

**SEATTLE PUBLIC UTILITIES
REVENUE CYCLE AUDIT**

– COMMERCIAL SOLID WASTE –

Internal Controls Review

April 9, 2008

City of Seattle
Office of City Auditor

Susan Cohen, City Auditor



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City of Seattle Office of City Auditor

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City of Seattle
Office of City Auditor



Susan Cohen, City Auditor

April 9, 2008

The Honorable Greg Nickels
Seattle City Councilmembers
City of Seattle
Seattle, Washington 98104

Dear Mayor Nickels and City Councilmembers:

Attached is our report on *Seattle Public Utilities Revenue Cycle Audit – Commercial Solid Waste*. The audit's primary objectives were to determine whether internal controls surrounding the billing and collection of fees for Commercial Solid Waste services were adequate. Audit objectives also included determining the adequacy of solid waste vendor contract terms, vendor performance, and the accuracy of charges for vendor services. This report is one part of an audit of the revenue cycle of Seattle Public Utilities' (SPU) primary utility services - Drainage, Solid Waste, Water, and Wastewater. The report for the Drainage Revenue Cycle audit was issued on February 8, 2007, the Transfer Stations Revenue Cycle audit report was issued on February 14, 2008, and the reports for the remaining modules of the audit will be issued as the work is completed. We selected the SPU utility services revenue cycle for audit due to the magnitude of its revenue stream, which is over \$400 million annually.

We appreciate the excellent cooperation of SPU management and staff during the review process, and that of other City departments. SPU's response to our review is included under the 'Actions Planned' section for each issue in the report.

Sincerely,

A handwritten signature in cursive script that reads "Susan Cohen".

Susan Cohen
City Auditor

SC:rh

Attachment

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REPORT HIGHLIGHTS

Seattle Office of City Auditor – April 9, 2008

A copy of the Office of City Auditor's report regarding Seattle Public Utilities' (SPU) Commercial Solid Waste Revenue Cycle can be obtained at the Auditor's website at <http://seattle.gov/audit> or by calling (206) 233-3801. Please direct any questions or comments regarding this report, or suggestions for future audits to Susan Cohen, Seattle City Auditor, at (206) 233-3801 or susan.cohen@seattle.gov.

SEATTLE PUBLIC UTILITIES COMMERCIAL SOLID WASTE REVENUE CYCLE



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AUDIT OBJECTIVES

We evaluated internal controls over the billing and collecting of commercial solid waste services fees.

BACKGROUND

SPU provides solid waste collection, processing, and disposal services to about 9,000 commercial customers in the City. SPU outsources many of the functions associated with these services, including waste collection, some waste processing and transfer, waste transport and long-term disposal, and customer billing and administration services. In 2007, SPU received over \$42 million from commercial solid waste customer fees for these services.

AUDIT CONCLUSIONS

Overall, we found internal controls were adequate for the policies, procedures, and operations involved in billing and collecting fees for Seattle Public Utilities' (SPU) commercial solid waste services. However, we noted several significant issues. Controls relating to delinquent account collections functions need improvements so that SPU can maximize its revenue recoveries. There are also issues related to vendor services, including the need for better verification of tonnages used to calculate vendor charges, improved contractor reporting of customer complaints, and the need for SPU to assess penalty fees to contractors for service failures. We are pleased that SPU has provided 'Action Plans' to address the findings in this report, which are listed in the table at the end of this document.

Commercial Solid Waste Revenues

2002	\$36,721,223
2003	\$38,470,511
2004	\$37,725,319
2005	\$38,138,589
2006	\$38,608,478
2007	\$42,425,594

Delinquent Account Collections: Controls over the collections functions for delinquent commercial solid waste accounts need significant improvement. Delinquent accounts are not consistently sent to SPU's collection agency in a timely manner, accounts in collections are not adequately tracked and monitored, adequate support and documentation are not provided to the collection agency, and collection policies and procedures are contributing to the poor collection rate for these accounts. Customer payments made to the collection agency are not transferred to the City in a timely manner, and there are some issues related to collection fees and collection agency commission charges, including the way fees are applied to accounts and SPU's lack of validation of charged fees. In addition, customer payments made directly to the contractors are not consistently reported to SPU.

AUDIT CONCLUSIONS (Continued)

Vendor/Contractor Services: There are issues that need to be addressed related to outsourced solid waste services. Procedures were not adequate to ensure SPU was charged accurately for yard waste processing tonnage due to the truck weighing procedures at the vendor's scale house, but the vendor has since changed their procedure. Better verification is needed of tonnage numbers used to calculate charges for transfer services, yard waste processing, recycling processing, and the monthly recycling commodity credit SPU receives for recycling waste. SPU is not assessing penalty fees to the waste collection contractors for service failures, such as missed pick-ups, in accordance with contract terms, and this may be partly due to the contractors' inadequate reporting on customer calls and complaints. In addition, all of the critical scales involved in the SPU solid waste processes need to be licensed with and tested by the State of Washington Weights and Measures unit.

Other Significant Findings:

- ❖ SPU's should improve its review of contractor adjustments to customer accounts.
- ❖ A significant percentage of commercial customers consistently pay a month or more late, and this trend may be increasing. Interest fees charged to delinquent accounts do not appear to be adequate to encourage timely payment.
- ❖ Some improvements are needed with contractor and SPU customer communications related to delinquent commercial solid waste accounts.

SPU Commercial Solid Waste Revenue Cycle - Risk Matrix

Green: Low risk – Internal controls appear to be adequate

Yellow: Medium risk – It would be ideal to strengthen internal controls

Red: High risk – Internal controls should be strengthened as soon as possible

Scope Area and Issues	Risk Level
Rates and Service Usage	Green
Billing and Account Adjustments	Yellow
Payment Processing and Remittance of Payments	Green
Accounts Receivable Management	Yellow
Collections, Dishonored Items, and Write-Offs	Red
Fund Accounting – Revenues and Receivables	Yellow
Information Technology	Green
Vendor Billing, Contracts, and Performance	Yellow



Photo from Seattle Municipal Archives

SIGNIFICANT AUDIT RECOMMENDATIONS

- 1) SPU's collections policies and procedures should be strengthened and compliance with existing collections procedures needs to be improved. Specifically, accounts should be submitted timely to the collection agency, tracked and monitored, reconciled to collection agency data, and commission fees charged should be validated. Proper backup and support should be provided to the collection agency and all direct payments should be reported by the contractors.
- 2) Policies and procedures related to delinquent accounts should be re-evaluated given the numbers of customers who consistently pay late.
- 3) The solid waste contractors should provide adequate reporting on customer calls and complaints, and SPU should assess penalties for contractor service failures, as specified in the contract terms, or the terms should be revised.
- 4) SPU should strengthen procedures for invoice review for transfer services, yard-waste processing services, and recycling processing services.

Audit Conclusion	Risk	Management Action Plan
1. Customer Account Adjustments - SPU is not periodically reviewing Waste Management's customer account adjustments, as is done for Allied Waste/Rabanco.	High	SPU Finance reviewed Waste Management's customer adjustments during their 2007 billing review. Beginning in 2008, SPU will request Waste Management provide detailed customer adjustments reports, and SPU will review these annually.
2. Contractor Remittance of Customer Payments - Controls could be improved to ensure timely remittance of customer payments.	Medium	All contractors will transmit payments daily beginning in April 2009, with the implementation of the new solid waste collection contracts.
3. Accounts Receivable Aging Reporting - There are no regular aging reports prepared for Commercial Solid Waste Accounts Receivable.	Medium	SPU has requested the contractors to provide monthly aging reports. These reports will be reviewed and followed up on by SPU accounting staff on a monthly basis starting in 2008.
4. Customer Delinquency Rates - A significant percentage of commercial customers consistently pay a month or more late, and this may be increasing.	High	SPU will analyze the delinquent rates of each contractor, evaluate current policies and procedures and take necessary actions to minimize delinquencies. Estimated to be completed by October 2008.
5. Interest and Penalties for Delinquent Accounts - Interest fees charged do not appear to be adequate to encourage timely payment.	High	1) SPU will not pursue the unpaid interest fees. 2) Since September 2007, both contractors have been providing SPU with itemized information on delinquent accounts. 3) SPU will consider the options recommended to increase incentives for timely payment, and will make a decision on these by early fall 2008.
6. Contractor/SPU Communications - Some improvements are needed with contractor and SPU customer communications related to delinquent commercial solid waste accounts.	High	As part of the next annual review, SPU will request: 1) Contractors send the demand letter earlier, 2) Accounts are not referred to as "closed," 3) Bills display interest will be assessed.
7. Timeliness of Account Turn-In to Collection Agency - Delinquent commercial solid waste accounts are not sent to collections timely.	High	1) The contractors began sending monthly detailed reports in September 2007 and SPU Accounts Receivable (AR) forwards them to Treasury for collection as soon as possible. 2) SPU will work with the contractors and Treasury to resolve the issue of timing of the demand letter. 3) Treasury will forward all eligible items for collection to NCO in a timely manner.
8. Monitoring Accounts in Collections - SPU is not adequately monitoring the performance of the commercial accounts in collections.	High	1) Treasury now provides SPU AR a report on accounts in collections. SPU AR is working on an efficient way to reconcile this to their data. Once AR can reconcile to Treasury's data, Treasury will begin to reconcile to NCO's data. 2) SPU AR will continue to work with the contractors to send all the information needed to SPU.
9. SPU/City/Contractor Support for Collections Effort - The collection agency does not receive the support and documentation it needs from the contractors, SPU, and Treasury.	High	See Conclusion #5 and # 7: Accounts Receivable will continue to work with Treasury, NCO and the contractors to address any concerns that may arise.

10. Collection Rate Performance - Procedures are not adequate to maximize the collection rate and revenue recoveries.	High	See Conclusion #5. SPU will work with Treasury to ensure accounts are passed to NCO timely and start measuring NCO's collection rate performance in the spring of 2008.
11. Collection Agency Remission of Customer Payments - Policies and procedures governing the remission of customer payments to the collection agency need improvements.	High	When the City looks to negotiate a new collections contract, all of the cash flow terms and policies will be taken into consideration.
12. Collection Agency Commission Fees - Policies and procedures related to collection agency commission fees need some improvement.	High	1) See Conclusion 11. 2) SPU AR will verify NCO's commission fees charged, beginning in spring 2008.
13. Direct Payments - Controls related to direct payments need improvement.	High	SPU will reinforce to the contractors the importance of reporting all direct payments and work with them on a process for re-opening inactive accounts.
14. Customer Account Write-Offs - SPU is not consistently writing off accounts timely, per policy.	Medium	SPU's current practice is to write off accounts that are more than one year old. SPU will provide instruction and training to its staff to follow this guideline.
15. Reconciliation of Receivable Accounts - The Commercial Solid Waste Receivable accounts were not being reconciled frequently.	Medium	SPU will reconcile commercial solid waste receivables to the General Ledger on a monthly basis beginning in 2008. Variances will be researched. Reconciliations will be reviewed and approved.
16. Yard and Food Waste Processing Tonnage Charges - Control procedures are not adequate to ensure SPU is charged accurately for tonnage for yard waste processing services.	High	Cedar Grove, the composting vendor, implemented automatic scale data entry in December 2007 as recommended. Manual entry was eliminated.
17. Review and Approval of Yard Waste Processing Invoices - Improved procedures are needed for the review of invoices for yard waste processing.	Medium	1) SPU implemented a monthly query of scale data in December 2007. 2) SPU began routinely checking scale tickets against monthly invoices in January 2008.
18. Transfer Services Invoicing - Verification of transfer tonnage invoiced needs strengthening.	High	SPU will sample and check scale tickets against submitted scale data during the annual SPU contractor review beginning in 2008.
19. Invoicing for Recycling and Commodity Credit - Verification of recycling tonnage could be improved.	High	SPU will sample and check scale tickets against submitted scale data during the annual contractor review beginning in 2008.
20. Certification of Scales - None of the critical scales involved in the SPU solid waste processes have been licensed with or tested by the State.	High	SPU has requested that all critical scales be licensed with the State by May 2008 and that licensing is maintained in all future years.
21. Customer Complaint Tracking - Contractor reporting provided to SPU on customer complaints is inadequate.	High	1) SPU now receives detailed quarterly complaint logs from Waste Management and will require monthly logs from both contractors beginning May 2008. 2) SPU will expand the monthly complaint summary reporting to include complaints other than "missed."
22. Assessment of Penalties for Customer Service Failures - SPU is not assessing penalties for service failures, except for noise violations.	High	1) SPU tracks complaints and assesses penalties per contract based on customer calls or letters to the City. 2) SPU will monitor contractor complaint logs beginning in May 2008 for any other non-compliance.

