

Audit Report



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Citywide Disbursements 2005

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Summary

Our audit covered the period July 1, 2004, through June 30, 2005. Total disbursements for that period were \$636,103,658, which were segregated, for purposes of our audit, into four broad categories: general disbursements, salary payments, retirement benefit payments, and energy purchases.

Generally, disbursements were proper, authorized, supported, correctly recorded, and in compliance with laws, rules, policies, and procedures. However, we did note instances where controls were not in place or operating effectively to ensure proper, timely, and efficient disbursement of City funds in accordance with City policies and procedures. Those instances, which are identified for management's review, resolution, and disposition, are as follows:

- The City's Fleet Department overpaid a vendor (\$8,781 identified to date) for fire apparatus equipment during the period June 2003 through September 2005. The overpayments occurred when the vendor used a pricing formula that was not in accordance with its contract with the City.
- Documentation was not obtained by the Fleet Department to allow a determination that amounts paid for fuel surcharges were accurate and appropriate.
- An original invoice received by the Purdom Power Plant in August 2004 was not timely forwarded to Accounts Payable. As a result, the vendor was not paid in a timely manner.
- Seven contractual payments totaling

\$12.6 million were incorrectly coded as "architect services" in the City accounting system.

Actions to address the noted instances have been identified and developed in conjunction with applicable City management. We would like to acknowledge the full and complete cooperation and support of applicable City staff during this audit.

Scope, Objectives, and Methodology

The objectives of this annual audit were to determine whether disbursements of City funds were: (1) for authorized and necessary purposes; (2) made in accordance with governing laws, rules, policies, and procedures; (3) supported by appropriate documentation; and (4) properly recorded within the City's financial records. The results of this audit are relied upon by the City's external auditors and, as a result, reduce the costs associated with the City's financial statement audit.

The scope of this audit included a review of disbursements made during the period July 1, 2004, through June 30, 2005. To address the stated objectives, we selected samples of disbursements by category and reviewed the related supporting documentation, completed analytical procedures, interviewed applicable staff, and made observations as necessary.

This audit was conducted in accordance with Generally Accepted Government Auditing Standards and the Standards for the Professional Practice of Internal Auditing, as appropriate.

Background

During the period July 1, 2004, through June 30, 2005, the City disbursed funds totaling approximately \$636 million. For purposes of this audit we classified those disbursements into four areas as shown in the following table:

Disbursement Summary		
Category	Transactions	Amount
General	22,563	\$ 285,085,342
Salary	89,375	\$ 141,014,084
Retirement	11,872	\$ 25,541,284
Energy	325	\$ 184,462,948
Totals	124,135	\$ 636,103,658

Note: Excluded from general disbursements is \$44,902,408, which represents disbursements of salary and retirement payroll withholdings/deductions to applicable entities (e.g., IRS and insurance providers). This amount was excluded to preclude counting that amount twice as it is also included in the payroll and retirement amounts above.

For each of the disbursement categories we completed analytical procedures, selected samples, and applied test criteria designed to address our stated audit objectives. An overview of the testing performed for each category and the resultant findings are noted in the following sections of this report.

General Disbursements

General disbursements include all disbursements not specifically identified as part of another category (i.e., salary, retirement, and energy). Examples of disbursements audited as part of the general disbursement category included, but were not limited to:

- payments for the acquisition of services, supplies, materials, parts, fuel, equipment, land, and postage;
- contractual payments;
- purchases of goods and services using City purchase cards;
- payments to other governmental entities (e.g., municipal utility regulatory fees and gross receipt taxes);

- disbursements under City programs (e.g., grant payments); and
- refunds, such as refunds of registration fees to individuals that signed up for but could not participate in Parks and Recreation activities.

For this category we selected 35 sample items totaling \$8,529,274. Test criteria applied to these sampled items included:

- verifying that disbursements were authorized, supported, and for reasonable purposes;
- verifying that appropriate competitive acquisition procedures were followed;
- verifying that payments were made in proper amounts and in accordance with contractual terms and conditions;
- verifying that the disbursements were properly recorded in the City's accounting records; and
- verifying that the disbursements were otherwise made in accordance with established laws, rules, policies, and procedures.

