

PERFORMANCE AND FINANCIAL AUDIT
OF THE
BUREAU OF CONSTRUCTION CODES
DEPARTMENT OF CONSUMER AND INDUSTRY SERVICES
October 1, 1998 through September 30, 2000

EXECUTIVE DIGEST

BUREAU OF CONSTRUCTION CODES

INTRODUCTION

This report contains the results of our performance* and financial* audit of the Bureau of Construction Codes, Department of Consumer and Industry Services. The financial portion of our audit covered the period October 1, 1998 through September 30, 2000.

AUDIT PURPOSE

This performance and financial audit was conducted as part of the constitutional responsibility of the Office of the Auditor General. Performance audits are conducted on a priority basis related to the potential for improving effectiveness* and efficiency*. Financial audits are conducted at various intervals to provide for enhanced financial reporting of significant State programs and/or activities and to complement the annual audit of the State's financial statements. Also, this audit complements the Departmentwide financial audit.

BACKGROUND

The Bureau administers laws governing the construction of buildings, including electrical, plumbing, and mechanical laws; barrier free designs; building officials' and inspectors' registration; boiler installation and operation; and elevator safety. Bureau staff review plans for proposed construction and conduct inspections to determine compliance with the various construction codes. In addition, the Bureau receives permit and fee revenue related to these activities. The financial transactions for

* See glossary at end of report for definition.

the Bureau's boiler and elevator programs are accounted for in the State's General Fund. The financial transactions for the rest of the Bureau's programs and operations are accounted for in the State Construction Code Fund.

For fiscal year 1999-2000, the Bureau reported General Fund expenditures and operating transfers out totaling approximately \$3.9 million and State Construction Code Fund expenditures and operating transfers out totaling approximately \$9.7 million. As of September 30, 2000, the Bureau had 161 employees, including student interns and temporary inspectors.

AUDIT OBJECTIVES,
CONCLUSIONS, AND
NOTEWORTHY
ACCOMPLISHMENTS

Audit Objective: To assess the Bureau's effectiveness in meeting its program responsibilities and goals*.

Conclusion: We determined that the Bureau was generally effective in meeting its program responsibilities and goals. However, our assessment disclosed one material condition*:

- The Bureau needs to improve its controls over the monitoring of inspections to ensure that inspection fees are properly invoiced and collected. The Bureau also needs to develop procedures to ensure that violations identified during inspections are corrected in a timely manner. (Finding 1)

The Bureau agreed with the corresponding recommendations and informed us that procedures will be developed to ensure that all payments for the inspection of boilers and elevating equipment are received and that correction orders are followed up and violations corrected. The Bureau emphasized that the correction orders and violations that have not

* See glossary at end of report for definition.

been corrected are minor in nature and do not endanger the users of the equipment. The Bureau added that all major violations that have an impact on customer safety are followed up in a timely manner and that the hand-held computer system has been corrected to properly generate invoices for all inspection activity of premanufactured housing units.

Our assessment also disclosed reportable conditions* related to permit monitoring, boiler inspections, and elevating equipment inspections (Findings 2 through 4).

Noteworthy Accomplishments: The Bureau converted to new hand-held computers for inspectors, which the Bureau reported increased productivity and enabled the Bureau to be year 2000 compliant. Also, the Bureau increased the speed in issuing permits so that 97% of permits were issued within two days of receipt. In addition, the Bureau staggered renewal dates of the plumbing and mechanical licenses to improve the effectiveness of processing licenses.

Audit Objective: To assess and report on the Bureau's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the financial statements, and on its internal control* over financial reporting, based on our audit of the financial statements.

Conclusion: Our assessment of compliance did not disclose any instances of noncompliance that could have a direct and material effect on the financial statements. Also, our assessment of internal control over financial reporting did not disclose any material weaknesses*. However, our assessment identified

* See glossary at end of report for definition.

reportable conditions related to the recording of revenues and accounts receivable and the reconciliation of Permits Plus (Findings 5 and 6).

Audit Objective: To audit the State Construction Code Fund financial statements as of and for the fiscal years ended September 30, 2000 and September 30, 1999.

Conclusion: We expressed an unqualified opinion* on the State Construction Code Fund financial statements.

AUDIT SCOPE AND
METHODOLOGY

Our audit scope was to examine the program and other records of the Bureau of Construction Codes. Also, our audit scope was to examine the financial records for the period October 1, 1998 through September 30, 2000. Our audit was conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

Our audit procedures included examination of the Bureau's programs and operations primarily for the period October 1, 1997 through September 30, 2000. Based on our preliminary review, we selected program and other records for review to assess the Bureau's effectiveness in meeting its program responsibilities and goals. Also, we analyzed financial records and tested records related to licenses and permits.

AGENCY RESPONSES
AND PRIOR AUDIT
FOLLOW-UP

Our audit report includes 6 findings and 7 corresponding recommendations. The Bureau's preliminary response

* See glossary at end of report for definition.

indicated that it agreed with all of the recommendations and that it had or will implement them.

The Bureau complied with 6 of the 12 prior audit recommendations. We repeated 3 prior audit recommendations and the other 3 prior audit recommendations were rewritten for inclusion in this audit report.

