Verizon
3. Electronic Signature of Orders (RTS) – electronically process new orders to increase the ease and timeliness of information on changes to inventory

Action (X marks completion date)	Complete	Q2'06	Q3'06	Q4'06	2007 / Beyond
1. Telecom Prog. Dir.		X			
2. VISION Vendor Portal	X				
3. ATC Training & Certification	>>>>>>>>>>>>>>>>>>>>>>>>>>>>X				
4. Enhanced Telecom. Inventory	>>>X				
5. Business Process Enhancement….	X (and ongoing "continuous process improvement)>>>>>>>>>>>>>>>>>>>>>>>>>>>>>				

EXHIBIT C. MANAGEMENT RESPONSE - OCFO

GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER
GOVERNMENT OPERATIONS CLUSTER

June 1, 2006

Mr. Charles J. Willoughby
Inspector General for the District of Columbia
717 14th Street, N.W.
Washington, D.C. 20005

Re: OIG Draft Report – Audit of the Fixed-Costs Allocation Process (OIG No. 05-2-10MA)

Dear Mr. Willoughby:

Thank you for the opportunity to comment on the draft report of the Office of the Inspector General's (OIG) Audit of the Fixed-Costs Allocation Process. We would like to comment on the following four findings:

Finding # 1:

Address the need for Office of Finance and Resource Management (OFRM) to improve the Fixed Costs Memorandum of Understanding (M OU) process by executing the MOU timelier, wording the MOU more exacting, and enhancing the signatory section of the MOU.

Response to Finding # 1:

The objectives of the (MOU) summit, held in August and September for the upcoming fiscal year, are to ensure that the forecasted fixed costs are in line with the budgeted amounts, which were established in the previous spring. The summit is the **third** opportunity to revisit and evaluate the forecast for reasonableness.

If the forecast exceeds the budget, then the agency has to identify any spending pressures and either initiate a reprogramming or submit a spending pressure notification to the Office of Budget and Planning (OBP).

To calculate agency Local budget targets, OBP integrates OFRM, Office of Chief Technology Office (OCTO), and Office of Property Management (OPM) Fixed Cost forecasts; those forecasts are shared with agencies at the very beginning of the budget development process (August or September). It is the responsibility of the budget development staff from the OCFO, Executive office of the Mayor (EOM), and OBP to ensure that their Fixed Cost budgets equal those forecasts. This is the **first** opportunity to

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EXHIBIT C. MANAGEMENT RESPONSE - OCFO

evaluate the forecasts, to identify any deficiencies with those forecasts, to discuss the forecasts with the Seller and Administering agencies, and to include those forecasts in agency budgets. During the Budget Review Team meetings, chaired by the City Administrator, agency budgets, including Fixed Costs are scrutinized and discussed. There is even a special session devoted exclusively to Fixed Costs. Thus, it is the responsibility of the EOM and OCFO to ensure that budgets equal forecasts prior to submission of the Mayor's budget to Council, and to understand the basis of the forecasts. Therefore, no MOU summit is necessary at that stage.

In addition, agencies must provide testimony on their budgets to Council. This is the **second** opportunity for the District to scrutinize the basis for the budgets, and make any necessary changes prior to final Council approval.

Beginning in FY 2006, the City Administrator has streamlined the MOU process by signing Fixed Cost MOU's on behalf of all agencies. The Seller agencies—OPM, OCTO, and OFRM—all sign as well.

Finding # 2:

The second finding addresses deficiencies relating to the forecast process for telecommunications expenditures. Agency Telecommunications Coordinators (ATCs) do not always provide OCTO with sufficient information that reflects the telecommunications needs of their respective agencies and should be included in the forecast. As a result, the forecast process may not be as accurate as possible and may lead to spending pressures or under spending. Additionally, agencies' variable telecommunications needs are not fully considered during the forecast and budgetary processes.

Response to Finding # 2:

The observation is correct.