CONTENTS

CHAPTER 1: INTRODUCTION AND BACKGROUND	1
Results in Brief	1
Background	3
Scope and Methodology	4
CHAPTER 2: SEATTLE PUBLIC UTILITIES REVENUE CYCLE AUDIT – COMMERCIAL SOLID WASTE - INTERNAL CONTROLS REVIEW	6
Conclusions	
<u>I. Rates and Service Usage Tracking</u> <i>No issues noted.</i>	6
<u>II. Billing and Customer Account Adjustments</u>	7
1. Customer Adjustments - Controls could be improved by reviewing customer account adjustments made by Waste Management, as is currently done for Allied Waste/Rabanco. <i>High risk</i>	8
<u>III. Payment Processing and Payment Remittances</u>	9
2. Contractor Remittance of Customer Payments - Controls could be improved to ensure timely remittance of customer payments to SPU. <i>Medium risk</i>	11
<u>IV. Accounts Receivable Management</u>	11
3. Accounts Receivable Aging Reporting – There are no regular account aging reports prepared for Commercial Solid Waste Accounts Receivable. <i>Medium risk</i>	13
4. Customer Delinquency Rates - A significant percentage of SPU Commercial Solid Waste customers appear to consistently pay a month or more late, and this trend may be increasing. <i>High risk</i>	13
5. Interest and Penalties for Delinquent Accounts - The current interest fees charged do not appear to be adequate to encourage timely payment of monies due and there are other issues relating to interest fees. <i>High risk</i>	14
6. Contractor/SPU Communications - Some improvements are needed with contractor and SPU customer communications related to delinquent Commercial Solid Waste accounts. <i>High risk</i>	16

<u>V. Collections, Dishonored Items, and Write-Offs</u>	17
7. Timeliness of Account Turn-In to Collection Agency - Delinquent Commercial Solid Waste accounts are not sent to collections timely, and this negatively impacts the collections rate and revenue recoveries. <i>High risk</i>	20
8. Monitoring Accounts in Collections – Procedures for tracking and monitoring the performance of Commercial Solid Waste accounts in collections require improvement. <i>High risk</i>	22
9. SPU/City/Contractor Support for Collections Effort – The collection agency does not receive the support and documentation it needs from the solid waste contractors, SPU, and Treasury to help maximize revenue recoveries. <i>High risk</i>	23
10. Collections Rate Performance – The City’s collection procedures require improvements in order to ensure the collections rate and revenue recoveries are maximized for Commercial Solid Waste accounts. <i>High risk</i>	25
11. Collection Agency Remission of Customer Payments - Policies and procedures governing the remission of customer payments to the collection agency need improvements. <i>High risk</i>	26
12. Collection Agency Commission Fees - Policies and procedures related to collection agency commission fees need some improvement. <i>High risk</i>	27
13. Direct Payments - Controls related to direct payments (i.e., customer payments made directly to the contractors or the City) could be improved. <i>High risk</i>	29
14. Customer Account Write-Offs - SPU is not consistently writing off commercial solid waste accounts by the time they are one-and-a half years delinquent, as is the current policy. <i>Medium risk</i>	30
<u>VI. Solid Waste Fund Accounting – Revenues and Receivables</u>	31
15. Reconciliation of Receivable Accounts - The Commercial Solid Waste Receivable accounts were not being reconciled frequently enough to provide adequate control. <i>Medium risk</i>	32
<u>VII. Information Technology</u> <i>No issues noted.</i>	33
<u>VIII. Vendor Billing for Services, Contracts, and Performance</u>	34
16. Yard and Food Waste Processing Tonnage Charges - Control procedures are not adequate to ensure SPU is charged accurately for tonnage for yard and food waste processing services. <i>High risk</i>	37

17. Review and Approval of Yard Waste Processing Services Invoices - Improved procedures are needed for the review and approval of invoices for yard waste processing services. <i>Medium risk</i>	39
18. Transfer Services Invoicing - Controls over the verification of tonnage invoiced for transfer services could be strengthened. <i>High risk</i>	40
19. Recycling Invoicing for Processing Services and Commodity Credit – The verification of the recycling tonnage used for invoicing recycling processing services and for calculating the “recycling commodity credit” could be improved. <i>High risk</i>	41
20. Certification of Scales - None of the critical scales involved in the SPU Solid Waste processes have been licensed with or tested by the State of Washington Weights and Measures unit within the last several years. <i>High risk</i>	42
21. Customer Complaint Tracking - Contractor reporting provided to SPU on customer complaints/issues needs to be improved. <i>High risk</i>	43
22. Assessment of Penalties for Customer Service Failures - SPU is not assessing penalties or “liquidated damages” specified by contract terms for service failures, except for noise violations. <i>High risk</i>	44

APPENDICES

Appendix 1	Data on Drainage Revenues from 2002 to 2007	46
Appendix 2	SPU Revenue Cycle Audit – Commercial Solid Waste – Risk Matrix	47

CHAPTER 1: INTRODUCTION AND BACKGROUND

Seattle Public Utilities (SPU) provides solid waste collection, processing, and disposal services to the Commercial Solid Waste customers located within the City. SPU outsources many of the functions associated with these services to several solid waste vendors. The outsourced commercial waste functions include waste collection, some waste processing and transfer, some waste transport, long-term disposal, and customer billing and billing administration services. Commercial Solid Waste revenues totaled over \$42 million in 2007. (See Appendix 1 for data on Commercial Solid Waste revenues for the past 6 years.)

This audit evaluated the internal controls governing the billing and collecting of SPU Commercial Solid Waste service fees. The audit's scope also included internal controls governing the outsourced solid waste services, including the areas of vendor contracts, vendor performance of services, and invoicing for services. We evaluated the policies, procedures, and operations involved in these processes. This report is one part of a larger audit of the revenue cycle for all of the SPU primary utility services - Drainage, Solid Waste, Water, and Wastewater. The report for the Drainage revenue cycle audit was issued on February 8, 2007, the Transfer Stations Revenue Cycle audit report was issued on February 14, 2008, and the reports for the remaining modules of this audit project will be issued as the work is completed. This area was selected for audit due to the size of the revenue stream associated with SPU's utility services, which is over \$400 million annually.

RESULTS IN BRIEF

Overall, we found internal controls were adequate for the policies, procedures, and operations governing the billing and collecting of fees for SPU Commercial Solid Waste services, and for the solid waste functions SPU outsources to vendors. However, we also noted some significant control weaknesses that require immediate resolution, as well as several less serious control weaknesses. See Appendix 2 for a color-coded risk level chart for the audit's major scope areas and the individual findings within these areas.

The following is a summary of our findings in each major scope area.

Rates and Service Usage Tracking: We did not find any control weaknesses within this area. Commercial Solid Waste service rates are established in a logical and equitable manner, rates are accurately applied for commercial waste services, and commercial customer usage of solid waste services, are generally accurately tracked.

Billing and Customer Account Adjustments: We concluded that controls over billing functions are adequate but controls over customer account adjustments could be improved. Our audit work indicated that SPU's Commercial Solid Waste customers are billed accurately and timely for regular and exception/additional solid waste services. However, SPU needs to strengthen their review of the customer adjustments made by one of its contractors.

Payment Processing and Remittance of Payments: Overall, we found proper controls are in place and functioning adequately for customer payment processing and payment remittance functions. We concluded that customer payments are processed, posted, and deposited accurately and securely. However, one of SPU's contractors could improve the timeliness of its remittance of customer payments to SPU.

Accounts Receivable Management: Accounts receivable management functions controls should be improved. We found that accounts receivable are accurately recorded, but they are not adequately tracked or monitored due to a lack of account aging reporting. The solid waste contractors follow procedures properly for delinquent accounts in terms of customer notification procedures, and services are suspended per contract terms. However, we noted that a significant percentage of commercial customers appear to consistently pay a month or more late, and this trend may be increasing. While we found that interest fees are currently accurately applied to delinquent accounts, there are issues with policies related to interest fees and/or penalties for delinquency. The fees do not appear to be sufficient to encourage timely payment of monies due, and there is a problem with the solid waste contractors' reporting of interest fees for collection purposes. We also found that contractor and SPU customer communications related to delinquent Commercial Solid Waste accounts need some improvement.

Collections, Dishonored Items, and Write-offs: We found controls governing the collections functions require significant improvements. Delinquent accounts are not submitted for collections in a timely manner, improvements to procedures are needed for tracking and monitoring accounts in collections, and the City is not adequately supporting the collections effort in terms of responding to questions and requests for supporting documentation in a timely manner. Payments made directly to the contractors by customers are not consistently reported to the collection agency, as is required, and the collections rate and recovery of revenues are not being maximized. We found that the policies and procedures related to the remission of customer payments from the collection agency to the City need improvements. There are some issues with the policies and procedures relating to collection fees and commission charges for the City's accounts, including the way fees are applied to accounts and SPU's lack of validation of the fees charged. While controls appear to be adequate for the handling of dishonored items (i.e., NSF checks and credit card charge backs), SPU is not consistently writing off commercial customer accounts by the time they are 1 1/2 years delinquent in accordance with policy.

Solid Waste Fund Accounting – Revenues and Receivables: We found controls over accounting for Commercial Solid Waste (CSW) revenues and receivables need some improvement. We concluded that CSW revenues and receivables are accurately and properly accounted for and accounts are properly monitored by management. However, we noted during the audit that the CSW revenue accounts were not reconciled frequently enough to provide adequate control.

Information Technology: Overall, we found the controls over information technology functions for Commercial Solid Waste to be adequate, and we did not note any control weaknesses within this area. Systems handling Commercial Solid Waste business and

accounts, including SPU's CSW system and the contractors' customer accounting systems, are backed up regularly and back-up files are stored securely. There appear to be proper procedures in place for system change control and management of system access rights. Adequate audit trails (i.e., audit logging) are in place for the systems handling the commercial business.

Vendor Billing for Services, Contracts, and Performance: Although many of the processes are well controlled, we found that controls over outsourced solid waste functions related to vendor invoicing, vendor contracts, and vendor performance need improvements. We noted some concerns in these areas:

- Due to the procedures followed at the Cedar Grove Composting (CGC) scale house, SPU cannot be assured charges are accurate for yard and food waste processing services, which are based on tonnage. Improvements are also needed over SPU's review of CGC invoices.
- Tonnage used for invoicing outsourced transfer services is not properly verified.
- Recycling tonnage numbers used for invoicing outsourced recycling processing services and calculating the recycling commodity credit are not properly verified.
- While all of the critical scales involved in the SPU solid waste processes are regularly tested, none of them have been licensed with or tested by the State of Washington Weights and Measures unit within the last several years.
- SPU is not assessing penalty fees to the contractors for service failures, such as missed pick-ups, in accordance with contract terms.
- While SPU commercial customer complaints/issues appear to be handled appropriately by the contractors, the contractor reporting provided to SPU on customer complaints/issues needs to be improved and this hampers SPU's ability to assess service failure penalty fees.

BACKGROUND

History of the SPU Commercial Solid Waste Contracts

The SPU Commercial Solid Waste contracts were established in 2000. Solid waste used to be a "franchised service" that was regulated by the Washington Utilities Commission (WUTC). Businesses in the City were direct customers of the solid waste companies and rates for solid waste services were set by the WUTC. Now, businesses are customers of SPU and SPU sets the rates for its customers, though SPU contracts for most of the actual solid waste services. Leading up to the time of the inception of SPU's commercial contracts, there was a trend within the solid waste industry for larger companies to buy smaller local companies that resulted in a consolidation of the industry into a few "mega" solid waste companies. Two of these "mega-waste companies" served the Seattle market area, including SPU's two current waste collection vendors, Allied Waste/Rabanco (AW) and Waste Management (WM). Under the prior franchised system, the City could select either company to provide service in any part of the City. Because the City believed this system provided insufficient competition, it decided to contract for solid waste services and give each contractor a certain geographic area within the City to serve residential and

commercial customers. SPU management stated that commercial rates dropped by 10% after SPU assumed responsibility for managing the contracts.

At the time SPU took ownership of the Commercial Solid Waste accounts, it did not have an infrastructure in place to bill commercial customers like they did for residential customers, who were billed by the CCSS/Banner customer accounting system. (Note: The CCSS/Banner system is used to bill residential and commercial water and waste water services, as well as residential solid waste services.) Because of this lack of process and system infrastructure, SPU decided to leave the billing administration and customer service functions with the contractors while it monitors the contractors' service delivery for these functions, as well as for waste collection functions.

Current Commercial Solid Waste Services

SPU provides solid waste collection and disposal services to about 9,000 commercial customers in the City. Customer garbage, and optionally their yard/food waste, is collected, transported, processed, and disposed of for fees that vary by established service levels. Currently, SPU contracts with Allied Waste/Rabanco and Waste Management to provide waste collection services, and billing, customer service, and various administrative functions for commercial customers.

SPU also outsources other solid waste services, including recycling waste processing, yard and food waste processing, long-term waste disposal and transportation, and some waste transfer services.

SCOPE AND METHODOLOGY

During this review, we focused on internal controls that affect SPU's and the City's revenues and expenses. In addition to reviewing control procedures, we tested compliance with procedures whenever possible. Specifically, we reviewed internal controls relating to the following areas:

- Rates and service usage tracking
- Billing and customer account adjustments
- Payment processing and remittance of payments
- Accounts receivable management
- Collections, dishonored items, and write-offs
- Solid Waste Fund accounting – revenues and receivables
- Information technology
- Vendor billing for services, contracts, and performance

We based our audit conclusions on interviews with City personnel, interviews with SPU's solid waste vendors, testing of data found in reports and computerized systems, and review and analyses of procedures, policies, and available documentation and electronic data. We observed operations related to this review's scope, including visits to

the vendor locations where key solid waste processes occur for the SPU Commercial Solid Waste functions, and SPU's transfer stations.

We conducted the audit fieldwork and analysis phase of this review between August 2006 and August 2007.

We used sampling techniques based on a risk-based approach, which is a cost-effective way to review significant controls. Our review, therefore, would not necessarily disclose all significant weaknesses and irregularities.

We conducted this audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

CHAPTER 2: SEATTLE PUBLIC UTILITIES REVENUE CYCLE AUDIT – COMMERCIAL SOLID WASTE - INTERNAL CONTROLS REVIEW

The Office of City Auditor conducted this review to assess the condition of internal controls for the Seattle Public Utilities (SPU) Commercial Solid Waste revenue cycle. Overall, we found that internal controls were adequate for these areas, but we also noted several control weaknesses. We found that controls related to accounts receivable management and collections functions require significant improvements in order to maximize revenue recovery. And, we noted several improvements that need to be made in the areas related to vendor services.

I. RATES AND SERVICE USEAGE TRACKING - *Controls are adequate overall -*

Background: SPU's Solid Waste rates, including those for the collection of waste from SPU's commercial customers, are formally adopted by the City Council by ordinance. New rates are usually adopted about every two or three years, and rate changes are generally the result of a SPU rate study. Rate studies involve analyzing current and projected costs, including the costs of operations and capital projects, and setting rates at the level needed to cover these expected costs. SPU strives to keep the rates as low as possible but high enough to cover costs. Rates are also set with the objective of meeting SPU and City policy goals, such as encouraging recycling and assisting low-income citizens with reduced rates. SPU sets the rates that the solid waste vendors use to bill the commercial customers.