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August 24, 2001

Ms. Kathleen M. Wilbur, Director
Department of Consumer and Industry Services
G. Mennen Williams Building
Lansing, Michigan

Dear Ms. Wilbur:

This is our report on the performance and financial audit of the Bureau of Construction Codes, Department of Consumer and Industry Services. The financial portion of our audit covered the period October 1, 1998 through September 30, 2000.

This report contains our executive digest; description of agency; audit objectives, scope, and methodology and agency responses and prior audit follow-up; comments, findings, recommendations, and agency preliminary responses; and independent auditor's reports on compliance and on internal control over financial reporting and on the financial statements. This report also contains the State Construction Code Fund financial statements and notes to the financial statements and a glossary of acronyms and terms.

Our comments, findings, and recommendations are organized by audit objective. The agency preliminary responses were taken from the agency's responses subsequent to our audit fieldwork. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a formal response within 60 days after release of the audit report.

We appreciate the courtesy and cooperation extended to us during this audit.

AUDITOR GENERAL

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Description of Agency

The Bureau of Construction Codes is organized within the Department of Consumer and Industry Services. The Bureau administers laws governing the construction of buildings, including electrical, plumbing, and mechanical laws; barrier free designs; building officials' and inspectors' registration; boiler installation and operation; and elevator safety. Bureau staff review plans for proposed construction and conduct inspections to determine compliance with the various construction codes. In addition, the Bureau receives permit and fee revenue related to these activities. The financial transactions for the Bureau's boiler and elevator programs are accounted for in the State's General Fund. The financial transactions for the rest of the Bureau's programs and operations are accounted for in the State Construction Code Fund.

The Bureau provides support staff to the following commission and boards to assist them in achieving their objectives:

- a. The State Construction Code Commission was created in 1973 and is governed by Sections 125.1501 - 125.1531 of the *Michigan Compiled Laws*. The Commission's purpose is to promulgate the State Construction Code, which governs the construction, use, and occupancy of buildings and structures; the manufacture and installation of building components and equipment; the construction and installation of premanufactured units; and other requirements relating to safety in such buildings and structures.
- b. The Barrier Free Design Board was created in 1966 and is governed by Sections 125.1351 - 125.1356 of the *Michigan Compiled Laws*. The Board's purpose is to review and process requests for exceptions to barrier free design specifications, to require alternatives when exceptions are granted, to review and process complaints of noncompliance with barrier free design specifications, and to make recommendations for barrier free design rules.
- c. The Electrical Administrative Board was created in 1956 and is governed by Sections 338.881 - 338.892 of the *Michigan Compiled Laws*. The Board prescribes rules and standards for licensing electricians and electrical contractors. Also, the Board accepts license applications, conducts examinations, grants licenses, and may investigate violations and conduct hearings in reference to any of the matters specified in Sections 338.881 - 338.892 of the *Michigan Compiled Laws*.

- d. The Plumbing Board was created in 1929 and is governed by Sections 338.901 - 338.917 of the *Michigan Compiled Laws*. The Board prescribes rules and standards for licensing plumbers. Also, the Board accepts license applications, conducts examinations, grants licenses, and may investigate violations and conduct hearings in reference to any of the matters specified in Sections 338.901 - 338.917 of the *Michigan Compiled Laws*.
- e. The Board of Mechanical Rules was created in 1984 and is governed by Sections 338.971 - 338.988 of the *Michigan Compiled Laws*. The Board prescribes rules and standards for licensing mechanical contractors. Also, the Board accepts license applications, conducts examinations, grants licenses, and may investigate violations and conduct hearings in reference to any of the matters specified in Sections 338.971 - 338.988 of the *Michigan Compiled Laws*.
- f. The Board of Boiler Rules was created in 1966 and is governed by Sections 408.751 - 408.776 of the *Michigan Compiled Laws*. The Board regulates the construction, installation, use, and repair of boilers and enforces uniform rules and regulations. Also, the Board accepts license applications, conducts examinations, and grants licenses for boiler installers, repairers, and inspectors.
- g. The Elevator Safety Board was created in 1967 and is governed by Sections 408.801 - 408.824 and 338.2151 - 338.2160 of the *Michigan Compiled Laws*. The Board has the responsibility to provide for the safe use of elevators by the public. The Board regulates the construction, installation, alteration, maintenance, repair, and operation of elevators and enforces uniform rules and regulations. Also, the Board accepts license applications, conducts examinations, and grants licenses for elevator contractors and inspectors.

For fiscal year 1999-2000, the Bureau reported General Fund expenditures and operating transfers out totaling approximately \$3.9 million and State Construction Code Fund expenditures and operating transfers out totaling approximately \$9.7 million. As of September 30, 2000, the Bureau had 161 employees, including student interns and temporary inspectors.

Audit Objectives, Scope, and Methodology and Agency Responses and Prior Audit Follow-Up

Audit Objectives

Our performance and financial audit of the Bureau of Construction Codes, Department of Consumer and Industry Services, had the following objectives:

1. To assess the Bureau's effectiveness in meeting its program responsibilities and goals.
2. To assess and report on the Bureau's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the financial statements, and on its internal control over financial reporting, based on our audit of the financial statements.
3. To audit the State Construction Code Fund financial statements as of and for the fiscal years ended September 30, 2000 and September 30, 1999.

