



City of Houston

Annise D. Parker
City Controller

City-Wide Accounts Receivable and Billings Internal Audit

Fire Department

Report No. 04-43



OFFICE OF THE CITY CONTROLLER
CITY OF HOUSTON
TEXAS

ANNISE D. PARKER

December 9, 2004

The Honorable Bill White, Mayor
City of Houston, Texas

SUBJECT: City-Wide Accounts Receivable and Billings Internal Audit
Fire Department (Report No. 04-43)

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 Fire 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 City's financial system includes accrual accounting for the Department's significant receivables. Also, the Department would benefit from enhanced technology to monitor, record, assess and report non-EMS receivables. 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
Phil Boriskie, Fire Chief
Judy Gray Johnson, Director, Finance and Administration Department

October 15, 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 Fire 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 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 we appreciate the cooperation received during this engagement from the Fire 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 Fire 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 Fire Department generally provides its services from general tax revenues. However, the Department generates revenue arising from the following revenue streams:
 - ✦ **Protective Fire Services** – Charges for Fire services to other City operations or services provided outside of city limits;
 - ✦ **Fire Permits** – Revenue pursuant to fire alarm permits, fire inspections and special fire permits;
 - ✦ **Hazardous Material Response** – Voluntary annual fees for companies participating in the HazMat program to provide for incident response services and hourly fees for response services for non participating companies.
 - ✦ **Recoveries and Refunds/Standby Fire Watch** – Service fees for standby fire watch services at special events.
 - ✦ **Facility Rental** - Houston Community College pays a facility use fee per student for the Department's training facility.
- ✦ Further, significant revenues related to the Department's operations, such as emergency medical services (EMS or ambulance) is recorded and monitored by the Finance and Administration (F&A) Department. Receivables related to these revenues were included in F&A's report.
- ✦ Grant revenues from the Federal Emergency Management Agency (FEMA) for the reimbursement of allowable costs are monitored and recognized as revenue by Department, but all reimbursement submissions and receivable monitoring is done by the City's Department of Public Safety.

Summary

- ✦ The City's financial system includes accrual accounting for the Department's significant receivables.
- ✦ The Department has some revenue streams which can occasionally generate receivables related to Standby Fire Watch and HazMat response and remediation services. If receivables arise they are not recorded as billed or earned, but rather when received.
- ✦ The Department would benefit from enhanced technology to monitor, record, assess and report non-EMS 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>
Revenue Streams:				
✎ Emergency Medical Services	\$ 22,100,000	X	X	X
✎ Protective Fire Services	11,398,500	no	n/a	X
✎ Fire Permits	2,800,000	no	n/a	X
✎ Hazardous Material Response	180,500	†	no	no
✎ Stand-by Fire Watch Services	1,200,000	†	no	no
✎ Facility Rental	226,500	no	no	X
✎ Miscellaneous Fees	88,400	no	n/a	X

Definition of Terms:

- ✎ **X** – Represents a Yes answer related to determining if each identified revenue stream results in a receivable.
- ✎ **†** – Timing of events could cause an occasional receivable; however, substantially all revenue is collected as earned.
- ✎ **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 non-interfund service fees charged by the Department through City Ordinances. ✓ Interfund service revenues are supported by an approved cost allocation plan. ✓ Responsibilities and authorizations for the recording of receivables is defined, communicated and understood. ✓ The Department has not finalized its formal policies and procedures as required by the Executive Order. 	<ul style="list-style-type: none"> ✗ Recommend, for improved controls and long-term consistency of established procedures, that the formal policies and procedures be finalized as required by the Executive Order. 	Low
Cost Recovery	<ul style="list-style-type: none"> ✓ The Department establishes fees to provide recovery costs related to those services. 	<ul style="list-style-type: none"> ✗ None noted. 	None



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Transaction Processing	<ul style="list-style-type: none"> Billings and collections for the Department's services generating EMS receivables are outsourced and managed by F&A. All non-EMS revenues are recognized as received with outstanding amounts tracked through various Excel spreadsheets. Reimbursable costs through FEMA grants are tracked on a schedule and forwarded to the Mayor's Office monthly for submission to FEMA. Payments are received via wire transfer. The recording of the wire transfer triggers recording of the grant revenue. Revenue trends and transactions are monitored through a review of recorded amounts within the City's financial system. 	<ul style="list-style-type: none"> Although the Department's receivables are insignificant, controls over receivables could be enhanced if receivables were recorded in the City's financial system. The Department would benefit from enhanced system capability for the maintenance of detail subsidiary ledgers, generation of aging and monitoring reports, integration with the City's financial system and application controls over receivable adjustments. 	Low
Physical Safeguards	<ul style="list-style-type: none"> The Department has segregation of duties through the use of F&A related to billing and collection of EMS receivables. Revenues such as Stand-by Fire Watch and facility rental amounts are tracked in detail using Excel worksheets, generally collected in advance and reconciled with enrollment and activity reports. 	<ul style="list-style-type: none"> HazMat revenue and receivables are handled solely by that division. As such, controls over revenue and receivable tracking are needed to mitigate the risk of theft or misappropriation. Further, segregation of duties between service provision and receivable / cash handling should be implemented. See also recommendations above. 	Moderate