Commercial solid waste customers are set up with solid waste service-levels to match their specific needs. Commercial waste service options include varying sizes of garbage cans, garbage containers or dumpsters, and frequency of pick-up. Charges are specific to each customer's service-levels. For example, a large restaurant may have two large dumpsters that are picked up daily or three times a week, whereas a small business office may only require a regular-size garbage can with weekly pick-up. Most commercial customers pay for a set level of services per month, but some customers are set up on a tonnage basis, and pay a per ton rate based on the tonnage of waste collected from their dumpster. These tonnages are calculated and recorded at the transfer stations. In addition to normal monthly service-level charges, commercial customers can be charged for additional services, such as collection of "extra garbage," replacing dumpsters or cans, extra pick-ups, etc. There are rates established for these extra or special services, just as there are for the normal monthly services. SPU's solid waste contractors are responsible for recording and tracking any additional services performed for the SPU commercial customers, and for billing for all solid waste services.

Audit work we performed: We reviewed the processes and functions related to commercial solid waste rate-setting and service usage tracking to determine whether internal controls were adequate. We conducted a procedural review of the rate-setting functions by reviewing the rate-setting process procedures and the methodology. We

reviewed service usage tracking at a detailed level, which included reviewing the controls over these processes and testing them to verify that they were functioning properly. Specifically, we evaluated whether controls would ensure SPU Commercial Solid Waste rates are established in a logical and equitable manner and customer usage of services is accurately tracked and recorded. This included reviewing the most recent rate-study results and the methodology used to perform the study. We verified that rates were properly reflected in and billed by the solid waste contractors' customer accounting system, visited each contractor on two occasions and reviewed their customer billing systems, reviewed controls over tracking and billing for "extra garbage" and other additional services, and verified whether the contractor truck tare weight program was functioning accurately.

Conclusion: Overall, we found that proper controls were in place and functioning adequately. We did not find any control weaknesses within this audit area.

II. BILLING AND ACCOUNT ADJUSTMENTS - *Controls need some improvement* -

Background: SPU outsources billing and customer account administration functions for the Commercial Solid Waste customers to the two solid waste collection contractors, Allied Waste/Rabanco (AW) and Waste Management (WM). AW and WM bill SPU's commercial customers monthly with an itemized statement of services and charges. Customers have 30 days to make payment to the contractors or they are charged interest at the rate of 1% per month on the outstanding balance. The contractors remit/transfer the customer payments to the City/SPU as they are received. The contractors bill SPU monthly for the solid waste collection services they performed during the prior month, and the charges for these services are negotiated as part of the commercial collection contracts.

The contractors track the SPU commercial customer accounts in their own customer accounting systems, InfoPro for AW and MAS for WM, and download the updated account data monthly into SPU's Commercial Solid Waste (CSW) database system. The SPU Data Analysis unit oversees this download process and monitors the CSW data, including performing various data validity checks. The contractors' billing and customer service personnel are authorized to make adjustments and corrections to customer accounts in situations in which there are errors, customers dispute a transaction, etc. Each contractor has a procedure in place for handling customer adjustments and management approval is required for adjustments exceeding a certain dollar level.

Audit work we performed: We reviewed the billing and customer account adjustment functions to determine whether internal controls were adequate. Specifically, we evaluated whether controls would ensure that SPU's commercial solid waste customers were billed accurately and timely by the contractors, and any customer account adjustments were accurate and proper, approved, and handled securely. This included determining whether:

- Commercial customers were billed accurately by the contractors for their regular waste collection service-levels,
- Extra garbage or exception waste services were accurately recorded by the contractors and billed to the customers,
- Accurate customer statements were mailed out monthly,
- Customer account adjustments were made properly.

We met with contractor personnel involved in these functions at their offices on two separate occasions each, interviewed SPU personnel, and reviewed SPU Finance’s annual contractor review workpapers. We relied on SPU Finance’s test work covering billing accuracy, and tested samples of customer adjustments made to verify compliance with control procedures for these functions.

Conclusion: Overall, we found controls are adequate for customer billing, and customers are billed accurately and timely for regular and additional solid waste services. However, SPU needs to strengthen their review of account adjustments made by one of the contractors. Details are discussed below.

Customer Adjustments - Conclusion 1: Controls could be improved by reviewing customer account adjustments made by Waste Management. *High risk*

Background

AW and WM billing and customer service personnel are authorized to make adjustments and corrections to customer accounts in their customer accounting systems. Personnel can adjust customer balances and charges. The customer adjustment procedures followed by each of contractor are described below:

- Allied Waste The two AW Accounts Receivable (AR) clerks enter all the adjustments to customer accounts for billed amounts and amounts due. The AR clerks input adjustment to their InfoPro customer accounting system, the Billing Manager reviews and authorizes the adjustment on a “proof and post” screen in InfoPro, then an AR clerk finalizes the adjustment process in the system. An explanation of the reason for the adjustment is always entered in the Notes field on the account. A common reason for adjustments is a customer request for a credit, often to credit back interest charged to delinquent accounts. AW’s procedure for handling credits is for one AR clerk to write up the credit request, and the other AR clerk to enter the adjustment. If the customer adjustment is under \$50, management approval is not required, but if it’s over \$50, the Billing Manager reviews and approves it using the “Manual Adjustments Audit Report Over \$50”. If the adjustment is over \$250, there is a separate adjustment form filled out and, the Controller and the General Manager review and approve it, in addition to the Billing Manager.

- Waste Management Customers call in requests for adjustments to WM's Call Center, which is located at their Kirkland office. All calls are entered into the Notes screen on the customer's account and given a code, depending on the issue the customer called about. The Customer Service Representative (CSR) creates an adjustment ticket on their system. The "city desk" person in WM's Data Entry unit reviews the ticket, and enters it into MAS with the CRA adjustment code. If the adjustment is over \$100, it is coded as CR100 on the ticket and must be approved by the Controller. The system won't allow a CR100 adjustment to post without this approval. The WM Billing Manager also reviews and approves these adjustments.

Issue, Impact, and Recommendation

Controls over customer account adjustment functions are critical controls because customer adjustments are a common method to commit fraud. Employees can adjust accounts for customers in exchange for a "kickback" or something of value. Since SPU outsources this function to the solid waste contractors, SPU should ensure that the contractors are making adjustments that are accurate, appropriate, and properly approved by management.

Currently, SPU Finance reviews AW's customer adjustments as part of their testing for the annual contractor review, but they don't do this for WM. This is simply because AW has a regular report in place for customer adjustments. SPU Finance could request a query of adjustments from WM, which we did to perform our audit test work, and review the results of this query. We performed detailed test work on a sample of customer adjustments made by both AW and WM and did not find any issues with the accuracy, appropriateness, or approvals of these adjustments. We recommend that SPU periodically review a sample of customer adjustments made by both contractors to ensure that adjustments are appropriate and properly authorized.

ACTIONS PLANNED OR TAKEN

SPU agrees with this recommendation. During our 2007 annual review of Waste Management's billing system, customer adjustments were reviewed for propriety. Beginning in 2008, we will request that Waste Management provide a report detailing customer adjustments, which will be reviewed during our ongoing annual reviews.

III. PAYMENT PROCESSING AND PAYMENT REMITTANCES - *Controls are adequate overall -*

Background: SPU outsources billing and payment processing for Commercial Solid Waste customers to the solid waste contractors. Commercial customers may pay by mail, on-line, or over the phone using either a credit card or an Automated Clearing House (ACH) transfer. Each contractor utilizes a third-party "lockbox" vendor to receive, open, and process mailed payments. The lockbox vendors send payment batches via a file transfer process (ftp) to the contractors, who post the payment batches to the customer

accounts in their systems. The contractors update the customer accounts daily to reflect the payments received and posted. SPU's CSW system obtains updated customer payment information from the contractors as part of the monthly file download process.

The contractors remit the customer payments they have received by wire-transferring the funds to the City's bank, Wells Fargo. The Treasury unit within the Department of Executive Administration (DEA) receives notice of these wire transfers from the bank and posts the funds to SPU's Solid Waste fund. AW remits customer payments received two times a week and WM remits payments daily.

Audit work we performed:

We reviewed the payment processing and handling functions to determine whether internal controls were adequate. Specifically, we evaluated whether controls would ensure SPU Commercial solid waste customer payments are processed, posted, and deposited accurately, timely, and securely. This included performing audit work to verify payments were:

- Handled securely and properly for each method of payment, including ensuring on-line payments complied with Payment Card Industry (PCI) standards,
- Processed and posted to customer accounts in the contractors' systems accurately and timely,
- Remitted from the contractors to the City/SPU accurately and timely, including any interest fees paid,
- Deposited to the City's bank accurately and timely,
- Posted accurately and timely to the General Ledger (GL) in the City's Summit financial system.

We met with contractor personnel involved in these functions at their offices on two separate occasions each, interviewed SPU personnel, and reviewed SPU Finance's workpapers from its annual contractor review and relied on their test work for verification of accurate and timely payment posting, remission, and deposit. We reviewed the on-line payment procedures followed by both contractors and verified that both are using a PCI-compliant vendor for their "payment gateway" services.

Conclusion: Overall, we found that controls were adequate over these functions. We noted one opportunity for improvement relating to the timeliness of remittance of customer payments. Details are covered below.

Contractor Remittance of Customer Payments - Conclusion 2: Controls could be improved to ensure timely remittance of customer payments. *Medium risk*

Background

The contractors remit the customer payments they receive by wire-transferring the funds to Wells Fargo, the City's bank. AW remits customer payments to the City twice a week, and WM remits payments daily.

Issue, Impact, and Recommendation

Controls should ensure customer payments are remitted to SPU accurately and in a timely manner. We found that while the contractors are remitting payments completely and accurately to SPU and in the contractually specified timeframe, the timeliness of these payments could be improved. Currently, WM transfers commercial customer payments to the City daily, but AW only transfers them twice a week. The commercial collection contract terms (section 520) allow the contractors to transfer payments four days after they receive them, so AW is in compliance with the contract. We recommend that the contract terms be changed to require customer payments to be transferred daily, which would improve the City's cash flow and ensure consistency among the contractors.

ACTIONS PLANNED OR TAKEN

All contractors will transmit payments daily beginning in April 2009, with the implementation of the new solid waste collection contracts.

IV. ACCOUNTS RECEIVABLE MANAGEMENT - *Controls need improvement* -

Background:

SPU has outsourced the Commercial Solid Waste accounts receivable management functions to the solid waste contractors up to the point at which significantly delinquent accounts are turned over to a collection agency. Customers have 30 days to make payment for the charges on their monthly statement or they are charged interest at the rate of 1% per month on the outstanding balance. Each contractor has a procedure they follow with delinquent SPU accounts that includes mailing a series of delinquent notices to the customers, phoning the customers, providing a warning notice that garbage collection service will be suspended, and ultimately suspending service. The contractors suspend waste collection service when accounts are between 45 to 65-days delinquent, "close" the customer accounts on their systems when they're between 60-days to 90-days delinquent, and return the accounts to SPU Accounts Receivable, which sends the accounts to the City's collection agency. As of year-end 2006, there was about \$4 million in Commercial Solid Waste Accounts Receivable.

The contractors track the SPU commercial customer accounts in their customer accounting systems, InfoPro for AW and MAS for WM. These systems have been programmed to automatically trigger delinquent notices and phone call queues when accounts hit certain levels of delinquency. SPU's CSW database is updated monthly with the status of all accounts, including delinquent accounts, but SPU does not receive or

produce any sort of reports on delinquent accounts or account “aging”. The contractors send a monthly report on the accounts that have been designated as “closed” on the contractors’ customer systems, and which are being returned to SPU to pursue collections.

Audit work we performed:

We reviewed the accounts receivable management functions to determine whether internal controls were adequate. Specifically, we evaluated whether controls would ensure SPU’s Commercial Solid Waste accounts receivable are properly tracked and followed up on to ensure compliance with procedures and maximum recovery of monies owed. We also evaluated whether control procedures would ensure interest charges were accurately applied in accordance with SPU policy, and whether these charges provided adequate incentive to encourage timely payment on customer accounts. This included performing audit work to review and verify:

- Interest was properly and accurately applied to delinquent accounts and interest receivable was accurately tracked,
- Contractors properly notified customers via mailed notices and phone calls when their accounts became delinquent,
- Contractors suspended garbage collection services at the appropriate time consistent with SPU policy and after proper notification of the customer,
- CSW account aging status query report extracts used to identify delinquency rates for the commercial accounts,
- Penalty fees for account delinquency (i.e., interest charges) to determine whether they appeared to be sufficient to encourage timely payment.

We met with personnel involved in these functions at their offices on two separate occasions with each contractor, interviewed SPU personnel, reviewed customer accounts on the contractors’ systems, reviewed examples of contractor customer notices, selected a sample of delinquent accounts to determine whether the appropriate steps were taken in terms of customer notifications, application of interest charges, and suspension of service.

Conclusion:

We found controls over these functions need improvement. Regular account aging reports are not prepared on delinquent SPU Commercial Solid Waste accounts; this type of reporting is a standard management tool for monitoring account delinquency rates. We noted that a significant percentage of SPU Commercial Solid Waste customers appear to consistently pay a month or more late, and this trend may be increasing. We found issues with current SPU policies related to interest fees/penalties for delinquency in that they do not appear to be sufficient to encourage timely payment of monies due, and we noted that there is a problem with contractors’ reporting of interest fees for collection purposes. We also found that some improvements are needed with contractor and SPU customer communications related to delinquent Commercial Solid Waste accounts. Details on these issues are covered below.

Accounts Receivable Aging Reporting - Conclusion 3: There are no regular account aging reports prepared for Commercial Solid Waste Accounts Receivable.
Medium risk

Background

The contractors track the status of SPU's commercial customer accounts in their own customer accounting systems and SPU's CSW database is updated monthly with the download from these systems. The contractors send SPU Accounts Receivable a list of accounts that have hit the delinquency point to have their garbage collection service suspended, and a list of accounts they are closing on their systems and returning to SPU to pursue collections; however, they do not provide any regular reports on account delinquencies or account aging.

Issue, Impact, and Recommendation

SPU management should receive and review regular aging reporting for the Commercial Solid Waste Accounts Receivable so they can effectively monitor delinquent accounts and any delinquency rate trends. Aging reports should show current accounts, accounts that are 30-days delinquent, 60-days delinquent, 90-days delinquent, one-year delinquent, etc. Currently, there are no regular aging reports produced for commercial accounts. During audit fieldwork, we requested a query from CSW of account aging data and were only able to obtain query results showing summarized totals by contractor for accounts receivable that were current, over 30-days delinquent, and over 60-days delinquent. We recommend that adequate aging reporting be produced for the SPU Commercial Solid Waste accounts and that SPU management regularly review these reports.