ATCs are selected by and report to the agencies and have a "dotted-line" relationship with OCTO. The actual ATC job varies greatly from agency to agency, and OCTO can only suggest what type of skills and capabilities are required to successfully perform the key, telecommunications related functions. OCTO has strongly recommended that ATC have a thorough understanding of telecommunications products, services, and a solid working knowledge of the principles of forecasting and budgeting. The information provided by ATCs, the abilities of the ATCs, and the degree to which ATCs are included in the decision making processes, all play a major role on the accuracy and usefulness of the data provided during the OCTO forecasting process.

Finding # 3:

The third finding addresses deficiencies in the inventory of telecommunications lines. ATCs do not know the inventory of telecommunication lines and services assigned to their respective agencies. Adequate knowledge of the inventory composition is necessary

EXHIBIT C. MANAGEMENT RESPONSE - OCFO

to perform a meaningful forecast for telecommunications expenditure for any budgetary period. Most agencies believe that because OCTO coordinates and oversees their telecommunications budget, OCTO should take responsibility for every aspect of telecommunications, to include inventory manage. As a result, agencies do no perform a proper review of their telecommunications bills prior to payments. Payments have been made for telecommunications lines that were either not needed or not known to exist.

Response to Finding # 3:

This observation is correct. Most agencies have not actively participated in the review, correction and validation of its telecommunications inventory each month. The responsibility for control and management of the District's telecommunications inventory was recently shifted from OCTO to OFRM. OFRM fully recognizes the problems and have already started to design inventory management processes and programs which will require active involvement from the agencies. The OFRM initiatives include:

- Developing and rolling out a new Fixed Cost Management System (FCMS) to serve as the single, on-line system for agencies to view, disputed and validate all fixed cost commodities, starting with telecommunications;
- Identifying and implementing a series of cost avoidance and waste removal programs;
- Designing and implementing new Rationalization Processes to assist agencies in selecting who should receive which telecommunications package of services; and,
- Developing a full range of quality assurance programs to conduct "selective audits" to ensure that agencies are following the rationalization processes to avoid slipping back into old habits.

Finding # 6: Duplicate Rent Payments

A total of eight duplicate payments were made to one lessor. The duplication occurred when OFRM made two extra payments (14 payments, instead of 12 payments) of four monthly billed amounts, $113,723, $35, $46,417 and $1,435, respectively. These billings were for rented premises in the 2100 block of Martin Luther King Avenue Jr. S.E.

Adjustments to Cancel Duplicate Wire Transfers

OFRM made several adjustments to cancel some of the duplicate wire transfers. However, OFRM did not make adjustments for all duplicate payments. We found that OFRM failed to cancel four duplicate payments totaling $161,160.

Although the number of duplicate payments is not excessive, all duplicate payments could be avoided if OFRM heightened its due diligence review of rental expenditures prior to posting to the general ledger. Duplication of rental payments results in increased expenditures for the District and a waste of limited resources.

Duplicate payments can also affect the ability of OFRM fixed-costs manager to provide OFRM with an accurate forecast, since historical costs are used as the basis in the projection of rental forecasts. In addition, the OBP estimates can be affected since OBP relies on OFRM fixed-costs forecasts in the preparation of agencies fixed-costs budgets.

EXHIBIT C. MANAGEMENT RESPONSE - OCFO

During our review, we also found that OPM and OFRM do not perform a monthly reconciliation of rental expenditures. OFRM's monthly billing summary report for rental expenditures should be reconciled with the OPM monthly rent roll. This will identify discrepancies in the summary of monthly expenditures and the rent roll prior to posting to the general ledger.