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Substantiation and Evaluation	<p>See the controls and issues noted under transaction processing above. Further, based on a review of one month's activity – detail support exists for all receivables.</p>	<p>See recommendations noted under transaction processing related to maintaining general ledger control accounts.</p>	Low
Determination of Net Realizable Value <i>(Minimum of Annually)</i>	<p>Validation of realizable value is determined only as receivables are collected and revenue recorded. As such, all recorded receivables are reserved until the amount is realized. As such, no determination is made on unrecorded receivables.</p> <p>The Department pursues collection on past-due accounts.</p>	<p>Periodically receivables should be assessed as to their realizable value. This assessment should serve to prioritize collection efforts and on-going fees, late payment penalties, etc. Such assessment should specifically be made for insufficient fund receivables.</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 – procedures do not include an estimation of allowances for doubtful accounts since accounts are fully reserved and revenue is recognized as receivables are collected.</p>	<p>Old uncollectible accounts (NSF and EMS receivables) continue to be carried on the City's financial statements, which do not provide management with a realistic measure of current outstanding accounts or collection experience of such accounts.</p>	Moderate



Compliance Analysis Overview - EO #1-38

Compliance Area	Controls Noted	Issues Noted	Risk
Preparation of Reports & Analysis	Revenue trends are monitored using financial statement and budget to actual reports.	No formal or regular receivable monitoring reports are prepared. For each receivable type basic long overdue or larger outstanding amounts should be reported and reviewed.	Moderate
Use of Reports to Evaluate and Improve Collections	As noted above, the Department has outsourced EMS collection activities and records substantially all other revenue on a cash basis.	As recommended above, the Department would benefit from a system that could track and age report all non-EMS receivables.	Moderate

EXHIBIT A



CITY OF HOUSTON

Fire Department

Bill White

Mayor

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Houston, Texas 77251-1562

Telephone – Dial 311
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November 2, 2004

Annise D. Parker
City Controller
611 Walker
Houston, Texas 77002

Subject: City-Wide Accounts Receivable and Billings Internal Audit

Dear Ms. Parker:

Please find below our response to the final draft report of subject audit.

Issues Noted **Recommend that the formal policies and procedures be finalized as required by the Executive Order.**

HFD Response:

We agree with this finding; the policies and procedures are in draft form and needs only minor revisions to be finalized.

Issues Noted **Although the Department's receivables are insignificant, controls over receivables could be enhanced if receivables were recorded in the City's financial system.**

HFD Response:

We agree that this would improve the control over our receivables. Due to the small amount of actual receivables generated by the department, it has not been a high priority to implement. We will examine the occasional receivable that is generated and begin recording them in the City's financial system.

Issues Noted **The Department would benefit from enhanced system capability for the maintenance of detail subsidiary ledgers, generation of aging and monitoring reports, integration with the City's financial system and application controls over receivable adjustments.**

The Department agrees. The current software system used by the City is inadequate in many ways and fails to provide reports and functionality that would allow the department to better manage its receivables.

*Views of Responsible
Officials*

Council Members: Toni Lawrence Carol Mims Galloway Mark Goldberg Ada Edwards Addie Wiseman M.J. Khan Pam Holm Adrian Garcia Carol Alvarado
Mark Ellis Gordon Quan Shelley Sekula-Gibbs, M.D. Ronald C. Green Michael Berry Controller: Annise D. Parker

EXHIBIT A

Response to Cash Handling Procedures Audit
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Issues Noted HazMat revenue and receivables are handled solely by that division. As such, controls over revenue and receivable tracking are needed to mitigate the risk of theft or misappropriation. Further, segregation of duties, between service provision and receivable/cash handling should be implemented.

We agree with this finding. The department will move the billing and collection function to the Finance & Administration Division of the Fire Department.

Issues Noted Periodically receivables should be assessed as to their realizable value. This assessment should serve to prioritize collection efforts and on-going fees, late payment penalties, etc. Such assessment should specifically be made for insufficient fund receivables.

The department agrees that there are receivables currently on the City's books that are unlikely to be collected. These are NSF checks that are many years old and are no longer being actively pursued. There should be an annual write-off of any items that the department believes are not collectible.

Issues Noted Old uncollectible accounts (NSF and EMS receivables) continue to be carried on the City's financial statements, which do not provide management with a realistic measure of current outstanding accounts or collection expense of such accounts.

We agree with this issue. See comments above related to this issue.

We hope that we were able to clarify the concerns expressed during this audit. Please call Gracia Rosslow at 713-247-8721 if you need additional information.

Sincerely,



Phil Boriskie
Fire Chief

cc: Gracia Rosslow – Deputy Director
Diane Alcalá – Administrative Manager, Permits

*Views of Responsible
Officials*