ACTIONS PLANNED OR TAKEN

SPU agrees with this recommendation and has requested the contractors to provide monthly aging reports listing current accounts, accounts that are 30-days delinquent, 60-days delinquent, 90-days delinquent, one-year delinquent, etc. The report will be reviewed and followed up on by our accounting staff on a monthly basis starting in 2008.

Customer Delinquency Rates - Conclusion 4: A significant percentage of SPU Commercial Solid Waste customers appear to consistently pay a month or more late, and this trend may be increasing. *High risk*

Background

SPU Commercial Solid Waste customers are billed monthly by the contractors, for the prior month's solid waste collection services, and they have 30 days to pay or they are assessed interest at the rate of 1% per month on the outstanding balance. Garbage collection service is not suspended until customers are at least 45 to 65-days delinquent with their payments.

Issue, Impact, and Recommendation

SPU's policies and procedures should help ensure the Commercial Solid Waste customers pay in a timely manner. We found that a significant percentage of the commercial customers consistently pay a month or more late, and this trend may be increasing. For 2005, a query of CSW account status data showed that 17.5% (or \$677,191) of customers were over 30 days delinquent and 2.9% (or \$113,986) were over 60 days delinquent. For 2006, CSW account status data showed 20% of customers (or \$810,214) were over 30 days delinquent and 3.6% (or \$145,954) were over 60 days delinquent. We also noted there was some variation among delinquency rates for the accounts handled by each contractor. For 2006, 18.8% of the Allied Waste/Rabanco Commercial customers were over 30 days delinquent, versus 23.4% for Waste Management. Waste Management services the south-end commercial customers and Allied Waste/Rabanco services the north-end. We believe this high delinquency rate indicates that late penalties/interest charges are not adequate to encourage commercial customers to pay in a timely manner. See a detailed discussion of the issue involving penalties for delinquency at Conclusion 5. In addition, this issue also highlights the importance of establishing account Aging reporting that is regularly reviewed by SPU management. We recommend SPU re-evaluate its policies and procedures for handling of delinquent Commercial Solid Waste accounts with the objective of minimizing account delinquencies and maximizing revenue recovery.

ACTIONS PLANNED OR TAKEN

SPU will analyze the delinquent rates of each contractor, evaluate our current policies and procedures and take necessary actions to minimize account delinquencies. We plan to have this task completed in the early fall of 2008.

Interest and Penalties for Delinquent Accounts - Conclusion 5: The current interest fees charged do not appear to be adequate to encourage timely payment of monies due and there are other issues relating to interest fees. High risk

Background

As stated in their contracts with SPU, the solid waste contractors charge SPU's Commercial Solid Waste customers 1% per month on their outstanding balance if their accounts are delinquent by 30 days or more. WM's and AW's customer accounting systems are programmed to apply this interest charge automatically if it's applicable. One percent per month is the interest rate allowed by Washington state law (RCW 19.52.020) for this type of receivable. State law also allows municipal utilities to charge a penalty fee on delinquent solid waste charges (RCW 36.94.150), but SPU currently does not do this. The contractors remit any interest fees collected to the City/SPU along with customer payments for the "principal" balances. SPU posts interest fees collected to a separate Interest Revenues account in Summit, but interest fees due are tracked within the Commercial Solid Waste Accounts Receivable account; there is no separate receivable account for interest.

Issue, Impact, and Recommendation

Controls should ensure interest on delinquent Commercial Solid Waste accounts is accurately charged, tracked, collected, and remitted timely by the contractors to SPU. Interest and penalty fees for delinquent accounts should be sufficient to encourage customers to pay in a timely manner. We concluded that interest is currently accurately charged, tracked, collected, and remitted timely by the contractors, but there was a problem with this with one of the contractors in the past and the details are covered below. In addition, we noted problems with the contractors' reporting of interest fees for collection purposes and accrual of interest for accounts in collections. We also concluded that the current fees charged for delinquent accounts do not appear to be sufficient to encourage timely payment of monies due.

- SPU Finance found that Waste Management did not charge interest to delinquent SPU Commercial Solid Waste customers until they were 60-days delinquent, rather than 30-days delinquent as the contract required, from the inception of the commercial collection contract in 2001 until October 2006. Apparently, this situation was caused by a programming error on Waste Management's part. SPU Finance became aware of this issue by conducting their annual review of the contractors' performance of billing administration functions for the commercial accounts. SPU Finance called attention to the issue and Waste Management began charging interest properly in October 2006. Although this situation has been corrected, SPU Finance estimates it cost the City about \$45,000 annually since 2001 in lost interest revenues, or a total of \$273,000, and it amounted to \$35,000 in 2006. It appears that SPU management does not intend to attempt to recover the lost \$273,000 in interest revenues from Waste Management.
- To comply with collections industry regulations, the City's collection agency needs to receive customer account data with the accurate itemization of the balance owed (i.e., principal versus interest and any penalty fees) and they are required to provide this information to the customer. The contractors currently do not send the proper balance itemization for delinquent SPU Commercial Solid Waste accounts that they are returning to SPU for collections, so the collection agency cannot provide it to the customers in their statement as they are required to by regulation. Allied Waste/Rabanco does not provide any itemization of interest and principal. Waste Management sends itemized information on principal and interest, but interest figures are clearly wrong in some cases, specifically for the "co-mingled" accounts.
- The current interest fees of 1% per month probably do not provide sufficient incentive for customers to pay timely because this generally doesn't amount to a significant dollar amount, and we noted there was a fairly high delinquency rate for SPU's Commercial Solid Waste accounts (see this discussion in Conclusion 4). The biggest incentive for customers to pay their charges is to avoid suspension of garbage collection service. But, since service isn't suspended

until accounts are at least 45-65 days delinquent, it appears penalties are not sufficient to minimize the number of accounts that are “mildly delinquent”. We recommend that SPU consider assessing a late penalty fee, in addition to interest fees, for delinquent Commercial solid waste accounts.

- Although permissible under State law, delinquent Commercial Solid Waste accounts do not continue to accrue interest once they have been forwarded to collections and the City/SPU does not assess a collection fee to these customers. The City’s collection agency, NCO, noted that many of their other clients permit customer accounts in collections to continue to accrue interest. To assess interest for accounts in collections would require system changes by the City because updated account balances would need to be regularly passed to the collection agency’s information system, but the City/SPU could assess a collection fee without significant system changes. We recommend that SPU consider these two options.

ACTIONS PLANNED OR TAKEN

The potential uncharged interest fees related to late payments from prior years will not be recovered because 1) SPU does not recommend retroactive billing of customer late payment fees that were not routinely applied at the time; 2) the potential charges would have been penalty revenue not actual service delivery revenue. SPU is holding the contractor accountable for all charged and uncharged interest moving forward.

Starting September 2007, both Allied Waste and Waste Management have been providing SPU itemized information on delinquent accounts. We will continue to work with them to ensure the quality of data provided.

It is SPU’s goal to minimize account delinquencies. We will consider the options recommended to increase the incentive for our customers to pay their charges on time. We plan to arrive at a decision in the early fall of 2008.

Contractor/SPU Communications - Conclusion 6: Some improvements are needed with contractor and SPU customer communications related to delinquent Commercial Solid Waste accounts. *High risk*

Background

The solid waste contractors’ billing and customer service personnel communicate verbally and in writing with SPU’s Commercial Solid Waste customers at various times. The contractors’ billing units send a series of written notifications to delinquent commercial customers at different points, as well as phoning these customers. City personnel in SPU Accounts Receivable, SPU Contracts, and the Collections unit in DEA Treasury also communicate verbally and in writing with the commercial customers on various matters.

Issue, Impact, and Recommendation

All communications with SPU Commercial Solid Waste customers should be handled properly. Currently, there are some improvements needed with contractor and SPU customer communications related to the delinquent commercial accounts.

- The contractors send a “demand letter” or “notice of intent” letter to delinquent customers to notify them their account will be forwarded to a collection agency if it isn’t paid within 30 days. Currently, Allied Waste/Rabanco doesn’t send this letter until accounts are 75-days delinquent, whereas Waste Management sends this notification at the 30-days delinquent point. We recommend that Allied Waste send the demand notification sooner with one of their earlier scheduled delinquent notices so SPU can forward the accounts to collections as soon as they are returned by Allied Waste for collections.
- Contractor and SPU communications, both written and verbal, should not refer to any delinquent SPU Commercial Solid Waste accounts as “closed” or “cancelled,” when SPU is pursuing collections on the account through a collection agency because this could represent a violation of credit regulations. Currently, contractor personnel are communicating with customers that their accounts are “closed” because the contractors have suspended/written off the accounts on their system and returned the accounts to SPU.
- Allied Waste/Rabanco’s customer billing statement does not state that interest will be assessed to delinquent accounts in the amount of 1% per month and we recommend that it should include this.

ACTIONS PLANNED OR TAKEN

As part of the next annual review, SPU will ask the contractors to send the demand letter at the time the 45-day or 60-day notice is sent, and request they not refer to accounts as 'closed' when the City is pursuing collections. SPU will also request bills display that interest will be assessed on delinquent balances beginning in 2009.

V. COLLECTIONS, DISHONORED ITEMS, AND WRITE-OFFS - *Controls need significant improvements* -

Background: While SPU outsources the functions associated with managing the “mildly delinquent” (i.e., 30 to 90 days delinquent) Commercial Solid Waste accounts to the contractors, SPU and the City handle functions involved with sending the “seriously delinquent” (i.e., over 90 days delinquent) accounts to collections. However, the City/SPU outsources the actual collections activities to a collection agency, NCO. As of April 2007, SPU had about \$307,000 in collections for the commercial accounts.

When a commercial account is significantly delinquent, the contractors suspend waste collection services, send the customer a “demand letter,” and assign the account an

“impending write-off” status. Then, in two weeks to a month later, the contractors “close” or inactivate the account on their customer accounting system, although all account history is maintained on the system, and turn the account over to SPU Accounts Receivable for collections. SPU Accounts Receivable enters the account into a spreadsheet they keep for commercial accounts in collections status, hold the accounts for about one month, and then forwards it to the Department of Executive Administration’s (DEA) Treasury’s Collections unit, which sends it to NCO. (Note: Only accounts with a balance of \$50 or more are sent to the collection agency, and accounts with a balance of \$5,000 or more are sent to the City Attorney’s Office, which pursues recovery of the monies due.) The City uses NCO for all of their outside collections efforts, except for Seattle Municipal Court accounts, which are handled by a different collection agency. The customer account record in CSW shows the account is in collections and the account stops accruing the 1% monthly interest charges at the point it is inactivated on the contractors’ systems. The DEA Collections unit enters accounts into a Citywide Collections database (CDS), sends a demand letter to the customer notifying them their account will be sent to collections if they don’t pay within 30 days, and then sends the accounts via a file-transfer process (ftp) to NCO.

NCO adds a commission fee to the account balance and begins collection efforts, utilizing mailed notices and phone calls. If the customer pays, NCO wire transfers these funds less their commission fee to Treasury and sends a report identifying the accounts for which payments have been received. Treasury posts the payment amount to the correct GL/Summit accounts and notifies the departments about any payments they have received. SPU Accounts Receivable updates the spreadsheet for accounts in collections to reflect the payments. It should be noted that if the commercial customer wants to re-establish their account, they have to work with both the SPU Contracts unit and the solid waste contractor.

If a commercial customer in collections makes a payment to the contractor, SPU, or the City, this is called a “direct payment” and NCO needs to be notified about them because NCO is entitled to the commission fees on these payments. The contractors notify SPU Accounts Receivable of any direct payments they receive, and SPU Accounts Receivable notifies Treasury, which sends a report to NCO and an invoice to SPU for the amount of NCO’s commission fees. Timely and accurate reporting of direct payments to the collection agency is important to ensure that the agency’s system accurately reflects the customer’s balance.

There are two types of dishonored items received as payments for the Commercial Solid Waste accounts: non-sufficient funds (NSF) checks and credit card charge backs. These dishonored items are fairly rare with these customers, and both are handled by the lockbox vendors utilized by the solid waste contractors. NSF checks and credit card charge backs are reversed out on the customer’s account. Commercial customers are charged a \$20 fee for making a payment with a dishonored item.

Amounts due for Commercial Solid Waste accounts remain in the CSW Receivable account at the detail-level and in Summit at the summary-level, until they are collected or

written off. Currently, it is SPU Accounting's policy to write off account balances that are 1 to 1 ½ delinquent. At that time, accounts are written off from CSW, balance amounts are written off from Summit, and NCO is asked to write off the account on their system, too. Before this write-off occurs, SPU Accounts Receivable prepares a list of accounts they believe are ready to be written off and sends this list to NCO to see if they agree that the accounts are probably uncollectible. This account write-off is conducted annually.

Audit work we performed: We reviewed the functions and processes involved with collections, handling of dishonored items, and account write-offs to determine whether internal controls were adequate. Specifically, we evaluated whether controls would ensure delinquent Commercial Solid Waste accounts are sent to collections timely, properly tracked, worked, supported with response to requests for backup documentation and information, and followed up on to ensure maximum recovery of monies owed. In addition, we determined whether controls ensured customer payments to the collection agency were remitted accurately and timely to SPU and whether collection policies and procedures helped ensure maximum recovery of revenues. And, we evaluated whether controls would ensure dishonored items were handled properly, and bad debts were written off appropriately.

This included tracing a sample of delinquent accounts selected at each contractor's office through the entire collections process and verifying each step in the process was performed accurately, timely, and in compliance with credit laws and regulations. We also checked on the status of a small sample of delinquent commercial accounts that were sent to the City Attorney's Office, and traced the steps performed on a small sample of direct payments. We interviewed contractor personnel and made two on-site visits to each of their offices, interviewed City personnel, reviewed credit and collection regulations, reviewed customer account data on the contractors' systems and on CDS, and observed business processes. We also visited NCO at their branch office in Nevada that handles the City accounts to interview personnel and observe collections operations. We reviewed the account write-offs for 2005 and 2006, and the results of an account aging query from CSW to determine the age of accounts included in the CSW Receivable balance.