Response to Finding # 6:

OFRM does not agree with the finding as outlined. The payments in question were not duplicate payments which were explained to the auditor. A payment was made to the vendor and a check was cut and mailed to the vendor in question. The vendor never received the check due to circumstances surrounding hurricane Frances. The vendor notified the District and the check was cancelled. (See attached documentation). An attempt was made to wire the vendor the funds but due to incorrect bank information the wire transmission failed hence the wire was cancelled. (See attached documentation). Finally, a third check was issued to the vendor to which was duly received, thus completing the transaction. So there was no duplication of payments to the vendor.

Thank you for the opportunity to comment on your draft report. If you have any questions or concerns, please call me at (202) 727-3232.

Sincerely,
Barbara Jumper
Barbara Jumper
Associate Chief Financial Officer
Government Operations Cluster

cc: Natwar Gandhi, Chief Financial Officer
Sebastian Lorigo, Executive Director, Office of Integrity and Oversight
Mohammed Yussuf, Director Internal Audit
Mohamed Mohamed, Director of Financial Operations, OFRM
, OFRM

EXHIBIT D. MANAGEMENT RESPONSE - OCA

GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF CITY ADMINISTRATOR

★ ★ ★

Robert C. Bobb,
Deputy Mayor/City Administrator

August 8, 2006

Mr. Charles J. Willoughby
Inspector General for the District of Columbia
717 14th Street, N.W.
Washington, D.C. 20005

Re: OIG Draft Report – Audit of the Fixed-Costs Allocation Process
(OIG No. 05-2-10MA)

Dear Mr. Willoughby:

This letter gives my response to your recommendations for improving the District's Fixed-Costs Allocation Process.

Your staff recently completed an audit of the District's Fixed-Costs Allocation Process and arrived at a series of observations and recommended actions for each of the interested Offices, including the Office of the City Administrator (OCA). We appreciate that your office reviewed the District's processes related to fixed costs. In general, we agree with your recommendations. We believe they will help improve the allocation and oversight of fixed-costs. Our own view of the matter is, however, that fixed-costs have grown too much and that merely fixing the allocation process will not by itself bring them back under control.

We are very focused on lowering fixed-costs. We have pursued a strategy of restructuring the oversight of key aspects of fixed-costs to remove operational conflicts of interest and introducing cost savings programs. The full effect of some of these changes may not have been apparent until after your staff had completed its review of the facts on the ground. For example, in April, the Office of Financial Resource Management took over the function of telephony inventory management. This change by itself saved the District almost $5.5 million. We have also begun to guide our purchasing agencies toward adopting proven best practices like performance-based contracting and bundled equipment maintenance contracts that promise to reduce costs while boosting service delivery. We expect that in concert with your recommendations for improving the allocation process, fixed-costs will soon begin to fall.

EXHIBIT D. MANAGEMENT RESPONSE - OCA

2

In the meantime, we will begin carrying out the two actions you recommended for OCA:

FINDING 1. FIXED-COSTS MEMORANDUM OF UNDERSTANDING

Findings and Recommendations

Recommendation #4: Require the MOU to be signed by top officials of the Office of the Chief Financial Officer, OPM, OCTO and the user agencies.

Planned Action: At the start of the budget cycle, OCA will issue instructions that the top officials of in each of these agencies acknowledge their roles responsibilities and that of their respective agency with regard to fixed-costs allocation and oversight.

Recommendation #5: Request that a Mayor's Order or directive on fixed-costs be issued, which clearly spells out the responsibilities of: a) agencies that procure commodities (rent, telecommunications, etc.) categorized as fixed costs for use by other agencies: b) agencies using these commodities: and c) the administrative or paying agency.

Planned Action: At the start of the new administration, OCA will draft and request that the Mayor issue a directive that instructs each of the agencies on their role in managing fixed costs.

Let me or Oscar Rodriguez, Director of the Center for Innovation and Reform (727-9071), know if you have any questions.