Audit Scope

Our audit scope was to examine the program and other records of the Bureau of Construction Codes. Also, our audit scope was to examine the financial records for the period October 1, 1998 through September 30, 2000. Our audit was conducted in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

Audit Methodology

Our audit procedures, performed from September 2000 through January 2001, included examination of the Bureau's programs and operations primarily for the period October 1, 1997 through September 30, 2000. Based on our preliminary review, we selected program and other records for review to assess the Bureau's effectiveness in meeting its program responsibilities and goals. Also, we analyzed financial records, reviewed licensing and permit issuance procedures and records, reviewed examination integrity, tested records related to licenses and permits, and discussed operational practices with agency.

Agency Responses and Prior Audit Follow-Up

Our audit report includes 6 findings and 7 corresponding recommendations. The Bureau's preliminary response indicated that it agreed with all of the recommendations and that it had or will implement them.

The agency preliminary response which follows each recommendation in our report was taken from the agency's written comments and oral discussion subsequent to our audit fieldwork. Section 18.1462 of the *Michigan Compiled Laws* and Department of Management and Budget Administrative Guide procedure 1280.02 require the Department of Consumer and Industry Services to develop a formal response to our audit findings and recommendations within 60 days after release of the audit report.

The Bureau complied with 6 of the 12 prior audit recommendations. We repeated 3 prior audit recommendations and the other 3 prior audit recommendations were rewritten for inclusion in this audit report.

COMMENTS, FINDINGS, RECOMMENDATIONS, AND AGENCY PRELIMINARY RESPONSES

EFFECTIVENESS IN MEETING PROGRAM RESPONSIBILITIES AND GOALS

COMMENT

Background: The State Construction Code Act requires contractors or homeowners, prior to the commencement of work regulated by the Code, to obtain a permit from the appropriate agency for construction of buildings, including permits for electrical, plumbing, and mechanical work and elevators and related equipment. The appropriate enforcement agency can be the Bureau of Construction Codes within the Department of Consumer and Industry Services or a local unit of government depending on the type of construction and geographical location in the State. The Bureau and insurance companies perform inspections of boiler installation and operations.

Audit Objective: To assess the Bureau's effectiveness in meeting its program responsibilities and goals.

Conclusion: We determined that the Bureau was generally effective in meeting its program responsibilities and goals. However, our assessment disclosed one material condition. The Bureau needs to improve its controls over the monitoring of inspections to ensure that inspection fees are properly invoiced and collected. The Bureau also needs to develop procedures to ensure that violations identified during inspections are corrected in a timely manner.

Our assessment also disclosed reportable conditions related to permit monitoring, boiler inspections, and elevating equipment inspections.

Noteworthy Accomplishments: The Bureau converted to new hand-held computers for inspectors, which the Bureau reported increased productivity and enabled the Bureau to be year 2000 compliant. Also, the Bureau increased the speed in issuing permits so that 97% of permits were issued within two days of receipt. In addition, the Bureau staggered renewal dates of the plumbing and mechanical licenses to improve the effectiveness of processing licenses.

FINDING

1. Monitoring of Invoices and Correction Orders

The Bureau needs to improve its controls over the monitoring of inspections to ensure that inspection fees are properly invoiced and collected. The Bureau also needs to develop procedures to ensure that violations identified during inspections are corrected in a timely manner.

The Bureau conducts inspections of boilers, elevating equipment, and premanufactured housing units, as required by State law, and submits invoices to owners for payment of the inspections and certificates of operation as required by its administrative rules. Also, if violations are noted during the inspection, the inspector completes and forwards a correction order to the owner stating a time limit within which the correction ordered must be completed. The boiler correction order serves as a notice of suspension if the owner does not comply by the compliance date. Noncompliance with the elevator correction order may subject the holder of the certificate of operation to administrative rule penalty provisions.

Our review disclosed:

- a. The Bureau did not effectively monitor outstanding invoices to ensure that payments for the inspection of boilers and elevating equipment were received.

As of September 30, 2000, there were 9,093 invoices for boiler inspections totaling \$455,155 and 1,295 invoices for elevating equipment inspections totaling \$101,097 that were outstanding, including some dating back to 1994. Bureau staff informed us that they periodically generated outstanding invoice reports; however, the Bureau did not have any processes in place to actively and consistently follow up on outstanding invoices.

- b. The Bureau did not complete invoices for inspections of premanufactured housing units during the period November 1999 through September 2000.

During 1998, the Bureau implemented a new hand-held computer system, which allowed inspectors to log daily inspection activity. However, the system did not properly generate invoices for all inspection activity. As a result, 30 inspection invoices totaling \$31,528 were not generated and forwarded to manufacturers. The Bureau rules, regulations, and statutes require owners

and manufacturers to pay for required inspections and certificates of operation.

- c. The Bureau did not have procedures to ensure that violations identified during inspections of boilers and elevating equipment were corrected in a timely manner.