Conclusion: We found controls over the collections functions require significant improvements. (Note: Many of the findings for this audit scope area were also noted in the Transfer Stations Revenue Cycle audit report because they impacted both Transfer Station and Commercial Solid Waste customer accounts.) We found that there were weaknesses in submitting accounts for collections in a timely manner, monitoring and tracking accounts in collections, providing adequate support for accounts in collections, properly reporting all direct payments to the collection agency, and maximizing the collections rate. We concluded that policies and procedures governing the remission of customer payments from the collection agency to the City need improvements, and that the policies and procedures related to collection agency commission fees need improvements and re-evaluation. And, we found that SPU is not consistently writing off

Commercial Solid Waste accounts by the time they are 1 1/2 years delinquent, as is the current policy.

It should be noted that many of the issues we observed with the collections processes for the SPU Commercial accounts appear to be City-wide collections issues, and not just issues that relate to SPU. As a result, our office is currently working on a City-wide review of collections with DEA/Treasury and the City Attorney's Office and plan to issue a memorandum on the results of this project soon.

The details of this section's issues are covered below.

Timeliness of Account Turn-In to Collection Agency - Conclusion 7: Delinquent Commercial Solid Waste accounts are not sent to collections timely, and this negatively impacts the collections rate and revenue recoveries. *High risk*

Background

As outlined above, there are several steps that occur before a delinquent SPU Commercial Solid Waste account is sent to the collection agency and several parties are involved in these functions. The procedures are as follows:

- Solid Waste Contractors – suspend service at about the 45-65-day delinquent point, mail a demand letter to the customer at 30-75 days delinquent, inactivate customer account on their systems between 60-90 days delinquent, and return the account to SPU via a report to SPU Accounts Receivable,
- SPU Accounts Receivable – enter account into collections spreadsheet, hold account for 30 days to see if payment is made, forward account to Treasury,
- Treasury – enter account into CDS, send demand letter to customer and wait one month for payment, send account to NCO via ftp.

Issue, Impact, and Recommendation

According to NCO, the most important factor to increase collections recoveries is “recency of the debt” or the timeliness of getting the customer account to the collection agency. Consequently, delinquent Commercial Solid Waste accounts should be sent to NCO as soon as possible, in accordance with SPU policy, to maximize revenue recoveries. Currently, control procedures do not ensure delinquent accounts are sent to collections in a timely manner, and this is negatively impacting the collections rate and revenue recoveries:

- One contractor was not turning over delinquent accounts to SPU Accounts Receivable for collections in a timely manner. Waste Management forwarded 8 of 10 accounts we sampled (or 80%) later than the 90-day delinquent point that is specified in the commercial collection contract.

- It has been SPU Account Receivable's policy to hold Commercial Solid Waste accounts for one month before forwarding them to Treasury for collections. We recommend that this holding period be eliminated and that accounts are forwarded as soon as they are received from the contractors.
- SPU Accounts Receivable is not consistently forwarding Commercial Solid Waste accounts to Treasury for collections in a timely manner as required by SPU policy. Seven of the 17 accounts we sampled (or 41%) were not sent to Treasury in a timely manner, based on the current policy to hold accounts for one month before forwarding them.
- Treasury currently sends a demand letter to the SPU Commercial Solid Waste customers and then holds the account for about a month days before sending them to NCO. This demand letter and holding period are duplicative because the contractors have already sent a demand letter. Current policies and practices would result in commercial accounts getting to the collection agency when they are 6 months or more delinquent (or about 3 to 3 ½ months after the contractor has written off the accounts). Treasury should forward Commercial Solid Waste accounts to the collection agency as soon as they receive them.
- Treasury may need to improve their timeliness with which they send accounts to collections. One account we sampled (or 5%) was held longer than the current procedure allows for before it was sent to the collection agency, and records indicated that two of the 20 accounts sampled (or 10%) were sent to Treasury by SPU Accounts Receivable, but never forwarded to the collection agency.
- The collection agency does not consistently receive accounts from SPU in a timely manner. NCO indicated the accounts tend to be quite old, and the older the debt, the harder it is to collect. By the time NCO receives these accounts, many of the businesses have already ceased operations. According to NCO, SPU accounts are up to 2 years old when they're turned in for collection and most are over 6 months old. An NCO aging report on SPU commercial accounts for the period October 2005 through November 2006 showed that the majority of accounts turned in were 9 months old or more when they were turned in and 33% were over 14 months old. If all steps were carried out in a timely manner and in accordance with current contract terms and SPU/Treasury eliminated their unnecessary demand letter mailings and holding periods, accounts could reach NCO when they were about 3½ to 4½ months delinquent, not 6 months and older as currently occurs.
- Treasury and NCO indicated that a significant percentage of the Commercial Solid Waste accounts that are turned in for collections have actually been paid - about 1/3 according to Treasury. This issue could largely be resolved if SPU

Accounts Receivable verified the status of the account before turning them in to Treasury and/or by forwarding them to Treasury in a more timely manner.

ACTIONS PLANNED OR TAKEN

SPU AR has been working closely with the contractors to improve the handling of delinquent accounts. Starting September 2007, we have been receiving monthly delinquent reports with detail supporting documents from contractors and forward them to Treasury for collection on the same day or as soon as possible. The timely turnover of delinquent accounts to Treasury will eliminate the situation that certain accounts have actually been paid when they are forwarded to collection.

The Fair Debt Collection Act requires the City to provide a final 30-day notification letter prior to assigning the debt to collection. It does not appear the contractor's demand letter meets the same requirement. SPU will work with contractors and Treasury to resolve this issue.

It is the intent of Treasury to turn over accounts to NCO in a timely manner. There are occasions when action may be pending because of the response generated from the 30-day notification letter, however all eligible items for collection will be forwarded to the collection agency.

Monitoring Accounts in Collections - Conclusion 8: Procedures for tracking and monitoring the performance of Commercial Solid Waste accounts in collections require improvement. *High risk*

Background

SPU Commercial Solid Waste accounts and all other City accounts are entered into Treasury's CDS database when they're sent to the collection agency NCO.

Issue, Impact, and Recommendation

SPU should track and monitor the status and performance of the Commercial Solid Waste accounts sent to collections. Currently, this is not happening:

- At the time of our audit, SPU Accounts Receivable indicated that they did not receive any reports from either NCO or Treasury on the status and collections performance of the SPU Solid Waste accounts and they were not monitoring account status or collections rates for their accounts. Accounts Receivable personnel commented that sending accounts to collections was like sending them "into a black hole." However, we learned that NCO produces reports on the City's accounts in collections, broken down by City department and the various account or client codes, in the form of a CD. This NCO report is provided to Treasury monthly and it shows account age, status, and the collection rate for the client code. Treasury provides an excerpt from this report to the departments

upon request. SPU Accounts Receivable should request and review the NCO account status reporting quarterly or semi-annually. In addition, Treasury has committed they will send out the NCO report excerpts to each department with accounts in collections on a semi-annual basis.

- SPU Accounts Receivable does not have lookup access to the CSW system and this impedes their ability to efficiently respond to customer questions related to Commercial Solid Waste accounts in collections.
- SPU Accounts Receivable has not reconciled the Commercial Solid Waste accounts in their collections spreadsheet to what Treasury shows in CDS to what NCO shows in their system. This type of reconciliation should be performed at least annually, as it is important for SPU to periodically verify the amount of their debt that is in collections. A variety of account changes can occur on any of the customer account systems maintained by SPU, the contractors or NCO, including balance changes, debt cancellations, and account updates. Periodic reconciliations are important to ensure that NCO is working on collecting a valid debt and account balance and that SPU and the solid waste contractors have accurate account information. It may be difficult for SPU to reconcile to NCO's system because the collections fee/commission is not recorded in CDS, CSW, or SPU Accounts Receivable's collections spreadsheet, although it is added to the customer's balance in NCO's system. NCO's Account Inventory report may require a change to break out the commission fee from the customer's principal balance.

ACTIONS PLANNED OR TAKEN

Treasury now provides Accounts Receivable a report that shows the accounts that Treasury has in collections for SPU. This report must be manually reconciled to Accounts Receivable's data. Accounts Receivable is now looking at the report and trying to find an efficient way to reconcile the data. Treasury has placed a request to IT to have this report placed into an Excel format to make the reconciliation easier. To have this report placed into an Excel format would greatly speed up the reconciliation process. Once AR is able to reconcile to Treasury's data, Treasury will begin to reconcile to the CD that NCO provides.

Accounts Receivable will continue to work with the contractors to have them send us all the information for the delinquent accounts so that we can respond to customer questions.

SPU/City/Contractor Support for Collections Effort - Conclusion 9: The collection agency does not receive the support and documentation it needs from the solid waste contractors, SPU, and Treasury to help maximize revenue recoveries. *High risk*

Background

Regulations governing the collections industry require collection agencies to provide a breakdown of the customer's balance in their "notice to the customer" or account

statement, and specify that the balance should be separated out into principal, interest, and any other fees. In addition, if a SPU customer in collections challenges a collection amount or requests “validation of the debt,” then NCO needs to be able to provide the customer a copy of the itemized customer statement from SPU, or in the case of a Commercial Solid Waste customer, a copy of the customer’s statement from the contractor. The Fair Debt Collections Protection Act (FDCPA) mandates that collection agencies provide customers seeking validation of their debt with itemized statements, even if this has been supplied to them previously. In the case of the SPU Commercial Solid Waste accounts, NCO has to request this documentation from Treasury, which requests it from SPU Accounts Receivable, which requests it from the contractors. If the proper documents aren’t provided to NCO within a fairly short period, then the debt is not “validated” according to collections regulations and NCO has to cancel the account, stop collections activities on it, and cannot add negative information to the customer’s credit report. By company policy, NCO is not allowed to contact the consumer again, until they receive a response from the client (i.e., SPU in this case). NCO indicated that consumers in collections in current times tend to be very knowledgeable about collections laws and NCO estimated that about 75% of them ask for debt validation.

Issue, Impact, and Recommendation

Timely and adequate support should be provided by SPU and the City for any NCO requests for backup documentation and information to help maximize revenue recovery for the Commercial Solid Waste accounts in collections. Currently, this is not occurring.

- NCO is not providing the itemization or breakdown of the balance to the SPU Commercial Solid Waste customers in collections because this information isn’t provided to them by the City/SPU. This is because it’s not provided to SPU by the contractors. To be fully compliant with credit regulations, NCO should provide an itemization of the customer’s balance separated out into principal, interest, and any other fees.
- NCO does not receive all of the information it needs to work the Commercial Solid Waste accounts. NCO needs the name of the contractor (Allied Waste/Rabanco or Waste Management) for the account, the service date of the activity for which the debt was incurred, the date the debt became delinquent, and the amount of the debt “principal” versus the amount of the interest fees. Currently NCO does not receive all of this in a legible and accurate condition.
- NCO personnel indicated that when they request backup documentation from Treasury and/or SPU due to a customer’s request for validation of the debt, it is “hit or miss” whether they receive a response, or that they often receive a response with incorrect information. NCO said the backup they receive for Allied Waste/Rabanco accounts are illegible screen prints, and the backup invoices/screen prints for Waste Management accounts are legible but the dollar amounts do not match the amounts of the account balances in collections. NCO indicated this is a very significant issue and that more often than not, they end up having to write off the accounts. This situation results in reduced revenue

recoveries for SPU, reduced collections commissions for NCO (and undoubtedly reduced efforts on their part), and a lot of wasted time on NCO's part (and possibly the City's too). We recommend that the contractors submit copies of customer statements at the time they turn in accounts to SPU Accounts Receivable for collections. SPU and Treasury may also want to consider whether it would be helpful for NCO to work directly with SPU Accounts Receivable when they have questions on a SPU commercial account, instead of working through Treasury, since this delays the process by adding another process layer.

ACTIONS PLANNED OR TAKEN

See Conclusion #5 and # 7: Accounts Receivable will continue to work with Treasury, NCO and the contractors to address any concerns that may arise.

Collections Rate Performance - Conclusion 10: The City's collection procedures require improvements in order to ensure the collections rate and revenue recoveries are maximized for Commercial Solid Waste accounts. High risk

Background

While collections rates vary substantially based on the nature and type of debt, NCO stated the industry standard for "regular third party debt" generally averages between 7% and 13%. Critical factors that impact collections rate performance include the age of the debt (debt recency) and the collection agency's ability to respond in a timely manner to customer requests for debt validation with proper backup documentation.

Issue, Impact, and Recommendation

NCO's collections rate for SPU's Commercial Solid Waste accounts should meet or exceed the industry standard for collections of 7%-13%. Currently, this is not happening with SPU's Commercial Solid waste accounts.

- NCO's collection rate for SPU Commercial Solid Waste accounts was about 4.8% as of the end of 2006. According to NCO officials, this rate is "not very good" for the collections industry, in general, or compared to NCO's collection rates for their other utility clients. NCO has several utility clients, but SPU is the only government-owned utility; the others are for-profit utilities. We were unable to find any statistics for the utility industry to benchmark with SPU's collection rate. It should be noted that SPU currently does not collect the same level of information about their customers that for-profit utilities do, including driver's license and social security numbers, and this additional information is very helpful to collectors for customer identification purposes and for tracing individuals.
- Currently, it will be difficult to impossible to measure NCO's collections performance with the SPU Commercial Solid Waste accounts until SPU and Treasury address the issues they have control of that are negatively impacting collections, specifically timeliness of account turn-in and provision of adequate

back-up documentation and information to NCO when customers challenge or request debt validation. Once these issues have been addressed, we recommend that SPU and Treasury measure NCO's collections rate performance against the industry standard.

ACTIONS PLANNED OR TAKEN

Starting September 2007, SPU Accounts Receivable has been receiving detail delinquent reports from both commercial solid waste contractors monthly. Our current practice is to forward the delinquent accounts to Treasury for collection on the same day or as soon as possible. We will work with Treasury to ensure these accounts are passed on to NCO timely and start measuring NCO's collection rate performance in the spring of 2008.

