



City of Houston

Annise D. Parker
City Controller

City-Wide Accounts Receivable and Billings Internal Audit

Building Services Department

Report No. 04-32



OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS

ANNISE D. PARKER

October 25, 2004

The Honorable Bill White, Mayor
City of Houston, Texas

SUBJECT: City-Wide Accounts Receivable and Billings Internal Audit
Building Services Department (Report No. 04-32)

Dear Mayor White:

In accordance with the City's contract with Jefferson Wells International (JWI), JWI has completed an Accounts Receivable and Billings Internal Audit pertaining to the Building Services Department (Department). The purpose of the audit was to assist management with an assessment of the adequacy and effectiveness of the internal controls and reporting related to the City's accounts receivable and billing processes. Additionally, the audit determined if the Department has developed and implemented written accounts receivable policies and procedures which address the requirements of Executive Order No. 1-38 (Accounts Receivable Policy).

The report, attached for your review, noted that the Department does not account for receivables within the City's financial system. Various recommendations were made to improve the Department's controls over the accounting and reporting of receivables. Draft copies of the matters contained in the report were provided to Department officials. The views of the responsible officials as to actions being taken are appended to the report as Exhibit A.

We commend the Department for taking immediate steps to implement the recommendations. Also, we appreciate the cooperation extended to the JWI auditors by Department personnel during the course of the engagement.

Respectfully submitted,

Annise D. Parker
City Controller

xc: City Council Members
Anthony Hall, Chief Administrative Officer
Michael Moore, Chief of Staff, Mayor's Office
Issa Dadoush, P.E., Director, Building Services Department
Judy Gray Johnson, Director, Finance and Administration Department

October 4, 2004

Ms. Anise Parker
City Controller
City of Houston
901 Bagby, 8th Floor
Houston, TX 77002


Dear Controller Parker:

We have completed the internal audit of the Accounts Receivable and Billings for the Building Services Department (Department) as outlined in our engagement letter dated October 10, 2003, under Contract No. 51783. This report documents our final report for the Department. A report summarizing significant issues identified across the departments will be issued at the conclusion of the City-wide engagement when the internal audit procedures have been completed for all departments.

Our observations and recommendations noted during the performance of the procedures are presented in this report and views of responsible officials are attached as Exhibit A. Our procedures, which accomplished the project objectives, were performed through January 15, 2004 and have not been updated since that date. Our observations included in this report are the only matters that came to our attention, based on the procedures performed.

Jefferson Wells International is pleased to have assisted the City Controller and the Department, and we appreciate the cooperation received during this engagement from the City Controller's Office and the Department.

This report is intended solely for the information and use of the City, the Department and the City Controller's Office, and is not intended to be used for any other purpose.





Project Scope & Objectives

Scope:

This internal audit was performed to assist City management with an assessment of the adequacy and effectiveness of the internal controls and reporting related to the City's accounts receivable and billing processes. The scope of this report is the revenues and receivables managed by the Building Services Department.

Objectives:

- Determine whether all receivables managed by the Department are recorded in the City's financial records.
- Determine whether there are receivables that are not recorded in the City's books.
- Review and evaluate the type of records that are maintained to support the receivables.
- Determine what steps, if any, are being performed to collect the outstanding receivables.
- Determine whether billing systems are in place to bill timely those persons/entities that may owe the City monies.
- Determine whether the Department has developed and implemented written accounts receivable policies and procedures, which address the requirements of Executive Order No. 1-38 (Account Receivable Policy).



Procedures Performed

- Requested and gathered pertinent documents related to the Department's revenue sources, including written accounts receivable procedures applicable to each of its sources of revenue.
- Compiled a preliminary list of revenue sources for the Department.
- Identified and scheduled interviews with key financial personnel for the Department.
- Interviewed key Departmental personnel and obtained an understanding of the Department's process, as applicable, related to:
 - Capturing each transaction that results in a source of revenue/receivable;
 - Timing of revenue/receivable recognition;
 - All applicable accounting entries;
 - Billing systems for monies owed the City; and
 - Monitoring and collection of accounts receivable, including supporting documentation.
- As applicable, for each of the Department's revenue/receivable source that involves the generation of a bill for monies owed the City:
 - Traced each receivable source to the City's financial system;
 - Determined whether the applicable billing system had been designed to mitigate the risk of bills not being generated on a timely basis; and
 - Determined whether the described billing system is in-place and operating effectively.