The Bureau issues correction orders whenever a violation is identified during a licensing inspection. As of September 30, 2000, there were 341 outstanding correction orders resulting from boiler inspections dating back to January 1996 and 6,090 outstanding correction orders resulting from elevating equipment inspections dating back to March 1987. Bureau staff informed us that they periodically generated delinquent correction order reports; however, the Bureau did not have a process to ensure that these correction orders were followed up and that the violations were corrected.

Timely follow-up of correction orders is necessary to ensure proper repair and use of boilers and elevating equipment.

RECOMMENDATIONS

We recommend that the Bureau improve its controls over the monitoring of inspections to ensure that inspection fees are properly invoiced and collected.

We also recommend that the Bureau develop procedures to ensure that violations identified during inspections are corrected in a timely manner.

AGENCY PRELIMINARY RESPONSE

The Bureau agreed with the recommendations and informed us that procedures will be developed to ensure that all payments for the inspection of boilers and elevating equipment are received and that correction orders are followed up and violations corrected. The Bureau emphasized that the correction orders and violations that have not been corrected are minor in nature and do not endanger the users of the equipment. The Bureau added that all major violations that have an impact on customer safety are followed up in a timely manner and that the hand-held computer system has been corrected to properly generate invoices for all inspection activity of premanufactured housing units.

FINDING

2. Permit Monitoring

The Bureau did not use its automated permit system to effectively monitor the status of open permits and did not administratively close permits on a timely basis.

The Bureau issues permits for installation, construction, and other projects involving building, electrical, mechanical, and plumbing contractors and then performs inspections to ensure compliance with standards adopted by the Bureau. The Bureau developed an automated system to monitor the status of permits issued and assigned to inspectors. Inspectors electronically transmitted records of their daily activities, including final inspections, to the automated system. After review, administrative personnel would close the permits. However, the Bureau did not effectively monitor the status of inspections at sufficient intervals to detect or prevent a backlog of open permits.

Our review of permits disclosed:

- a. The Bureau had permits open for several years without any inspection.

Standards adopted by the Bureau specify that permits will become invalid if work is not commenced within 6 months after issuance of the permit or if work is suspended or abandoned for a period of 6 months after work has commenced.

As of September 30, 2000, there were 86,383 open permits. Our review disclosed that 30,651 (35%) of the open permits had not received any inspections within the previous 12 months. We also reviewed 69 permits and determined that 20 (29%) had no activity for periods ranging from 7 months to 29 months. The Bureau informed us that some of the 30,651 open permits were not active; however, there was no methodology in place to identify which permits were still active.

- b. The Bureau did not monitor open permits that were in hold status.

As of September 30, 2000, the Bureau had 2,203 open permits that had been placed in hold status, including 1 that had been placed in hold status in April 1988. Permits are placed in hold status because of insufficient fee payment,

the contractor's license is on hold, the contractor has outstanding violations on other projects, the contractor did not sign the application form, or the address for the construction site was insufficient.

The Bureau did not have procedures in place regarding how often open permits should be monitored and closed. The last administrative review and closing of permits was performed in 1997.

With proper monitoring and more frequent administrative closures, the Bureau can reduce the number of inactive permits on its system.

We reported a similar finding in a prior audit. In response to the prior audit finding, the Bureau stated that it agreed with the recommendation and was in the process of obtaining a new permit system that would allow the Bureau to monitor open permits and either make the necessary inspections or cancel a permit in accordance with the provisions of the State Construction Code.

RECOMMENDATION

WE AGAIN RECOMMEND THAT THE BUREAU USE ITS AUTOMATED PERMIT SYSTEM TO EFFECTIVELY MONITOR THE STATUS OF OPEN PERMITS AND ADMINISTRATIVELY CLOSE PERMITS ON A TIMELY BASIS.

AGENCY PRELIMINARY RESPONSE

The Bureau agreed with the recommendation and informed us that procedures will be developed to close open permits after a set amount of time. The Bureau added that it will also review the impact of closing permits if no work has been performed for 6 months. The Bureau further indicated that the procedures will also address the issue of closing applications that are in hold status.

FINDING

3. Boiler Inspections

The Bureau did not inspect some boilers in a timely manner as required by Section 408.769 of the *Michigan Compiled Laws*.

Section 408.769 of the *Michigan Compiled Laws* requires annual or biennial inspections of boilers depending on the type of boiler. Inspections determine

whether a boiler has been constructed, installed, repaired, and operated in accordance with the Boiler Act of 1965 (Act 290, P.A. 1965). In addition, Section 408.774 of the *Michigan Compiled Laws* states that it is unlawful for any person, firm, partnership, or corporation to operate a boiler without a valid inspection certificate.

The Bureau maintains a database that lists all boilers in operation, the last inspection date, and the number of days an inspection was overdue. As of September 30, 2000, the database included 70,717 boilers registered in the State, with 9,920 (14%) overdue for inspection. The inspections for 5,144 (52%) of these boilers were overdue between 90 days and 1 year. In addition, there were 461 inspections that were more than 6 years overdue. Of the registered boilers overdue for an inspection, 2,684 (27%) were insured boilers and therefore private insurance companies were responsible for the inspections. However, if the insurance companies fail to file an inspection report, as required by Section 408.770 of the *Michigan Compiled Laws*, the inspections become the Bureau's responsibility.