Collection Agency Remission of Customer Payments - Conclusion 11: Policies and procedures governing the remission of customer payments to the collection agency need improvements. *High risk*

Background

SPU and the solid waste contractors direct SPU Commercial Solid Waste customers with accounts in collections to send their payments to NCO. When NCO receives customer payments on SPU and other City accounts, they update the customer record on their system to reflect the payments, wire transfer the funds monthly to the City's Treasury unit less the amount of their commission fees, and send a report identifying the accounts with payments to the Collections unit in Treasury. Treasury posts the payments to the correct GL/Summit accounts and notifies SPU Accounts Receivable of the Commercial Solid Waste payments received. SPU Accounts Receivable updates their collections spreadsheet to reflect the payments.

Issue, Impact, and Recommendation

Commercial Solid Waste customer payments made to NCO should be remitted to SPU accurately and timely to maximize the City's cash flow and ensure customer account information is as up-to-date as possible. While we did not note any problems with the accuracy of customer payments remitted, there are issues with timeliness:

- NCO is generally adhering to the City contract requirement that specifies that customer payments made by check are to be reported and remitted by NCO 30 days after they're received, to allow for time to determine whether check payments will clear. NCO officials indicated that this is "extremely unusual" and that most of their clients have all payments remitted immediately and any NSF payments are debited against the account upon notification from the bank. The current situation causes unnecessary delays in keeping SPU customer account records up-to-date and it negatively impacts SPU's (and the City's) cash flow. In contrast, the collection agency for the Seattle Municipal Court holds check payments for 14 days before remitting them to the Court. We recommend that the City's collection contract terms and operating procedures be aligned with standard business practices.

- During audit fieldwork, we noted that NCO sometimes holds checks longer than 30 days. We saw an example of a payment received by NCO that wasn't remitted to the City until over two months later.
- NCO wire transfers all customer payments they have collected to the City only once a month, and the terms of the City's contract with NCO do not address payment remission frequency. This is not a reasonable or standard collections industry practice and it negatively impacts SPU's and the City's cash flow. In contrast, the collection agency for the Seattle Municipal Court remits payments daily. SPU's customer collection payments for a one month do not represent a substantial amount of money; however, monthly payment remittances in 2006 for all of the City's accounts in collections sometimes exceeded \$25,000. We recommend that the City's collections contract with NCO be revised to address payment remission frequency and specify that NCO remit payments at least weekly. The current contract doesn't expire for another two years, so Treasury will have to weigh the cost and benefits of pursuing a contract amendment before that time.

ACTIONS PLANNED OR TAKEN

When the City looks to negotiate a new collections contract, all of the cash flow terms and policies will be taken into consideration.

Collection Agency Commission Fees - Conclusion 12: Policies and procedures governing collection agency commission fees need improvement. *High risk*

Background

When NCO receives a new collections account from a SPU Commercial Solid Waste customer or any other City account, their contract permits them to add a commission fee to the customer's balance of 21% for debts up to \$100 and 17% for debts over \$100. Then, when the customer makes a payment, NCO remits the amount of the payment less their commission fee to the City, thereby ensuring NCO receives their payment for services, even if the customer payment was not sufficient to cover both the principal amount owed to the City and the commission fee owed to NCO. NCO sends a monthly statement to Treasury that shows the gross amount of customer payments by account, the commission amount deducted, and the net amount remitted to the City. If collection customers make payments to SPU, the solid waste contractors, or the City instead of to NCO, this is known as a direct payment. Treasury notifies NCO about direct payments, and NCO invoices Treasury for the amount of the commission fees. Treasury sends these commission fee invoices to the City departments that "own" the accounts and the departments are responsible for paying these invoices.

Issue, Impact, and Recommendation

Fees for collection services should be reasonable and in line with standard industry practices, charged accurately to customer accounts, and properly reviewed and approved.

Currently, there are some issues with the policies and procedures relating to collection commission fee charges for the City's accounts.

- The City's method of handling the commission fee charges for NCO's services is unusual and is negatively impacting the City's revenue recoveries. NCO adds the collection fee to the customer's balance when they receive the account. NCO deducts their commission fee amount from what the customer pays, so if the customer doesn't pay the entire balance, the City does not receive the full value of the debt principal owed. It is fairly common for customers to underpay by the amount of the collection agency commission because it is a separate charge noted on the customer's statement from the collection agency and many people do not want to pay it. And, since NCO has already collected their fee on these accounts and the NCO collectors are paid on a commission-basis, they may not be motivated to pursue collections efforts on the remaining balances for these customers. The City's current procedure also causes problems when customers make direct payment to the City or the solid waste contractors, because the amount of the collection fee is not visible to City department or contractor personnel accepting these payments since it's applied by NCO and neither the contractors' nor the City's systems are updated to reflect the fee still owed to NCO.

A more standard method for handling collection fees and agency commissions is for the client (the City) to add the collections fee to the customer's balance before submitting the account to the agency, and for the agency to add their own commission and retain this amount from the customer payments. Treasury indicated the collection fee could possibly be applied in CDS before submitting the accounts to NCO, but noted that the contractors' or source systems wouldn't reflect it so there would still be a problem in the case of direct payments. Treasury also noted that the City has historically taken a "softer" approach towards collections than would be normal in a for-profit enterprise and has opted not to add a collection fee on top of the collection agency commission fee. We recommend that Treasury re-evaluate the current collection/commission fee structure and policies, consider how they compare to other municipalities, and possibly discuss this area with NCO to determine if it would be beneficial for the City to make any changes.

- Treasury provides SPU with NCO's invoices for commission fees for customer payments collected whenever payments are made for Commercial Solid Waste accounts in collections. However, SPU is not performing any type of reconciliation or verification of the accuracy of NCO's commission fees charged and deducted from the customer payment amounts remitted. This should always be done to ensure NCO is charging SPU accurately. While most of the commission fee charges we sampled appeared to be accurate and in accordance with the contract terms, we noted two exceptions:

- NCO charged 20.5% for a Commercial Solid Waste customer on the October 2006 statement when it should have charged 17% because the debt was over \$100.
- NCO charged 7.6% for a Commercial Solid Waste customer on the November 2006 statement and they should have been charged 17%.

The differences noted were minor but lend weight to the importance of reconciling NCO's commission charges.

ACTIONS PLANNED OR TAKEN

When the City looks to negotiate a new collections contract, all of the cash flow terms and policies will be taken into consideration. This will include a review of the placement of a collection fee with each billing department instead of after assignment to the collection agency.

SPU Accounts Receivable will verify the calculation of NCO commission fees according to the contract terms when NCO's invoices for commission fees are received from Treasury. We will start this practice in the spring of 2008.

Direct Payments - Conclusion 13: Controls related to direct payments (i.e., customer payments made directly to the contractors or the City) could be improved. *High risk*

Background

If a commercial customer with an account in collections makes a payment to the contractor, SPU or the City, this is considered a "direct payment" and NCO needs to be notified about these because NCO is entitled to the commission fee on these payments. The contractors notify SPU Accounts Receivable with an email of any direct payments they receive, SPU Accounts Receivable notifies Treasury, and Treasury sends a report to NCO and an invoice to SPU for the amount of NCO's commission fee. Timely and accurate reporting of direct payments to NCO is important to ensure NCO's system accurately reflects the SPU customer balances and that NCO is not pursuing collections on debts that have been paid.

Issue, Impact, and Recommendation

Timely and accurate reporting of direct payments to NCO is important to ensure NCO's system accurately reflects SPU customer balances and NCO is not pursuing collections on debts that have been paid, which is not allowed per regulations governing the collections industry. Currently, some improvements are needed in this area:

- Both contractors have procedures in place to report direct payments. However, SPU Accounts Receivable and NCO indicated that all direct payments are not always reported to SPU. If direct payments aren't reported, then NCO is pursuing collections on an account that has been paid or they are pursuing it for the incorrect balance, which puts NCO in a non-compliant situation with credit

regulations. In addition, if direct payments are not accurately reported to NCO, then NCO is not properly compensated for their commission percentage for these customer payments.

- If a customer in collections makes a direct payment to the contractor in order to re-open their Commercial Solid Waste account, the contractors have no way of knowing if the customer has any amount due to NCO for unpaid commission fees, since this amount is not reflected in the contractors' customer accounting systems. Before allowing an account to be re-established, the contractors should verify with SPU Accounts Receivable or Treasury whether there are any remaining amounts owed.

ACTIONS PLANNED OR TAKEN

SPU will reinforce to the contractors the importance of their requirement to report all customer payments they receive for accounts in collections.

SPU Accounts Receivable will work with the contractors to establish a process that when an inactive account customer requests to reopen the account, the contractor will communicate with

SPU Accounts Receivable to verify all account balance and fees (including NCO commission fees) have been paid before the account is reopened.

Customer Account Write-Offs - Conclusion 14: SPU is not consistently writing off Commercial solid waste accounts by the time they are one-and-a-half years delinquent, as is the current policy. Medium risk

Background

Currently, it is SPU Accounting's policy to write off Commercial Solid Waste account balances when they are between one and one-and-a-half years delinquent. The account write-off process is conducted annually. Before the write-off occurs, SPU Accounts Receivable prepares a list of accounts they believe are ready to be written off and sends this list to NCO to see if they agree these accounts are most likely uncollectible. Then, accounts are written off from CSW and balance amounts are written off from Summit.

Issue, Impact, and Recommendation

The CSW Accounts Receivable balance should accurately reflect accounts and monies owed for SPU Commercial Solid Waste accounts that are reasonably believed to be realizable or collectable. Currently, SPU is not consistently writing off commercial accounts by the time they are one-and-a-half years delinquent, as required by current policy. For the write-off for 2006, we noted that while most of the accounts written off were under two years old, there were 48 accounts over 800 days delinquent (or 2 ½ years), representing about \$17,000, and there were some accounts that were up to 1,100 days delinquent (or 3 years).

ACTIONS PLANNED OR TAKEN

SPU's current practice is to write off accounts that are more than one year old. We will provide instruction and training to staff to follow this guideline.

VI. SOLID WASTE FUND ACCOUNTING – REVENUES AND RECEIVABLES

- Controls need improvement -

Background

Commercial Solid Waste revenues and receivables are accounted for separately within SPU's Solid Waste Fund from Residential Solid Waste and Transfer Station revenues and receivables. Revenues and receivables are also tracked and accounted for separately by solid waste contractor. There is a SPU Principal Fund Accountant who has ultimate responsibility for all entries made to the Solid Waste Fund. SPU fund balances are monitored by SPU and Department of Finance management, and each fund is audited annually as part of the external financial audit performed by Moss Adams.

The CSW database serves as the sub-ledger system for the Commercial Solid Waste accounts, and accounting entries at the summarized level are posted to Summit, which is the City's General Ledger. No entries are made to CCSS/Banner for the Commercial Solid Waste accounts but CCSS/Banner serves as the sub-ledger system for the Residential Solid Waste accounts. Allied Waste/Rabanco and Waste Management download the billing data for the SPU commercial customers from their systems (InfoPro and MAS, respectively) during the first week of the month. The Solid Waste Fund Accountant books the billed amounts to the Commercial Solid Waste (CSW) Revenue and Receivable accounts in Summit. Then, when SPU commercial customer payments are wire-transferred from the contractors to City Treasury, Treasury posts these monies to the CRS (Cash Receipting System) and to Summit as a credit to the CSW Receivable accounts and a debit to Cash. Any interest fees paid are booked to CSW Interest Revenue. SPU Accounts Receivable unit logs the incoming wire transfers in a spreadsheet and compares them to the monthly email/report from the contractors listing the wire transfers they sent to SPU. Accounts Receivable researches and resolves any variances between the contractors' reports and wire transfers received. In addition, the Solid Waste Fund Accountant monitors the balances of the CSW Revenue accounts and reconciles them periodically. As of year-end 2006, there was a total balance of about \$5.2 million in the CSW Receivable account. Commercial Solid Waste revenues totaled about \$38 million in 2006 and associated interest revenues were about \$76,000.

The Solid Waste Fund Accountant annually books a reserve for Commercial Solid Waste bad debts for each contractor to CSW Allowance for Doubtful Accounts in Summit, to account for the commercial receivables that will not be collected.

Audit work we performed: We reviewed the functions involving Solid Waste Fund accounting for revenues and receivables to determine whether internal controls were adequate. Specifically, we evaluated whether controls would ensure that the accounting

for Commercial Solid Waste revenues and receivables is accurate, and properly reviewed and monitored. This included performing audit work to verify that account reconciliations were performed accurately and timely, reconciliations were approved by management, significant variances were properly researched and resolved, account balances were properly monitored by management, and losses from bad debt were reserved for in a reasonable manner. We interviewed staff on these functions, reviewed account balances and reconciliations, and reviewed the calculations for bad debt reserves for 2005 and 2006 and compared them to the actual CSW Receivable write-offs for these years.

Conclusion: Overall, we found controls over these functions need some improvement. We concluded that CSW revenues and receivables are accurately and properly accounted for, but we noted that the CSW Revenue accounts were not reconciled frequently enough to provide for adequate control. Details on this issue are covered below.

Reconciliation of Receivable Accounts - Conclusion 15: The Commercial Solid Waste Receivable accounts were not being reconciled frequently enough to provide for adequate control. Medium risk

Background

WM sends a monthly report to SPU Accounting on commercial receivables, and AW sends a monthly Trial Balance report on commercial receivables. The Solid Waste Fund Accountant maintains a tracking spreadsheet for Commercial Solid Waste Accounts Receivable that he updates monthly and uses to monitor the account balances. In addition to this spreadsheet tool, there are detailed reconciliations performed of the receivables for AW and WM. Within these detailed reconciliations, any variance or reconciling item is documented. For example, an adjustment is always necessary on the WM receivable reconciliation to account for the “co-mingled” accounts, which are customers who have both garbage and construction waste (CDL) picked up by WM. CDL is not part of the SPU commercial collection contract but WM bills the customer for it along with garbage collection charges on a combined customer statement, so payments for CDL charges need to be included as an adjustment on the reconciliation.

