



City of Houston

Annise D. Parker
City Controller

City-Wide Accounts Receivable and Billings Internal Audit

Finance and Administration Department

Report No. 04-41



OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS

ANNISE D. PARKER

December 2, 2004

The Honorable Bill White, Mayor
City of Houston, Texas

SUBJECT: City-Wide Accounts Receivable and Billings Internal Audit
Finance and Administration Department (Report No. 04-41)

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 Finance and Administration 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, did not note any high-risk issues and stated that the City's financial system includes accounting for the general government taxes, licenses, fees and assessments. Draft copies of the matters contained in the report were provided to Department officials. The views of the responsible officials 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
Judy Gray Johnson, Director, Finance and Administration Department

September 13, 2004

Ms. Annise D. 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 Finance and Administration 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 City 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 the March 23, 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 we appreciate the cooperation received during this engagement from the Finance and Administration Department as well as your office.

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 Finance and Administration 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

- ✦ The Finance and Administration Department (F&A) collects or monitors the collection and accounting of various general government tax revenues, business licenses, franchise fees, grants, and property liens and assessments. Substantially all revenues are collectible pursuant to a state law or local ordinance.
- ✦ Revenues consist of the following:
 - ✦ **General Government Tax Revenues** – property, sales, franchise, mixed beverage, and bingo taxes
 - ✦ **Business Licenses** – taxicab, alcohol beverage, dance, occupational, and school bus licenses.
 - ✦ **Franchise Fees** – utility franchises regulated by ordinance or state statute
 - ✦ **Grant Revenues** – community development reimbursement-based grants
 - ✦ **Property Liens and assessments** – street and bridge, demolition, weed cutting, industrial assessments
- ✦ F&A collects or monitors the collection of certain revenues generated by other departments, including emergency medical services provided by the Fire Department and Hotel Occupancy Tax revenue generated for the Convention and Entertainment Facilities Department.
- ✦ In addition, the Department serves as the City-wide initial control for returned checks with insufficient funds.
- ✦ Other inter-fund recoveries for indirect costs, other reimbursements, and the allocation of investment earnings are outside the scope of this internal audit.

Summary

- ✦ The City's financial system includes accounting for the general government taxes, licenses, fees and assessments.
- ✦ Grant receivables are not recorded on a cash basis within the City's financial system until received.



Revenues & Receivables Overview

	<u>2004 Annual Budget</u>	<u>Are Receivables Generated</u>	<u>Are Receivables Recorded</u>	<u>Recording is in Accordance with GAAP</u>
Revenues:				
✍ Property taxes	\$660,000,000	X	X	X
✍ Sales taxes	330,000,000	X	X	X
✍ Other taxes	40,400,000	X	X	X
✍ Licenses and permits	2,320,000	no	n/a	X
✍ Franchise fees	156,200,000	X	X	X
✍ Liens and assessments	2,630,000	X	X	X
✍ Grants	980,000	X	no	no
✍ Miscellaneous other	3,000,000	no	n/a	X

Definition of Terms:

- ✍ **X** – Represents a Yes answer related to determining if each identified revenue stream results in a receivable.
- ✍ **Receivables** – The resulting asset 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 revenue / receivables is defined, communicated and understood. ✍️ The Department does not have formal policies and procedures as required by the Executive Order (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 EO. ✍️ F&A should follow-up to ensure required departments submit formal policies and procedures for F&A's approval. 	Moderate
Cost Recovery	<ul style="list-style-type: none"> ✍️ The Department has cost recovery grants, and as such, generates a receivable as reimbursable grant expenditures are incurred. Grant receivables are recorded as amounts are requested for reimbursement. ✍️ The Department's revenue is received in a number of checks from individuals and businesses, which results in checks being returned due to insufficient funds (NSF). Finance and Administration receives the checks, records the receivable and then returns them to the Department for recovery. ✍️ NSF receivables are tracked in detail and in total through a general ledger control account. F&A has collection procedures to collect its amounts but does not monitor other Departments for timely collection efforts. 	<ul style="list-style-type: none"> ✍️ The Department or City could consider the use of an outside collection agent for long outstanding NSF checks. 	Moderate