Timely inspections of boilers are necessary to ensure that the public is protected from the operation of unsafe boilers.

We reported a similar finding in a prior audit. In response to the prior audit finding, the Bureau stated that it agreed with the recommendation and would evaluate the boiler program to determine if additional staff were necessary to meet its statutory functions and to assess alternative approaches for the Boiler Division to function more effectively and efficiently.

RECOMMENDATION

WE AGAIN RECOMMEND THAT THE BUREAU INSPECT BOILERS IN A TIMELY MANNER AS REQUIRED BY SECTION 408.769 OF THE *MICHIGAN COMPILED LAWS*.

AGENCY PRELIMINARY RESPONSE

The Bureau agreed with the recommendation and informed us that it will modify its procedures to place priority on inspections that are overdue and that the Bureau is also researching ways to ensure that inspection agencies file timely reports. The Bureau added that a new hand-held inspection system is currently being developed

that should increase inspector activity and that, once this system is in place, a study will be conducted to determine if the Boiler Division has enough inspection personnel.

FINDING

4. Elevating Equipment Inspections

The Bureau did not inspect some elevators and elevating equipment in a timely manner as required by *Michigan Administrative Code R 408.8134*.

Michigan Administrative Code R 408.8134 requires passenger and freight elevators, belt manlifts, and special elevating devices to be inspected annually; escalators, dumbwaiters, inclined lifts, one-person elevators, wheelchair-elevating devices in buildings other than private residences, and sidewalk elevators to be inspected biennially; and personal hoists to be inspected as least once every 30 days.

As of September 30, 2000, 19,182 elevating devices required annual inspection, 2,540 required biennial inspection, and approximately 1,123 new devices needed to be inspected before being placed into service each year.

We reviewed the inspection activities of the Elevator Division, which is responsible for the elevator inspections. We determined that 10,052 (52%) of 19,311 and 9,134 (49%) of 18,825 elevating devices were not inspected for fiscal years 1999-2000 and 1998-99, respectively. We also determined that, as of September 30, 2000, 6,575 (31%) of 21,545 elevator inspections were past due ranging between six months and six years.

We noted that the number of elevator inspectors ranged from a low of 12 inspectors in January 2000 to a high of 20 inspectors April 1998. However, the Bureau had not determined the number of inspectors needed to meet the required frequency of elevator inspections. Bureau staff informed us that it was difficult to recruit qualified elevator inspectors because of high rates of compensation in the construction industry.

Timely periodic inspections help ensure that equipment receives necessary adjustments, calibrations, and major repairs. Inspections also verify that routine maintenance and required repairs have been performed.

We reported a similar finding in a prior audit. In response to the prior audit finding, the Bureau stated that it agreed with the recommendation and would evaluate possible methods to obtain additional staff for the elevator inspection program.

RECOMMENDATION

WE AGAIN RECOMMEND THAT THE BUREAU INSPECT ELEVATORS AND ELEVATING EQUIPMENT IN A TIMELY MANNER AS REQUIRED BY *MICHIGAN ADMINISTRATIVE CODER* 408.8134.

AGENCY PRELIMINARY RESPONSE

The Bureau agreed with the recommendation but noted that the Elevator Division has not been able to be fully staffed for a long period of time. The Bureau informed us that it will evaluate possible corrective actions that involve a combination of either increasing the number of inspections per employee or obtaining additional staff for the elevator inspection program.

The Bureau added that examples of items under consideration are: analyzing the assignment of staff to ensure that the distribution of inspectors is appropriate; following up certain violation notices by central office staff for cases in which a reinspection is not needed; installing a hand-held data collection system; and relying on certifications by contractors of load tests at the time of initial installation.

FINANCIAL ACCOUNTING AND INTERNAL CONTROL

COMMENT

Audit Objective: To assess and report on the Bureau's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the financial statements, and on its internal control over financial reporting, based on our audit of the financial statements.

Conclusion: Our assessment of compliance did not disclose any instances of noncompliance that could have a direct and material effect on the financial

statements. Also, our assessment of internal control over financial reporting did not disclose any material weaknesses. However, our assessment identified reportable conditions related to the recording of revenues and accounts receivable and the reconciliation of Permits Plus.

FINDING

5. Recording of Revenues and Accounts Receivable

The Bureau needs to improve its internal control to ensure the proper recording of revenues and corresponding accounts receivable.

Department of Management and Budget (DMB) Administrative Guide procedure 1210.27 requires the recording of revenues in the period that they become susceptible to accrual and are measurable.

The Bureau assesses fees for inspections of boilers, elevating equipment, premanufactured housing units, and construction projects. These inspection fees are recorded in both the State's General Fund and in the State Construction Code Fund. In accordance with DMB procedure, these inspection fees should be recorded as revenues as soon as the inspections have been completed even if the fees have not been collected.