Sincerely,

Robert C. Bobb

Robert C. Bobb
Deputy Mayor and City Administrator

EXHIBIT E. MANAGEMENT RESPONSE - OPM

GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF PROPERTY MANAGEMENT

Carol J. Mitten
Director

August 21, 2006

Mr. Charles J. Willoughby
Inspector General for the District of Columbia
717 14th Street, N.W.
Washington, D.C. 20005

Re: OIG Draft Report – Audit of the Fixed-Costs Allocation Process
(OIG No. 05-2-10MA)

Dear Mr. Willoughby:

Thank you for the opportunity to comment on the revised draft report of the Office of the Inspector General's (OIG) Audit of the Fixed-Costs Allocation Process. As we have said since the entrance interview, we are very supportive of your office's review of the processes related to fixed costs, and we welcome your recommendations.

FINDING 1. FIXED-COSTS MEMORANDUM OF UNDERSTANDING

Recommendations

#1: This recommendation is excellent, but will only serve one purpose: to enhance the role of the MOU as a budgeting tool. The recommendation does not recognize the reason why the MOU's have been signed at the commencement of the fiscal year in the first place – to authorize collection of the most recent fixed cost estimates (made in the August prior to the commencement of the new fiscal year). These collections are made regardless of whether the most recent estimate exceeds the budgeted amount or not.

At several points during the fiscal year (most notably, at the beginning), OFRM collects the fixed cost amounts reflected in the most recent estimates prepared by OPM. (We are unaware whether the same exercise is conducted with DPW and OCTO.) The agencies do not authorize this collection; OFRM is empowered to collect these monies without their consent and thereby potentially place the agencies (temporarily) in deficit. As the draft report notes, some agencies do not

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sign the MOU, but the collections occur in spite of their lack of consent. Moving the signing date to coincide with the release of the budget by the Mayor will reinforce the budgeted amounts, but will do nothing to address the collections issue. Can the OIG recommend a better way to manage incremental collections of fixed costs (in excess of budgeted amounts)?

#2. We agree.

#3. We agree.

#4. We agree.

#5. A Mayor's Order clarifying the management of fixed costs is long overdue. For instance, the Budget Support Act (BSA) in 2005 required that any excess fixed costs be carried forward to the next fiscal year. This new practice, once implemented by the OCFO, will be a significant departure for agencies that have relied on fixed-cost surpluses to cover program deficits in the past. Most important, however, is the fact that, without a mechanism to address the collections issue discussed in #1 above, misunderstandings and mid-fiscal-year budget problems will persist.

FINDING 4. RENT ADMINISTRATION AND MONITORING

OPM staff and the OIG audit team have had extensive discussions regarding the information contained in Table IV. We agree with the general conclusion of the report that, "The lack of automated leasing systems, the high volume or rental activity, and limited resources resulted in OPM not sufficiently monitoring operational expenses." However, we do not agree with some of the specific conclusions that are represented in Table IV. Rather than attempting to address each of the individual entries in Table IV, we will comment on the broader issues.

The category of issues represented by column four of Table IV is perhaps the largest area of disagreement that we have with the OIG report. Column four details certain leases for which the OIG concluded that OPM had not monitored base operating expenses. In each of these leases, the base amount for operating expenses was quoted as a fixed rate (e.g., $6.00 per square foot). By contrast, the practice in more recent leases is that the base for operating expenses is an amount to be determined subsequent to lease commencement (e.g., operating expenses to be incurred in calendar year 2007). In this latter type of lease, it is imperative to monitor the establishment of the base year to ensure that only appropriate categories of expense are included. However, in the former type of lease, the actual expenses incurred in the base year are irrelevant to lease administration, but (for good or ill) the base rate was negotiated prior to lease commencement. It is not subject to further adjustment. Therefore, the approximately $1.8 million in base operating expenses represented by column four are fixed, and no amount of monitoring on OPM's part can change that.

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We also disagree that a requirement to follow GAAP must be adhered to if the lease provides the landlord with flexibility regarding the use of cash accounting or accrual accounting. The examples cited where expenses incurred in one fiscal year were paid in another fiscal year are not, on their face, in error. It is certainly more challenging to administer a lease where the accounting is performed on a cash basis, but there is no *de facto* prohibition against it. Many of our older leases do not preclude the use of cash accounting.