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Transaction Processing	<p>Managed Revenues:</p> <ul style="list-style-type: none"> ☞ Outside parties are under an agreement to bill, collect and remit revenue to the City. ☞ Revenue is recorded as the tax liability attaches or as service is provided. ☞ Collections are recorded against the receivables as payments are received. <p>State Collected Revenues</p> <ul style="list-style-type: none"> ☞ State laws establish the rates, reporting and remission frequency and process. ☞ Taxpayers report & remit revenue to the State. ☞ Revenue is estimated by the City based on historical trends with accruals recorded for large revenue amounts such as sales tax. ☞ The State remits the City its portion, which is recorded against the accrued estimate and the difference reconciled and recorded. <p>Direct Collections</p> <ul style="list-style-type: none"> ☞ Revenue is recorded as provided for in the ordinance or contract with uncollected amounts accrued monthly. ☞ Payors remit to the City amounts due, which are recorded against the receivable with any differences reconciled and recorded. <p>Grant Revenues - Schedules and financial reports from the accounting system are used and maintained for grant reimbursable costs. Monthly a report is submitted to Housing for submission of the reimbursement request.</p>	<p>☞ To improve controls over grant receivables, we recommend a receivable be recorded as a reimbursement request is submitted. Collection of an amount other than the receivable could then enable a timely reconciliation /follow-up.</p>	Moderate



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Physical Safeguards	<ul style="list-style-type: none"> ☑ The Department has procedures over the handling and deposit of cash receipts. ☑ The Department uses lockbox services or outside parties to collect receivables or amounts to minimize cash handling. ☑ Tax revenues – either collected by Harris County or the State are wired into the City’s accounts resulting in no cash handling. ☑ Receivable balances are reconciled monthly. 	☑ None noted.	Low
Substantiation and Evaluation	<ul style="list-style-type: none"> ☑ Certain billing and collection services are provided pursuant to an executed contract that states the City has the right to audit their services. ☑ Collection rates and receivable reconciliations are prepared and reviewed monthly ☑ Other revenues are reviewed and analyzed on a trend basis and in comparison to an annual budget. 	☑ None noted.	Low



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Determination of Net Realizable Value <i>(Minimum of Annually)</i>	<p>Realizable value is determined only as revenues are collected and recorded, except for NSF receivables, which are reviewed at least annually.</p> <p>The Department pursues collection on past-due accounts and checks that have been returned due to insufficient funds.</p>	<p>The Department could consider deploying additional collection efforts on these receivables, including the use of an independent collection agent.</p>	Moderate
Identification of Accounts to be Written-off / Determination of an Appropriate Allowance for Doubtful Accounts <i>(Minimum Annually)</i>	<p>See determination of realizable value.</p>	<p>None noted.</p>	Low
Preparation of Reports & Analysis	<p>Monthly reports are routinely prepared by the Department to monitor receivables and revenue completeness as well as trends.</p> <p>All reports are reconciled to the general ledger as appropriate and reviewed by the Department's management.</p>	<p>None noted.</p>	Low



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Use of Reports to Evaluate and Improve Collections	As noted above, collection efforts are made on NSF receivables supported by use of available reports.	None noted.	Low

EXHIBIT A



CITY OF HOUSTON

Finance & Administration
Department

Interoffice

Correspondence

To: Annise D. Parker
City Controller

From: Judy Gray Johnson, Director

Date: November 8, 2004

Subject: **City-Wide Accounts Receivable and
Billings Internal Audit - F&A Dept.
Response**

The Finance & Administration Department has received the draft copy of the City-Wide Accounts Receivable and Billings Internal Audit Report regarding the department's accounts receivable and billing processes.

F&A offers responses to the following areas:

1. "The Department does not have formal policies and procedures as required by the Executive Order".
 - Response: F&A does have written procedures for the major areas of its receivables, including 1) Property Taxes, 2) Hotel Taxes, 3) Industrial District Assessments, and 4) Ambulance fees. Additional associated procedures are contained within various contracts relating to 1) Current and Delinquent Property Tax collections, 2) Industrial District Assessment collections, and 3) Ambulance fee collections.
2. "F&A should follow-up to ensure departments submit formal policies and procedures for F&A's approval".
 - Response: Agreed, section 3.3 of the EO states that departments should submit their policies and procedures to F&A for approval. F&A will follow up with all departments to ensure this process is completed.
3. "The Department or City could consider the use of an outside collection agent for long outstanding NSF checks".
 - Response: F&A will review the cost-benefits of an RFP for City-wide NSF check collection efforts.

*Views of Responsible
Officials*

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EXHIBIT A

Page 2

4. "To improve controls over grant receivables, we recommend a receivable be recorded as a reimbursement request is submitted. Collection of an amount other than the receivable could then enable a timely reconciliation/follow -up.

- Response: Agreed, F&A will revise the current grant accounting procedures to adopt this recommendation.

Thank you and please feel free to call if there are any questions.


Judy Gray Johnson, Director

CC: Gary E. Gray, Assistant Director

*Views of Responsible
Officials*

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