Our review disclosed:

- a. As of September 30, 2000, the Bureau had not recorded all fees assessed, but not collected, for inspections of premanufactured housing units and plan reviews. This resulted in understating revenues and accounts receivable in the State Construction Code Fund by approximately \$34,800.
- b. As of September 30, 1999, the Bureau had not recorded all fees assessed, but not collected, for inspections of boilers, elevating equipment, plan reviews and permits in hold status. This resulted in understating revenues and accounts receivable in the State's General Fund by approximately \$617,200 and in the State Construction Code Fund by approximately \$26,800. Of the understatement in the State's General Fund, \$342,000 pertained to the inspection of boilers and \$275,200 pertained to the inspection of elevating equipment.

The Bureau needs to properly record accruals to ensure the accuracy of the Department of Consumer and Industry Services' General Fund financial schedules and the State Construction Code Fund's financial statements.

RECOMMENDATION

We recommend that the Bureau improve its internal control to ensure the proper recording of revenues and corresponding accounts receivable.

AGENCY PRELIMINARY RESPONSE

The Bureau agreed with the recommendation and informed us that controls are being developed to ensure the proper recording of all revenues and that documentation to support financial transactions is properly retained.

FINDING

6. Reconciliation of Permits Plus

The Bureau should reconcile its permit database system (Permits Plus) with the Michigan Administrative Information Network* (MAIN) to improve its effectiveness as a management tool.

The Bureau established Permits Plus to record, track, and manage permits. Through Permits Plus, the Bureau issued 49,211 and 49,130 permits for fiscal years 1999-2000 and 1998-99, respectively. The Bureau entered permit application information into Permits Plus, including revenues received, based upon the original applications and money received by the Department of Consumer and Industry Services' Receipts Accounting Section. However, Permits Plus did not maintain account code information nor did it contain a field for an audit trail that would allow periodic reconciliation of permit revenues with either the Department's internal receipts accounting system or with MAIN to verify revenues and other data related to permits and licenses.

We compared the permit revenue activity in Permits Plus with MAIN and noted differences of \$195,000 and \$284,000 during fiscal years 1999-2000 and 1998-99, respectively. Because the Bureau does not use Permits Plus in the accounting of

* See glossary at end of report for definition.

permit revenues, we performed other auditing procedures to ensure that revenues were properly recorded. However, periodic reconciliation of Permits Plus to MAIN would help identify undetected errors or irregularities because the Bureau uses Permits Plus to establish the year-end accounts receivable, which are then recorded in the State Construction Code Fund. DMB Administrative Guide procedure 1210.27 requires prompt and proper reconciliation of decentralized subsidiary ledgers to the general accounting system's control totals during the closing process.

As a good management tool, the Bureau should modify Permits Plus and reconcile the data with revenues recorded in MAIN to help ensure its integrity.

RECOMMENDATION

We recommend that the Bureau reconcile Permits Plus with MAIN to improve its effectiveness as a management tool.

AGENCY PRELIMINARY RESPONSE

The Bureau agreed with the recommendation and informed us that procedures will be developed to reconcile its permit database system with MAIN.

FINANCIAL STATEMENTS

Audit Objective: To audit the State Construction Code Fund financial statements as of and for the fiscal years ended September 30, 2000 and September 30, 1999.

Conclusion: We expressed an unqualified opinion on the State Construction Code Fund financial statements.

Independent Auditor's Report on Compliance and
on Internal Control Over Financial Reporting

January 26, 2001

Ms. Kathleen M. Wilbur, Director
Department of Consumer and Industry Services
G. Mennen Williams Building
Lansing, Michigan

Dear Ms. Wilbur:

We have audited the financial statements of the State Construction Code Fund, Department of Consumer and Industry Services, as of and for the fiscal years ended September 30, 2000 and September 30, 1999 and have issued our report thereon dated January 26, 2001. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the State Construction Code Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the State Construction Code Fund's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or

operation of the internal control over financial reporting that, in our judgment, could adversely affect the State Construction Code Fund's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in Findings 5 and 6.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that neither of the reportable conditions described in the previous paragraph is a material weakness.

This report is intended solely for the information and use of the Department of Consumer and Industry Services, the State's management, and the Legislature and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

Independent Auditor's Report on
the Financial Statements

January 26, 2001

Ms. Kathleen M. Wilbur, Director
Department of Consumer and Industry Services
G. Mennen Williams Building
Lansing, Michigan

Dear Ms. Wilbur:

We have audited the accompanying balance sheet of the State Construction Code Fund, Department of Consumer and Industry Services, as of September 30, 2000 and September 30, 1999 and the related statement of revenues, expenditures, operating transfers, and changes in fund balance and statement of revenues, expenditures, operating transfers, and changes in fund balance - budget and actual for the fiscal years then ended. These financial statements are the responsibility of the State Construction Code Fund's management and the Department's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1b, the accompanying financial statements present only the State Construction Code Fund and are not intended to present fairly the financial position and results of operations of the State of Michigan or its special revenue funds.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the State Construction Code Fund as of

September 30, 2000 and September 30, 1999 and the results of its operations for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated January 26, 2001 on our tests of the State Construction Code Fund's compliance with certain provisions of laws, regulations, contracts and grants and on our consideration of its internal control over financial reporting. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

AUDITOR GENERAL

STATE CONSTRUCTION CODE FUND
 Department of Consumer and Industry Services
 Balance Sheet
 As of September 30