Issue, Impact, and Recommendation

Because of the large amount of money that flows through the CSW Receivable accounts, these accounts should be reconciled to the GL/Summit monthly and all significant reconciling variances should be researched and resolved. These reconciliations should be reviewed and approved by management. Monthly reconciliations of key accounts help ensure management and accounting staff spot any problems as soon as possible. At the time audit fieldwork was conducted, SPU Accounting was only reconciling the Commercial Solid Waste Receivable accounts at year-end, due to limited Accounting staff resources. However, Accounting was maintaining and updating the receivable spreadsheet monthly and this served as a partial compensating control. The year-end reconciliation practice was approved by SPU’s prior external audit firm. We recommended the accounts be reconciled monthly. As of 2007, SPU Accounting began

reconciling the CSW Receivable accounts monthly, but they were four months behind in doing so when we last checked.

ACTIONS PLANNED OR TAKEN

SPU agrees with this recommendation and will begin reconciling commercial solid waste receivables to the GL/Summit on a monthly basis beginning in 2008. All significant reconciling variances will be researched and resolved. These reconciliations will be reviewed and approved by management.

VII. INFORMATION TECHNOLOGY - *Controls are adequate overall*

Background: The SPU commercial solid waste customer accounts are tracked by the two solid waste contractors in their customer accounting systems, InfoPro for AW and MAS for WM, and then updated account data is downloaded monthly to SPU's Commercial Solid Waste (CSW) database system. CSW has customer account-level data that includes information on charges and payments for the current month, and the 30-day and 60-day balances, if applicable. CSW has monthly data going back to April 2001. SPU is currently developing a Solid Waste Integrated Database (SWIDI), to serve as a repository of solid waste data related to SPU's primary solid waste services lines - residential, commercial, and transfer stations.

The SPU Data Analysis unit oversees the contractor download process and monitors the data in CSW. Before AW's and WM's data is loaded into CSW, Data Analysis runs data validation checks on it, fixes any errors found, and then loads it to the Oracle table in CSW. All data loaded into CSW goes through automated data validation procedures to help ensure its integrity, including the transfer tonnage data loaded into CSW. All data is reviewed for missing fields, checked to see if residential garbage trips were mixed up with commercial trips, checked for duplicate trip numbers within a certain timeframe (e.g., on the same day), etc. In addition, the detailed trip-level data files are compared to the summary-level file of invoiced charges to verify that they match. In addition to the automated data checks, the SPU Data Analysis unit and other solid waste data users are constantly looking for anything that looks unusual with the data as they are using it. If anything is noted, it's investigated. The new SWIDI Solid Waste Integrated database will further automate many of these data review steps that look for potential invalid data.

The server running CSW, along with all SPU servers located downtown at SPU headquarters are backed up nightly. Back-ups are stored for 45 days, and the monthly back-up files are stored off-site at a records retention facility for three years. The previous procedure was to send back-up files to the records retention facility weekly, but now the files are backed up with a hard-drive system (i.e., a redundant replication box) located at SPU's Cedar Falls watershed location near North Bend and back-up files are sent monthly to the offsite records location.

Audit work we performed: We reviewed the information technology functions involved with recording commercial solid waste data. Specifically, we evaluated whether controls would ensure information systems used for customer account functions were secure, accurate, effective, and properly controlled. This included performing audit work to verify access rights were properly assigned in a secure manner using the principle of “least privileges,” adequate audit trails were in place, monitoring of exception-type system activity occurred, adequate procedures were in place to ensure complete system backups occurred daily, and proper change control procedures were followed for any systems changes. We interviewed both SPU and vendor staff on these functions, and reviewed system operations and system monitoring tools, and system access lists.

Conclusion: Overall, we found that proper controls were in place and functioning adequately. We did not note any control weaknesses within this area.

VIII. VENDOR BILLING FOR SERVICES, CONTRACTS, AND PERFORMANCE - *Controls need improvements*

Background: SPU contracts with several vendors to perform commercial waste collection and other solid waste services. SPU currently contracts with Allied Waste/Rabanco (AW) and Waste Management (WM) to collect commercial customers’ garbage and yard and food waste. In addition, SPU contracts with WM and AW to handle the billing administration functions for commercial customers. All of these solid waste-related services are covered as part of SPU’s commercial solid waste collection contracts. The commercial collection contract expires in 2009 and SPU is currently working on negotiating the new contracts. SPU also contracts with AW and WM to use their transfer stations for waste transfer services during the hours the SPU transfer stations are closed. SPU contracts with AW for recycling processing services and the terms of this arrangement are currently included within the residential solid waste collection contract, which also expires in 2009 and is currently in negotiation. SPU contracts with Cedar Grove Composting for yard waste and food waste processing services and this contract expires in March 2008, but may be extended for two additional years. SPU contracts with WM for “long haul and disposal” services, which includes transporting SPU customer waste to WM’s landfill in eastern Oregon and permanently disposing of it there. The long haul contract expires in 2028, with an option for either party to terminate the contract in 2014.

Waste Collection and Billing Administration

AW and WM collect garbage for SPU’s commercial solid waste customers. Currently, WM collects waste from the commercial customers in the northern half of the City and AW collects it from customers in the southern half. The type of waste collected from commercial customers includes regular garbage, as well as food and yard/green waste for those that subscribe to that optional service. The contractors are responsible for collecting waste and delivering it to a SPU or contractor-owned transfer station.

While SPU handles the billing and customer service functions for the residential solid waste customers, SPU outsources these functions to AW and WM for its commercial customers. The contractors are responsible for setting up new SPU commercial accounts, tracking services provided, billing customers, processing customer payments, following up on mildly delinquent accounts, and handling customer service inquiries and contacts. The SPU Contracts unit serves as the SPU-liaison with the contractors, and they get involved in customer issues that are escalated to them.

Transfer Services

SPU's waste transfer services involve receiving waste from contractor garbage collection trucks at a transfer station, compacting the waste into containers, and delivering the containers by truck to the Argo Union Pacific rail yard in Seattle, where it is shipped to a landfill site in Oregon. The two SPU transfer stations provide the majority of the waste transfer services needed for SPU's residential, commercial, and transfer station self-haul customers. The cost of transfer services for waste collected as part of the SPU Solid Waste Collection contracts is built into the contracted rates. SPU also contracts with AW and to a lesser degree with WM to provide "overflow" transfer services at AW's 3rd and Lander transfer station and WM's Eastmont station whenever the SPU transfer stations are closed, which is generally early in the morning or at night. SPU pays AW and WM a per-ton negotiated rate for these transfer services.

Recycling Processing

SPU contracts with AW to process the recycling waste (MRW) collected from SPU's residential solid waste customers. SPU pays a per-ton rate for these processing services. Recycling waste is collected by both AW and WM and delivered directly to AW's recycling plant at 3rd and Lander. AW sorts the MRW waste by commodity type and sells it to various parties, with much of it going to Asia. SPU receives a "recycling commodity credit" from AW if market prices are higher than they were when the terms of the original agreement were put in place, which has been the situation for several years. The terms of the agreement and the rates for recycling processing services and the recycling commodity credit are currently contained within the residential solid waste collection contract. The SPU transfer stations sell the recycling waste they collect from the self-haul customers directly to various parties.

Compostable Waste Processing

Cedar Grove Composting (CGC) processes all of the yard and food waste collected from SPU's Residential and Commercial customers. Currently, the majority of this "compostable" or "green" waste is collected from SPU's residential customers. AW and WM collect the waste and deliver it to the SPU North Transfer Station or to AW's 3rd and Lander station. From there, the green waste is delivered by truck by SPU or AW to CGC's Maple Valley facility. CGC charges SPU for processing the waste based on a flat rate per ton delivered.

Long Haul and Disposal

SPU contracts with Washington Waste Systems (WWS), which is owned by WM for long haul and disposal services for all SPU garbage (or MSW) waste. These services

include loading containers of SPU waste onto trains, transporting the waste by railcar to WWS's Columbia Ridge Landfill (CRL) in Arlington, Oregon, and permanently disposing of the waste at CRL. SPU and AW deliver SPU waste to the Union Pacific Argo rail yard. While WWS manages and oversees the waste loading and train transport process, Union Pacific actually performs these functions. WWS maintains a set of scales at Argo dedicated to handling WM's loads, which primarily consist of SPU waste loads. SPU pays WWS a per-ton rate for these services and the terms are covered in the separate long haul and disposal contract. There is a SPU "garbage train" departing six days per week from Seattle to CRL, with 80-120 containers on each train.

Audit work we performed: We reviewed vendor performance, contracts, and invoicing for the services outsourced by SPU for commercial solid waste and some aspects of the residential solid waste accounts. Specifically, we evaluated whether controls would ensure the contractors and vendors perform waste collection, transfer services, recycling waste processing, compostable waste processing, transportation and long-term disposal, and billing administration and customer service functions adequately and in accordance with contract terms. We also determined whether procedures are adequate to ensure invoiced charges for services are accurate and properly reviewed. This audit work included:

- Reviewing the terms of each solid waste service contract,
- Verifying adequate customer service channels were in place and customer complaints were handled appropriately,
- Vendors performed adequately for contracted services,
- Vendor charges for each outsourced solid waste service were accurate, and per-ton charges were based on accurate scales and proper scale house procedures,
- Vendor invoices were properly supported, reviewed, verified, and approved before payment,
- Annual consumer price index (CPI) adjustments were calculated and applied properly to vendor rates, per contract terms,
- Vendors were properly charged penalty fees or liquidated damages for various service failures, in accordance with contract terms,
- The truck turnaround time credit/penalty and average container weight credit were calculated and applied to invoice charges accurately, per the long haul and disposal contract terms,
- SPU did not pay for services related to "non-contract" waste,
- The monthly recycling commodity credit was calculated accurately by SPU, the proper credit was received from AW, and credits were posted accurately to the City's General Ledger (GL),
- The transactions for the sale of SPU transfer station recycling waste were properly handled, proceeds were accurately deposited, and amounts were accurately posted to the City's GL.

We tested samples of vendor invoices for each type of solid waste service and verified the accuracy of calculations and charges. We made on-site visits to AW's and WM's regional administrative offices, the Argo rail yard, AW's 3rd and Lander transfer station

and recycling plant, CGC's composting facility in Maple Valley and corporate office in Tukwila, and the CRL landfill in Oregon. We observed operations at each SPU and vendor location we visited, interviewed vendor and SPU personnel involved in these functions, observed invoice review and payment practices, and reviewed systems data and hard-copy documentation.

Conclusion: We found that controls over functions related to outsourced solid waste functions need improvements, although many of the processes in this area are well-controlled. Control procedures are not adequate to ensure that SPU is charged accurately by CGC for compostable waste processing services, due to CGC's scale house procedures, and improvements are needed in SPU's review of CGC invoices. We concluded that tonnage charges for solid waste transfer services are not properly verified. Recycling tonnage numbers used for invoicing charges for recycling processing services and calculating the recycling commodity credit are not properly verified. While all of the critical scales involved in the SPU solid waste processes are regularly tested, none of them have been licensed with and tested by the State of Washington Weights and Measures unit within the last several years. Contractor reporting provided to SPU on customer complaints/issues needs to be improved. SPU is not assessing penalties or liquidated damages for the various service failures, such as missed pick-ups, as is required by contract terms, except for noise violations. Details on these issues are discussed below.

Yard and Food Waste Processing Tonnage Charges - Conclusion 16: Controls are not adequate to ensure SPU is charged accurately for yard and food waste processing tonnage. *High risk*

Background

SPU contracts with Cedar Grove Composting (CGC) to process customer yard and food waste (also called green waste or compostable waste). The solid waste collection contractors pick up the green waste from the SPU residential and commercial customers and take it to either the SPU North Transfer Station or AW's 3rd and Lander transfer station. The transfer stations compact the green waste into containers and then take it by truck to CGC's composting facility in Maple Valley. CGC also has a composting facility in Everett, but only a very small amount of SPU waste is taken to that location. SPU pays CGC a flat rate per ton to receive and process the green waste into composting materials that CGC sells to consumers. Any "contaminated waste" that SPU delivers in the loads of green waste are sent back to SPU. SPU receives a credit from CGC at a set rate per ton for contaminants only if the total tonnage exceeds 1,000 tons for the year. The terms relating to contaminants are covered in SPU's contract with CGC.

CGC relies on the tonnage figures recorded at AW's transfer station for the net weights of the inbound green waste loads AW delivers to CGC. AW provides these tonnage numbers to CGC, which uses these tonnage figures to invoice SPU for the loads that came from AW's station. However, because the SPU transfer stations do not have scales

that are large enough to accurately weigh a truck plus a container of green waste, the SPU trucks are weighed at the CGC facility and the net weights recorded at CGC are used to invoice SPU for the loads from the SPU North Station.

The CGC scale house operation at Maple Valley involves only one scale that handles both inbound and outbound traffic, resulting in trucks having to drive around the scale house after dumping and passing over the same scale a second time. It should be noted that all the other scale houses used for SPU's solid waste operations – SPU's transfer stations, AW's and WM's transfer stations, and the Argo rail yard – utilize two scales, one for inbound traffic, and one for outbound traffic. While visiting CGC in Maple Valley and observing the scale house process, we noted that the inbound truck weight is manually entered into CGC's scale house system by a clerk, and the outbound truck weight is automatically fed from the scale to the system. CGC indicated their system and scale set-up did not allow for automatic weight feeds for both inbound and outbound weights. We noted that this scale and weighing procedure applies to all of CGC's customers at Maple Valley, not just SPU trucks. The CGC system generates a weight ticket for each truck load or trip, and CGC sends a copy of the tickets for the SPU loads to the SPU Contracts unit, along with the monthly invoice.

Issue, Impact, and Recommendation

Controls should be adequate to ensure the tonnage figures used to prepare SPU's invoices for yard and food waste processing services are accurate. Currently, this is not the case for the loads delivered by SPU to CGC because CGC is utilizing only one scale at their scale house and inbound weights are manually entered into their system. Truck weights could hypothetically be entered incorrectly or inflated and it's not likely that this would be detected. A SPU driver may know the outbound or empty weight of his/her truck, but would not know the weight of their truck plus the waste load. In addition, there are no back-end or detective controls in place that would catch this type of error. The truck weight tickets would always match the weight data in CGC's system, so a review of weight tickets would not spot any potential errors of this type. The ideal resolution to this situation would be the installation of a second scale at CGC's scale house, but if that is not possible or practical, we recommend that the automated weight feed from the scale should occur for the inbound weight, not the outbound weight. SPU management indicated that if only one scale were utilized, this would be the normal industry practice.