Landlords are required to amortize capital expenses that relate to the building, including common areas and building structures and systems. In the example cited for 2100 Martin Luther King (Lease #87-38), the work performed that the OIG asserts should have been capitalized was tenant build-out performed within the leased space at the District's request. This was billed and paid as a fee-for-service, not as a component of rent.

One of the specific leases included in Table IV was PennBranch Shopping Center, 3220 Pennsylvania Avenue, S.E. (Lease # 98-03). The deficiencies cited had been determined by OPM and incorrect payments were being litigated during the time period of the OIG audit.

FINDING 5. ALLOCATION OF RENTAL EXPENDITURES

The OIG correctly identified 51 N Street, N.E. as a location in which the space allocations in the building had changed from the original space allocations, but the fixed cost budget and the rent roll did not reflect the change. Although the allocations were incorrect, no agency was being charged for rent that had not been allocated to it, whether those allocations were more or less than the actual occupied space.

The OIG incorrectly identified 3330 V Street, N.E. as a space with an erroneous space allocation. During FY04, DHS vacated the space that they had formerly occupied at 3330 V Street, N.E. (the space is shared with DOH) and the allocation shifted entirely to DOH. This reallocation was not anticipated at the beginning of the fiscal year, therefore, each agency had been budgeted for its allocation of rent according to the amount of space occupied at the beginning of the fiscal year. If OPM had known that a shift would occur mid-year, then the rent would have been allocated differently in the budget to reflect the anticipated space reallocation. However, OPM's practice is to charge the rent where it was allocated in the budget when such alterations occur mid-year, unless the agencies explicitly agree otherwise. As mentioned above, this practice preserves the application of fixed cost allotments to fixed cost commodities, rather than the application of program dollars to fixed costs or vice versa.

Recommendations

#14. It is clear from the BSA language proposed by the Mayor and passed by the Council in 2005, that the practice of applying fixed cost dollars to fixed cost expenditures (rather than allowing them to be redirected to program costs) is the Mayor's policy preference. Although that policy was not made explicit until the

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FY2005 BSA, it is the policy to which OPM has subscribed since November 2003 and which informed the actions taken by OPM in the case of 3330 V Street, N.E., described above. On that basis, it is most important that once a year OPM validate with agencies the amount of space that they occupy in a given building for the purpose of budget development.

That being said, however, it is important for other reasons that agencies keep OPM informed of alterations in the amount of space they occupy. If an agency is in leased space, a reallocation of space likely means that an agency is moving (even within a given building) – OPM is the agency's contact with the landlord and should be informed (so that we can ensure that the landlord is informed). If an agency is vacating leased space in advance of lease expiration, OPM should be informed so that we can try and identify a backfill. If an agency requires additional space, we need to know that well in advance. In each case, we recommend a policy that requires agencies to inform OPM when they begin contemplating a space alteration. We would rather that this role be considered an on-going responsibility rather than a quarterly responsibility.

#15. We agree. In fact, we are having on-going discussions with OBP as to how to put more information into the hands of the agencies to enhance the accuracy of the information that we share, enhance agency knowledge of the fixed cost process, and increase accountability.

OTHER MATTERS OF INTEREST

We are grateful to the OIG audit team for making the additional effort to develop the section entitled Other Matters of Interest. Through their study of fixed costs, the OIG team discovered that there are many complex budgeting and financial management challenges that require further consideration, and their additional comments will provide a good basis for future discussions.

In general, both the findings and recommendations of the OIG report that related to OPM are well founded and constructive. The only exceptions are some of the specific conclusions drawn in Finding 4.

Thank you, again for the opportunity to review the revised draft report.

Sincerely,

Carol J. Mitten

Carol J. Mitten
Director

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