	<u>2000</u>	<u>1999</u>
ASSETS		
Cash	\$	\$ 31,736
Equity in Common Cash	12,470,468	13,243,030
Other current assets	<u>56,793</u>	<u></u>
Total Assets	<u>\$ 12,527,261</u>	<u>\$ 13,274,766</u>
LIABILITIES AND FUND BALANCE		
Liabilities:		
Warrants outstanding	\$ 15,675	\$ 27,417
Accounts payable and other liabilities	297,653	236,062
Amounts due to other funds	<u>35,677</u>	<u>21,674</u>
Total Liabilities	<u>\$ 349,005</u>	<u>\$ 285,153</u>
Fund Balance:		
Fund Balance - Reserved	\$ 45,887	\$ 47,874
Fund Balance - Unreserved	<u>12,132,370</u>	<u>12,941,740</u>
Total Fund Balance	<u>\$ 12,178,256</u>	<u>\$ 12,989,614</u>
Total Liabilities and Fund Balance	<u>\$ 12,527,261</u>	<u>\$ 13,274,766</u>

The accompanying notes are an integral part of the financial statements.

STATE CONSTRUCTION CODE FUND
 Department of Consumer and Industry Services
 Statement of Revenues, Expenditures, Operating Transfers, and Changes in Fund Balance
Fiscal Years Ended September 30

	<u>2000</u>	<u>1999</u>
REVENUES		
Permits and fees by functional unit:		
Plumbing	\$ 1,930,147	\$ 2,073,782
Electrical	2,642,354	2,643,299
Building and Plan Review	1,380,380	1,325,579
Mechanical	1,967,320	2,046,007
Local Government and Consumer Services	92,132	169,412
Code Book Sales	<u>92,550</u>	<u>157,290</u>
Total Permits and Fees	<u>\$ 8,104,883</u>	<u>\$ 8,415,370</u>
 Miscellaneous		
Interest	\$ 808,443	\$ 669,991
Other income	<u>2,921</u>	<u>9,821</u>
Total Miscellaneous	<u>\$ 811,364</u>	<u>\$ 679,812</u>
 Total Revenues	<u>\$ 8,916,247</u>	<u>\$ 9,095,182</u>
 EXPENDITURES		
Current	<u>\$ 9,661,818</u>	<u>\$ 8,904,120</u>
Total Expenditures	<u>\$ 9,661,818</u>	<u>\$ 8,904,120</u>
 Excess of Revenues and Other Sources Over (Under) Expenditures	<u>\$ (745,570)</u>	<u>\$ 191,062</u>
 OTHER FINANCING SOURCES (USES)		
Operating Transfers Out:		
Department of Civil Service	\$ (63,187)	\$ (57,813)
Department of Treasury	<u>(2,600)</u>	<u>(2,200)</u>
Total Operating Transfers Out	<u>\$ (65,787)</u>	<u>\$ (60,013)</u>
 Total Other Financing Sources (Uses)	<u>\$ (65,787)</u>	<u>\$ (60,013)</u>
 Excess of Revenues and Other Sources Over (Under) Expenditures and Other Uses	\$ (811,357)	\$ 131,049
 Fund Balance - Beginning of fiscal year	<u>12,989,614</u>	<u>12,858,565</u>
 Fund Balance - End of fiscal year	<u>\$ 12,178,256</u>	<u>\$ 12,989,614</u>

The accompanying notes are an integral part of the financial statements.

STATE CONSTRUCTION CODE FUND
Department of Consumer and Industry Services
Statement of Revenues, Expenditures, Operating Transfers,
and Changes in Fund Balance - Budget and Actual
Fiscal Years Ended September 30

<u>Statutory/Budgetary Basis</u>	<u>2000</u>		Variance Favorable (Unfavorable)
	<u>Budget</u>	<u>Actual</u>	
REVENUES AND OTHER SOURCES			
Construction code fees	\$ 8,104,883	\$ 8,104,883	\$
Miscellaneous	811,364	811,364	
Total Revenues and Other Sources	<u>\$ 8,916,247</u>	<u>\$ 8,916,247</u>	<u>\$ 0</u>
EXPENDITURES, OPERATING TRANSFERS OUT, AND ENCUMBRANCES			
Current expenditures	\$ 9,956,550	\$ 9,661,818	\$ 294,732
Operating transfer out - Department of Civil Service		63,187	(63,187)
Operating transfer out - Department of Treasury		2,600	(2,600)
Encumbrances at September 30		12,983	(12,983)
Total Expenditures, Operating Transfers Out, and Encumbrances	<u>\$ 9,956,550</u>	<u>\$ 9,740,588</u>	<u>\$ 215,962</u>
Revenues and Other Sources Over (Under) Expenditures, Operating Transfers Out, and Encumbrances	<u>\$ (1,040,302)</u>	\$ (824,341)	<u>\$ (215,962)</u>
Reconciling Items:			
Encumbrances at September 30		<u>12,983</u>	
Excess of Revenues Over (Under) Expenditures and Other Uses		\$ (811,357)	
FUND BALANCE (GAAP BASIS)			
Beginning balance		<u>12,989,614</u>	
Ending balance (GAAP Basis)		<u>\$12,178,256</u>	

The accompanying notes are an integral part of the financial statements.