Procedures Performed (continued)

- As applicable, reviewed the Department's written policies and procedures and determined compliance with Executive Order No. 1-38, Accounts Receivable Policy, specific to:
 - Appropriate Authorization;
 - Cost Recovery;
 - Transaction Processing;
 - Physical Safeguards;
 - Substantiation and Evaluation;
 - Determination of net realizable value;
 - Identification of accounts to be recommended to the Mayor and City Council for write-off approval;
 - Determination of appropriate allowance for doubtful accounts;
 - Preparation of accounts receivable aging analysis, aged cash receipts, and cash collections percentage reports; and
 - The use of the reports mentioned above to evaluate collectibility, target accounts requiring more aggressive collection efforts, and target accounts that yield better collections results.



Revenues & Receivables Overview

Background

- Building Services Department has the following revenue streams within the General Fund. Two are inter-fund, which are outside the scope of this internal audit and the remaining are:
 - ***Vending Machine Concession*** - a contractual revenue arrangement with the vending machine company to pay the greater of a monthly minimum or a percentage of the machines' monthly Net Sales.
 - ***Building Space Rental*** - consisting of lease payments from two restaurants leasing space in City buildings.
 - ***Facility Rental*** - consists of lease revenue from one of the City's parking lots, which pursuant to the contract is payable monthly.
 - ***Miscellaneous Fees*** – various charges for copies, which are collected as earned.
- The Department also handles refunds and recoveries associated with certain construction projects.

Summary

- The Department does not account for receivables within the City's financial system.
- The Department's accounting process for recognizing and collecting receivables enables substantiation and reconciliation of billed and collected amounts.
- Accounting and reporting of receivables with corresponding allowance accounts or deferred revenue could improve the City's monitoring controls over the Department's receivables.



Revenues & Receivables Overview

	<u>2004 Annual Budget</u>	<u>Receivables are Generated</u>	<u>Receivables are Recorded</u>	<u>Accounting is in Accordance with GAAP</u>
Building Services:				
Vending Machine Concession	\$ 34,600	X		X
Building Space Rental	107,000	X	no	X
Facility Rental	47,800	X	no	X
Recoveries and Refunds - CIP	2,122,000	X		X
Miscellaneous Fees	Not budgeted	n/a	n/a	X
Inter-fund Electric Maintenance	651,000	*	*	*
Inter-fund Engineering Services	1,422,000	*	*	*

Definition of Terms:

- **X** – Represents a Yes answer related to determining if each identified revenue stream results in a receivable.
- ***** – This revenue is out-of-scope of this internal audit.
- – Receivable is not recorded due to the final amount not being determinable until received.
- **Receivables** – The asset that results when revenue has been earned but no payment is made at the point the service or good is provided (normally the result of a bill being generated).



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Appropriate Authorization	<ul style="list-style-type: none"> ▪ The City has established all fees charged by the Department through City Ordinances and/or approving contracts with the customer. ▪ Responsibilities and authorizations for the recording of revenues is defined, communicated and understood. ▪ The Department does not have formal policies and procedures as required by the EO. 	<ul style="list-style-type: none"> ▪ Recommend, for improved controls and long-term consistency of established procedures, that formal policies and procedures be developed as required by the Executive Order. 	Moderate
Cost Recovery	<ul style="list-style-type: none"> ▪ The Department seeks to establish rental rates that at a minimum recover costs. Other cost recovery efforts are made with regard to the construction program 	<ul style="list-style-type: none"> ▪ None noted. 	Low
Transaction Processing	<ul style="list-style-type: none"> ▪ Since most revenues are contractual, most are determined and recorded as the payment is received. ▪ Revenues are recorded directly to the general ledger as received and reviewed for reasonableness. 	<ul style="list-style-type: none"> ▪ No receivables are recorded when the rents or amounts are due based on the various contracts. ▪ There are past due vending concession receivables which are not included in the City's financial system. Contractually this revenue is the minimum of \$2,400 monthly or 6% of net sales. ▪ Recommend that receivables be recorded as revenues become due. 	Moderate