Overall, we found that general disbursements were (1) supported and for authorized and reasonable purposes, (2) made in proper amounts, (3) properly recorded, and (4) made in compliance with established laws, rules, policies, and procedures. However, certain issues were identified as described in the following paragraphs.

The City's Fleet Department overpaid a vendor (\$8,781 identified to date) for fire apparatus equipment during the period June 2003 through September 2005. The overpayments occurred when the vendor used a pricing formula that was not in accordance with its contract with the City. The contract provides that the price of accessories (i.e., loose equipment for installation on apparatus) purchased is to be based on an established percentage (10% in this instance) above dealer net. However, the vendor applied a different formula that resulted in the City being overcharged. After we identified this issue, the

vendor researched prior invoices and asserted that overcharges totaled \$8,781 over a 27-month period. We recommend that Fleet management verify the accuracy of the asserted overcharges and recover overpaid funds from the vendor. In addition, Fleet management should enhance its procedures to ensure invoiced amounts are accurate and in accordance with applicable contractual agreements.

Documentation was not obtained by the Fleet Department to allow a determination that amounts charged and paid for fuel surcharges was accurate and appropriate. The City's Fleet Department contracts with vendors to acquire fuel needed to operate various City vehicles. The pricing schedule for one such contract provides that a Department of Energy (DOE) fuel surcharge is to be applied to shipping charges. That surcharge is to be based on DOE-determined costs to the hauler. While the fuel surcharge is not a material amount of the total charge (e.g., only \$16.90 out of \$11,581.21 for the sampled acquisition), documentation should be obtained (at least on a spot basis) that allows verification that the surcharge is appropriate and accurate. To ensure that amounts paid for fuel surcharges are correct, we recommend that the Fleet Department obtain DOE-determined hauling costs and, on a spot basis, use that information to ensure fuel surcharges are correct.

An original invoice received by the Purdom Power Plant in August 2004 was not forwarded to Accounts Payable until December 2004. The untimely receipt of that original invoice by Accounts Payable resulted in the applicable vendor not being paid in a timely manner. Under current City policy and procedures, vendors should send the original invoice for goods and services directly to the City's Accounts Payable Section located in City Hall. To reduce the risk of inappropriate duplicate payment, Accounts Payable will only authorize payment upon receipt of original invoices. Accordingly, in the event that a vendor submits an original invoice directly to a City

department, that department should immediately forward the original invoice to Accounts Payable to facilitate processing and payment. One sampled disbursement represented payment to a vendor for office supplies received at the Purdom Power Plant. In this instance, the vendor sent the original invoice (for a total of \$610) to the Purdom Power Plant on August 3, 2004. Purdom staff faxed a "copy" of the original invoice to Accounts Payable in City Hall on August 11, 2004. However, Purdom staff did not forward the original invoice to Accounts Payable until December 3, 2004, after receipt of a past due notice from the vendor. Although Accounts Payable timely processed the original invoice when received from Purdom, the vendor was not paid until December 14, 2004, or 133 days after the original invoice was received by City staff at the Purdom Power Plant. We recommend that Purdom staff remind applicable vendors of the importance of submitting their original invoices directly to Accounts Payable. In addition, plant management should remind applicable Purdom staff of the importance of timely forwarding original vendor invoices to Accounts Payable when the vendors inadvertently submit those invoices to the plant.

Seven contractual payments for construction of combustion turbines at Hopkins Power Plant were incorrectly coded as "architect services" in the accounting records. Those seven payments, totaling \$12,678,589, should have been coded as "unclassified contractual services." The coding error occurred when Electric Utility staff did not specify the appropriate account codes when creating the related purchase requisition in the PeopleSoft Financials System. As a result, when invoices were processed against the resulting purchase order, the incorrect code was applied to the expenditure in the PeopleSoft Financials System (i.e., instead of the desired code a default code was applied). Charging disbursements to incorrect accounting codes may result in management relying on

inaccurate information when monitoring and reviewing budgeted funds and disbursement activity. We recommend that these coding errors be corrected. In addition, management should emphasize to applicable staff the importance of correctly and accurately coding disbursements.