1999		
Budget	Actual	Variance Favorable (Unfavorable)
\$8,415,370	\$ 8,415,370	\$
<u>679,812</u>	<u>679,812</u>	
<u>\$9,095,182</u>	<u>\$ 9,095,182</u>	<u>\$ 0</u>
\$8,964,133	\$ 8,904,120	\$ 60,013
	57,813	(57,813)
	2,200	(2,200)
<u>\$8,964,133</u>	<u>\$ 8,964,133</u>	<u>\$ 0</u>
<u>\$ 131,049</u>	\$ 131,049	<u>\$ 0</u>
	\$ 131,049	
	<u>12,858,565</u>	
	<u>\$12,989,614</u>	

Notes to the Financial Statements

Note 1 Significant Accounting Policies

a. Reporting Entity

The accompanying financial statements report the financial position and results of operations of the State Construction Code Fund, Department of Consumer and Industry Services, as of and for the fiscal years ended September 30, 2000 and September 30, 1999. This Fund is part of the State of Michigan's reporting entity and is reported as a special revenue fund in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*.

The notes accompanying these financial statements relate directly to the State Construction Code Fund. The *SOMCAFR* provides more extensive general disclosures regarding the State's Summary of Significant Accounting Policies, Budgeting and Budgetary Control, Treasurer's Common Cash, Pension Benefits and Other Postemployment Benefits, Compensated Absences, and Contingencies and Commitments.

b. Basis of Accounting and Presentation

The financial statements contained in this report are prepared on the modified accrual basis of accounting. The modified accrual basis of accounting, which emphasizes the measurement of current financial resource flows, is explained in more detail in the *SOMCAFR*.

The accompanying financial statements present only the State Construction Code Fund. Accordingly, they are not intended to present fairly the financial position and results of operations of the State of Michigan or its special revenue funds.

Note 2 Deposits

All available funds are invested in the State Treasurer's Common Cash. Interest is paid quarterly on the average amount invested in the previous quarter. There are no withdrawal restrictions on funds invested in the State Treasurer's Common Cash. The deposits are insured or collateralized (Governmental Accounting Standards Board (GASB) credit risk category 1).

Note 3 Statement of Revenues, Expenditures, Operating Transfers, and Changes in Fund Balance - Budget and Actual

This statement presents comparisons of updated budget and actual amounts.

Accounting principles generally accepted in the United States of America require that the final legal budget be reflected in the "budget" column; therefore, the updated revenue estimates as of November 30, rather than the amounts shown in the original budget, are reported. The November 30 date is used because Act 431, P.A. 1984, permits budget adjustments by the Legislature through 60 days after year-end.

The expenditures budget column represents original and supplemental authorizations (i.e., appropriations and carry-forwards) as adjusted for carry-backs (i.e., current year appropriations for prior year overdrafts), approved transfers, executive order reductions, restricted revenue adjustments, prior year carry-forward corrections, and timing differences. "Favorable variances" generally reflect unused restricted revenue authority which carries over as a reservation of fund balance; "unfavorable variances" reflect budgetary overdrafts. If both favorable and unfavorable variances exist for a particular line, the amount shown is the net variance.

Glossary of Acronyms and Terms

DMB	Department of Management and Budget.
effectiveness	Program success in achieving mission and goals.
efficiency	Achieving the most outputs and outcomes practical for the amount of resources applied or minimizing the amount of resources required to attain a certain level of outputs or outcomes.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial schedules and/or financial statements of an audited entity are fairly presented in conformity with the disclosed basis of accounting.
GAAP	accounting principles generally accepted in the United States of America.
goals	The agency's intended outcomes or impacts for a program to accomplish its mission.
internal control	A process, effected by an entity's management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories: (1) reliability of financial reporting, (2) effectiveness and efficiency of operations, and (3) compliance with applicable laws and regulations.
material condition	A serious reportable condition that could impair the ability of management to operate a program in an effective and efficient manner and/or could adversely affect the opinion of an interested person concerning the effectiveness and efficiency of the program.

material weakness	A condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial schedules and/or financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.
Michigan Administrative Information Network (MAIN)	A fully integrated automated financial management system for the State of Michigan.
performance audit	An economy and efficiency audit or a program audit that is designed to provide an independent assessment of the performance of a governmental entity, program, activity, or function to improve public accountability and to facilitate decision making by parties responsible for overseeing or initiating corrective action.
reportable condition	A matter coming to the auditor's attention that, in the auditor's judgment, should be communicated because it represents (1) either an opportunity for improvement or a significant deficiency in management's ability to operate a program in an effective and efficient manner or (2) a significant deficiency in the design or operation of internal control that could adversely affect the entity's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial schedules and/or financial statements.
SOMCAFR	<i>State of Michigan Comprehensive Annual Financial Report.</i>
unqualified opinion	An auditor's opinion in which the auditor states, without reservation, that the financial schedules and/or financial statements are fairly presented in conformity with the disclosed basis of accounting or are fairly presented in relation to the primary financial schedules and/or statements.