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Physical Safeguards	<ul style="list-style-type: none"> ▪ Revenue is received in check form. ▪ Management, who stays informed regarding revenue variances, reviews financial reports monthly. ▪ Check receipt deposit processing and revenue entry activities have segregation of duties. 	<ul style="list-style-type: none"> ▪ Reviews of the receivable status is not documented. 	Moderate
Substantiation and Evaluation	<ul style="list-style-type: none"> ▪ Receivables are substantiated with executed contracts. ▪ Each contract enables the City to conduct audits regarding compliance with the contract. 	<ul style="list-style-type: none"> ▪ None noted. 	Low
Determination of Net Realizable Value <i>(Minimum of Annually)</i>	<ul style="list-style-type: none"> ▪ Validation of realizable value is determined as payments are received. ▪ Management reviews monthly financial reports. 	<ul style="list-style-type: none"> ▪ None noted. 	Low
Identification of Accounts to be Written-off / Determination of an Appropriate Allowance for Doubtful Accounts <i>(Minimum Annually)</i>	<ul style="list-style-type: none"> ▪ There have been no write-offs and none are expected. If there were a collectibility issue, the Department would involve the Legal Department. ▪ Since receivables are not recorded, no allowance for doubtful accounts would be needed. 	<ul style="list-style-type: none"> ▪ Receivables and allowances are not recorded creating the risk that management may not be aware of collection issues. 	Moderate



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Preparation of Reports & Analysis	<ul style="list-style-type: none">Management reviews monthly financial reports.	<ul style="list-style-type: none">At a minimum of monthly, management should be made aware of uncollected revenues and steps take to collect past due receivables. This reporting should be documented for control purposes.	Moderate
Use of Reports to Evaluate and Improve Collections	<ul style="list-style-type: none">Management reviews monthly financial reports.	<ul style="list-style-type: none">See recommendation regarding preparation of reports above.	Moderate

EXHIBIT A



CITY OF HOUSTON

Building Services Department

Interoffice

Correspondence

A handwritten signature in black ink, appearing to read "Issa Z. Dadoush".

To: Annise D. Parker, City Controller
City Controller's Office

From: Issa Z. Dadoush, P. E.
Director

Date: October 6, 2004

Subject: City-Wide Accounts Receivable and
Billings Internal Audit
Report No. 04-TBD

This memorandum responds to the audit findings and recommendations based on the internal audit of the Accounts Receivable and Billings for the Building Services Department.

1. APPROPRIATE AUTHORIZATION

- Since its creation, the department has complied with the citywide Accounts Receivable Policy, Executive Order No. 1-38 as well as adheres to directives given by the Finance and Administration Department.
- To improve controls and long-term consistency, Building Services has established informal guidelines and procedures to track and monitor monthly revenues to ensure receivables are recorded each month. As recommended, the department will formalize policies and procedures as required by the Executive Order within the next 60 days.

2. TRANSACTION PROCESSING

- As noted above, Building Services will establish written policies and procedures to address the proper handling of recording receivables and ensure that receivables be recorded as revenues become due.

3. PHYSICAL SAFEGUARDS

- The department will incorporate the documentation of the review process as part of its policies and procedures.

4. IDENTIFICATION OF ACCOUNTS TO BE WRITTEN-OFF/ DETERMINATION OF AN APPROPRIATE ALLOWANCE FOR DOUBTFUL ACCOUNTS

- Although receivables and allowances are not recorded, management is informed of collection issues as indicated in the Monthly Financial and Operating Report submitted to the Finance and Administration Department.

*Views of Responsible
Officials*

EXHIBIT A

Memorandum – City-Wide Accounts Receivable and Billings Internal Audit
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5. PREPARATION OF REPORTS & ANALYSIS/ USE OF REPORTS TO EVALUATE AND IMPROVE COLLECTIONS

- Building Services will report any uncollected revenues and past due receivables in its submission of the Monthly Financial and Operation Report to management.

If you have any questions, please call me directly at (713) 247-2157.

Attachments

IZD:JS:js

cc: Steve Schoonover, City Auditor, City Controller's Office

*Views of Responsible
Officials*