Salary Payments

Salary disbursements represent payments to individuals for services performed as employees of the City. As of June 30, 2005, there were 2,799 full-time City employees working in authorized positions. In addition, the City employs individuals in temporary positions. The number of temporary employees varies. During the period July 1, 2004, through June 30, 2005, the City employed and paid 1,081 temporary employees.

We selected and tested a sample of 20 salary disbursements totaling \$29,958. These 20 disbursements pertained to 20 employees, of whom 18 were in full-time positions, and two were classified as temporary employees. Audit criteria applied to the salary disbursements included, but was not limited to:

- verifying that the employees existed and were employed during the sampled pay periods;
- verifying that the employees' gross and net pay were properly authorized, calculated, and supported by appropriate leave and attendance records;
- verifying that payroll deductions were proper and supported by appropriate employee authorizations where applicable; and
- verifying that the disbursements were properly recorded in the financial records.

Overall, we found that the disbursements (1) were made to employees that existed and that were employed during the sampled pay periods, (2) were made in the proper amounts, (3) were authorized and supported by adequate documentation, and (4) were

properly recorded in the financial records. No reportable issues were identified.

Retirement Benefit Payments

Retirement benefit payments represent pension disbursements to retired employees and their designated beneficiaries/annuitants. This category also includes disability and pre-retirement benefits, which are paid to disabled employees or to employees' designated beneficiaries in the event an employee is disabled or dies while employed with the City. In addition, refunds of pension contributions to terminating employees are included in the category.

For the retirement disbursements category, we selected and tested pension disbursements pertaining to 14 individuals during the period July 1, 2004, through June 30, 2005. The tested payments totaled \$326,765 and were comprised of:

- payments from the City's defined benefit pension plan, totaling \$24,980, to two individuals that retired during the audit period;
- payments from the City's defined contribution plan, totaling \$139,957 on behalf of two individuals that retired during the audit period;
- payments from the City's defined benefit pension plan, totaling \$17,815, to seven individuals that retired prior to the audit period;
- a survivor death benefit totaling \$97,031 paid to the survivor of a deceased City employee;
- a pre-retirement benefit totaling \$40,000 paid to the beneficiary of a deceased City employee; and
- a pension refund of \$6,982 paid to a terminating employee.

Test criteria typically applied to these sampled transactions included the following:

- verifying that retirees had completed the minimum years of City service required to

- be eligible for retirement benefits (defined benefit and defined contribution plans);
- verifying that the pension/benefit payments were made in proper and accurate amounts based on the former employees' years of service, salary histories, pension plan types, payment options selected by the retirees, and other factors (defined benefit plan);
 - verifying that amounts contributed to eligible retiring employees' defined contribution accounts were correct in amount and based on the proper factors (defined contribution plan);
 - verifying that cost of living adjustments were properly determined and applied to retirement benefits (defined benefit plan);
 - verifying that deductions from retirees' pension payments were authorized and proper (defined benefit plan); and
 - verifying that benefit payments were made only to the eligible retirees/disabled employees or their designated beneficiaries/annuitants (defined benefit and defined contribution plans).

Overall, we found that procedures and controls were adequate to ensure that retirement payments and contributions were made only to eligible individuals and in proper amounts. No reportable issues were identified.

Energy Purchases

The City purchases both: (1) natural gas and other source fuels to generate power internally and to supply customers and (2) externally-generated power. The purchases of natural gas and source fuels are made by Energy Services staff located in the Gemini Building. The purchases of generated power are made by staff located in the Gemini Building (purchases for a day or more) and Electric Operations staff at the electric system control center on Van Buren Street (hourly purchases).

Purchases of natural gas and other source fuels by staff at the Gemini Building are done both through long-term contracts and short-

term agreements with energy companies/suppliers. The long-term contracts are for multiple years and require the purchase of minimum/maximum volumes of source fuel at contractually established prices. In addition, some of the long-term contracts are hedged through the financial markets to mitigate the risk due to fluctuations in gas prices. The short-term agreements range from daily to monthly deals. For those deals City staff negotiates and "shops" the open market to obtain the best prices for the City.

Purchases of generated power are made when the City's demand exceeds what is being produced at the City's power plants and/or when available information shows that generated power can be purchased from an external source cheaper than being generated by the City. Purchases of generated power are generally made from other utilities and independent power producers or through contracted power brokers.

In connection with our audit, we selected a sample of five energy purchases totaling \$2,865,346. Test criteria applied to these sampled transactions included the following:

- verifying that prices paid were in accordance with contractual and other governing terms and conditions;
- verifying that controls existed to ensure that quantities purchased were received;
- verifying that payments were timely; and
- verifying that the purchases were adequately supported and properly recorded in the City's financial records.

Our tests showed that controls were adequate to ensure that disbursements for energy were appropriate. No reportable issues were identified.

Conclusions

It is our opinion that, overall, City disbursements during the period July 1, 2004, through June 30, 2005, were (1) for authorized and necessary purposes; (2) made in accordance with established laws, rules,

policies, and procedures; (3) supported by appropriate documentation; and (4) properly recorded in the City's financial records. Given the complexities and diversity of City business, we commend City staff for their efforts in ensuring that disbursements of City funds were proper.

There are areas where improvements should be made to ensure City funds are (1) properly and timely expended in accordance with governing laws, rules, contractual terms, policies, and procedures, and (2) properly coded. We recommend that management review each issue in this report and take appropriate corrective action. The corrective action should be based on whether the issue is (1) a violation of an established internal control system or (2) an instance that identifies a weakness where a control system should be established. The anticipated benefits of each corrective action should exceed the related costs of control. A conscious involvement by City management in making those determinations and implementing improvements will help the City realize the intended benefits. We would like to acknowledge the full and complete cooperation and support of applicable City staff during this audit.

Response from Appointed Officials

City Manager:

I was pleased to see there were only minor issues reported in the 2005 Cash Disbursements Audit. Staff has established action steps to resolve these concerns in a very timely manner. I appreciate staff's diligence in completing these steps.

Also, I would like to thank the City Auditor's staff for their recommendations. This is a very comprehensive audit that is done annually, and it ensures that we have the necessary internal controls in place to maintain our fiduciary responsibilities. I appreciate the audit staff's professionalism and expertise

City Treasurer-Clerk:

We are very pleased that the audit found that the Treasurer/Clerk's Retirement Division had procedures and controls in place to ensure that retirement payments and contributions were made only to eligible individuals, in proper amounts and that the audit did not identify any reportable issues. It is always a pleasure to work with the Office of the City Auditor's staff and we appreciate the time that was taken to review our disbursement function.

Appendix A - Action Plan

Action Steps	Responsible Employee	Target Date
A. Objective: To ensure that disbursements are made in accordance with governing laws, rules, policies, and procedures.		
Fleet		
1. Staff will determine and/or verify the accuracy of amounts owed by the applicable vendor for overcharges on apparatus equipment, and recover those amounts from the vendor.	Terry Lowe	3/1/2006
2. Staff performing reviews of vendor invoices will be provided the necessary training on each vendor's contract pricing terms and/or schedule to ensure that vendor billings are in compliance with the applicable contracts.	Terry Lowe	3/1/2006
3. DOE-determined hauling costs will be identified and used, at least on a spot basis, to verify the accuracy and propriety of fuel surcharges. Documentation (e.g., DOE records showing hauling costs) will be obtained/retained as evidence of those efforts.	Terry Lowe	3/1/2006
Electric Utility – Purdom Power Plant		
4. Staff will be reminded of the importance of forwarding original vendor invoices to Accounts Payable in a timely manner to ensure prompt vendor payment. In addition, applicable vendors will be reminded that original invoices should be submitted directly to Accounts Payable in City Hall.	Diane Blanton	2/9/2006
B. To ensure that disbursements are properly recorded within the City's financial records.		
Electric Utility - Production Management		
1. The noted coding errors will be corrected and staff will be reminded of the importance of correctly coding disbursements/expenditures.	Diane Blanton	2/9/2006

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