ACTIONS PLANNED OR TAKEN

Cedar Grove, the composting vendor, implemented automatic scale data entry in December 2007 as recommended. Manual entry was eliminated.

Review and Approval of Yard Waste Processing Services Invoices - Conclusion 17: Improved procedures are needed for the review and approval of invoices for yard and food waste processing services. Medium risk

Background

CGC bills SPU monthly and sends the invoices, with the weight tickets for SPU-delivered loads, to the SPU Contracts unit. The SPU Contracts unit accountant is responsible for reviewing the invoice and charges, researching and resolving any potential discrepancies noted, and passing invoices to the Solid Waste Contracts Manager for payment approval. (Invoice payment is handled by SPU Accounts Payable.) CGC also sends a monthly summary report of contaminants it received to SPU, and the SPU Contracts unit maintains a contaminants spreadsheet to track annual tonnage. SPU Contracts receives a monthly report from AW on the tonnage of SPU green waste AW delivered to CGC from their transfer station and this tonnage figure is verified against the CGC-invoiced tonnage. SPU verifies that CGC is not charging SPU for any of the non-contract truckloads delivered by AW, since AW delivers this waste to CGC as well, and CGC deducts it from SPU's invoiced charges. There is also a line item on the CGC invoice for commercial food waste (CFW) tonnage and SPU verifies this tonnage with AW and WM.

Issue, Impact, and Recommendation

Invoices for CGC's yard and food waste processing services, as well as invoices for all solid waste services, should be properly verified and approved before payment, to help ensure charges are accurate. We found that some improvements are needed over the review of CGC invoices:

- The SPU Solid Waste Contracts unit occasionally checks some SPU truck trip weight tickets against the CGC invoice, but this is done very irregularly and may only happen a couple times per year. This should be done more regularly.
- SPU occasionally verifies that CGC invoices are summed accurately, but not always. We recommend that this be done monthly.
- SPU is not currently reviewing truckload tonnage figures for reasonableness. Truckload weights tend to be fairly consistent with the exception of some light loads at the end of the day, so this review could easily be done. We recommend that this be done monthly, or better yet, that an automated data query be established to look for abnormal tonnage or duplicate truckloads.

ACTIONS PLANNED OR TAKEN

SPU created a monthly query of scale data in December 2007 to confirm monthly invoice totals; check for duplicate entries; and check for outliers. This query is run and reviewed monthly (as of December 2007).

SPU began routinely checking scale tickets against monthly invoices in January 2008.

Transfer Services Invoicing - Conclusion 18: Controls over the verification of tonnage invoiced for transfer services could be strengthened. *High risk*

Background

While the SPU transfer stations receive the majority of the solid waste collected from SPU's customers, SPU also contracts with AW and WM to provide transfer services for hours when the SPU stations are closed and pays a negotiated rate per ton for these services. AW's 3rd and Lander transfer station provides the vast majority of these outsourced transfer services for SPU, but WM's Eastmont transfer station also provides a small amount of services. SPU guarantees a certain number of transfer tons to AW annually and negotiates a rate for these tons that is substantially lower than the rate that's paid for any tonnage exceeding the guaranteed number. The SPU Contracts unit uses a spreadsheet to track the annual transfer tonnage handled by AW.

Transfer services are included on the monthly invoices AW and WM send to SPU for commercial garbage collection. The SPU Contracts unit accountant is responsible for reviewing these invoice charges and the Solid Waste Contracts Manager approves them for payment. There are some query reports that were set up in the CSW database to help verify the accuracy of the solid waste invoice charges, including the Tonnage Check query report. The Tonnage Check report sums all the SPU transfer tons recorded in AW's and WM's systems and these totals are compared to the invoiced transfer tons for reasonableness. In addition, each transfer station in King County is required to report to the County Health Department on the number of tons of waste they transferred each month and SPU receives a copy of this report from AW and WM.

AW and WM do not pay for waste transfer services provided at the SPU stations because this has been factored into the rates in the residential and commercial solid waste collection contracts. SPU charges other customers who use SPU's transfer stations. AW and WM have contracts to collect garbage from some customers in the City who are not part of the SPU commercial collection contract and AW and WM use the SPU transfer stations for some of this waste.

Issue, Impact, and Recommendation

Invoiced charges for transfer services should be properly verified and approved before payment, to help ensure that the charges are accurate. Currently, controls over the verification of tonnage invoiced for transfer services need to be strengthened:

- There is insufficient validation of the transfer tons invoiced by AW. Currently, SPU relies completely on the contractors' data and does not perform any independent verification. Although SPU compares the sum of the transfer trip data recorded in CSW to the invoiced transfer tonnage, which is a good control practice, SPU does not verify the accuracy of the contractors' tonnage data. The detailed and summarized CSW data could match the invoiced tonnage, but it could also be inaccurate. A verification procedure could involve periodic sampling of weight tickets as part of the invoice review and approval process, or

this review/test could be added to the audit program for SPU Finance's annual solid waste contractor review.

ACTIONS PLANNED OR TAKEN

SPU will sample and check scale tickets against submitted scale data during the annual SPU contractor review beginning in 2008.

Recycling Invoicing for Processing Services and Commodity Credit - Conclusion 19: The verification of the recycling tonnage used for invoicing recycling processing services and for calculating the “recycling commodity credit” could be improved.

High risk

Background

Recycling waste is collected by both AW and WM and delivered directly to AW's recycling plant. AW invoices SPU for recycling processing services on the Residential Solid Waste Collection invoice and charges are based on a per-ton negotiated rate or “tipping fee.” The SPU Solid Waste Contracts accountant is responsible for reviewing these invoice charges and the Solid Waste Contracts Manager approves invoices for payment. The accountant maintains a Net Tonnage Recap spreadsheet to track the recycling (MRW) tonnage collected by both AW and WM, and the tonnage figures in this report should be close to those that are invoiced by AW. The data entered into this spreadsheet comes from the detail of the recycling trip-level files provided by AW and WM and uploaded to CSW in the TFR2 file.

AW sorts the SPU recycling waste by commodity type and then sells it to various parties, with much of it eventually going to Asia. SPU receives a “recycling commodity credit” from AW if market prices are higher than they were when the terms of the original agreement were put in place, which has been the case for several years for all MRW-commodity types except for glass. SPU received over \$1 million in 2006 from this recycling commodity credit.

Issue, Impact, and Recommendation

Invoices for recycling processing services should be properly verified and approved before payment and the recycling commodity credit should be calculated and applied accurately to the residential collection invoice. The verification of recycling tonnage figures could be improved. Currently, SPU relies on the monthly MRW tonnage figures provided by AW without performing any verification other than verifying that the tonnage in the trip-level data file (TFR2) provided by AW adds up to the tonnage invoiced. This MRW tonnage figure is also used by SPU to calculate the monthly recycling commodity credit. Although we did not find any calculation errors in either the invoiced charges or the commodity credit during our audit test work, because the vendors are the source of the recycling tonnage data, there should ideally be some sort of independent verification performed on it. For example, the recycling truck weight tickets

from AW's transfer station could be checked periodically against the data in the CSW TFR2 tonnage file.

ACTIONS PLANNED OR TAKEN

SPU will sample and check scale tickets against submitted scale data during the annual contractor review beginning in 2008.

Certification of Scales - Conclusion 20: None of the critical scales involved in the SPU Solid Waste processes have been certified/tested by the State of Washington Weights and Measures unit within the last several years. *High risk*

Background

Washington State Department of Licensing (DOL) requires that "a weighing and measuring device that's used to determine the charges for a product or service on the basis of weight or measure" is licensed annually with the State and the license must be posted at each location where the licensee operates. The scales utilized by SPU's solid waste vendors, including those at the Union Pacific Argo rail yard, AW's and WM's transfer stations in Seattle, and the Cedar Grove Maple Valley facility accommodate the full length of a large truck. There are inbound and outbound scales at each SPU transfer station, but these scales are only capable of accommodating the length of a smaller to mid-sized truck. All of these scales involved in SPU's solid waste processes are comprised of several load cells and each load cell needs to be calibrated within a certain level of tolerance to ensure the scale weighs vehicles accurately.

It is transfer station and solid waste industry practice and SPU policy for scales to be tested and certified regularly by an independent party. In addition, the State of Washington Weights and Measures unit, which is part of the Department of Agriculture (WSDA), has an oversight role for the entire State to ensure scale accuracy. The objective of the State's Weights and Measures Program is to promote marketplace equity in commercial transactions through testing and inspection of commercial devices. According to the Manager of the State Weights and Measures unit, all scales that are licensed with DOL are tested by his unit about every 28 months.

Issue, Impact, and Recommendation

All scales involved in SPU's commercial solid waste processes should be licensed annually with the State of Washington, the licenses should be posted at the solid waste facilities, and the scales should be periodically tested by the WSDA Weights and Measures unit. These scales should also be regularly tested and certified by an independent testing vendor to ensure they are accurate, and thereby ensure customer charges are accurate. We found that all of the SPU and vendor scales utilized as part of the SPU commercial solid waste functions were tested and certified at least annually and that the SPU Contracts unit tracks scale certifications to verify they have been conducted. However, we noted that several of the scales were tested by the same company that manufactured the scales. While it is not an uncommon practice for a manufacturer to test the scales they produced, this could appear to compromise the independence of the

test. We also noted that the State of Washington Weights and Measures unit had not tested any of the scales involved in SPU's solid waste functions for at least the last three years, and this is presumably because the scales have not been licensed with the State.

We recommend that SPU ensure that all critical scales involved in the SPU solid waste functions are licensed with the State and set up for periodic testing by the State Weights and Measures unit. SPU may also want to consider requiring scales to be tested and certified by a vendor other than the manufacturer of the scales, if this is feasible.

ACTIONS PLANNED OR TAKEN

SPU has requested that all critical scales be licensed with the State by May 2008 and that licensing is maintained in all future years.

Customer Complaint Tracking - Conclusion 21: Contractor reporting provided to SPU on customer complaints/issues needs to be improved. *High risk*

Background

SPU outsources customer service functions for commercial solid waste customers to the two solid waste contractors, AW and WM. Both AW and WM have a local "call center," staffed with customer service representatives, to handle all customer calls. Every time a customer calls to complain about something or to dispute a charge on their statement, the customer service staff make a note on the customer's account in a 'Comments' field. Both AW and WM apply a code to each type of customer issue that indicates the nature of the customer complaint or comment, such as "missed pick-up" or "too much noise." The contractors send SPU monthly reports on the number of missed pick-ups for commercial customers, but they don't provide reports that track any other types of complaints/issues and that show complaint/issue trends over time or compared to prior year. SPU management said missed pickups are tracked because they represent over 95% of the complaints in solid waste service delivery. SPU surveys a sample of commercial customers every two years and SPU management indicated that the surveyed Seattle businesses have routinely rated their garbage service as 5.5 on scale of 1 to 7, with 1 indicating poor service and 7 indicating exceptional service.

Issue, Impact, and Recommendation

There should be adequate tracking and reporting of SPU commercial customer complaints/issues by the solid waste contractors and SPU should regularly review this information in order to help monitor contractor performance and any customer issue trends. Currently, the contractors' reporting on customer complaints/issues to SPU is very limited and needs to be improved. SPU only receives reports on "misses" and "repeat misses," and SPU has never attempted to verify these numbers. Contractor customer service staff members receive a wide variety of customer complaints and comments, including excessive noise, improper re-placement of dumpster, rude drivers, etc. Each type of issue is coded in the contractors' customer accounting systems so it

would be possible to run a report itemizing the complaints/issues by code number. We recommend that SPU have the contractors provide a report including all complaint/issue codes for the commercial accounts and that the report show trends over time and/or provide a comparison to the prior year for the same code.

ACTIONS PLANNED OR TAKEN

SPU now receives detailed quarterly complaint logs from Waste Management. SPU will require both contractors to provide monthly complaint logs beginning in May 2008.

SPU will also expand the monthly complaint summary reporting to include complaints other than missed collection services.

Assessment of Penalties for Customer Service Failures - Conclusion 22: SPU is not assessing penalties or “liquidated damages” specified by contract terms for service failures, except for noise violations. High risk

Background

Section 750 in the Commercial Solid Waste Collection contracts covers "Omissions" and the associated "Liquidated Damages" or penalty fees that SPU will charge for various contractor customer service failures. These include the failure to collect missed waste pick-ups the contractors have received notice of, failure to deliver containers needing repair, using abusive language with the customer, etc. The contract lists the penalty fee associated with each service failure – for example, there is a \$50 fee for failure to pick up a garbage container that was missed within one business day after the makeup request was called in. This section of the contract was ostensibly put in place to encourage the contractors to provide good service to commercial solid waste customers. As discussed in the finding for Conclusion 22, the only reports SPU currently receives from the contractors on service failures is for missed pick-ups.

Issue, Impact, and Recommendation

Customer service failures listed as “omissions” in the commercial contracts should be accurately tracked and reported, and the associated “liquidated damages” or penalty fees should be charged to the contractors per contract terms. Currently, neither of these actions are occurring and this may have a negative impact on the quality of solid waste service. SPU is not assessing penalties or liquidated damages for the various service failures listed in the contracts. This occurs because the contractors do not provide reports to SPU on customer service complaints/issues by type of problem, which means that SPU has no way reliable way of knowing if and when these service failures have occurred. However, it should be noted that SPU does not assess the penalty fee for missed pick-ups, even though the contractors provide monthly reports on this. The only exceptions to this situation are noise complaint violations, for which contractors are charged a \$200 penalty. Noise complaints are handled by the SPU Contracts unit rather than the contractors’ customer service units, which may explain why SPU charges the penalty for

these. We recommend that the contractors track customer service failures by type of issue/complaint, provide monthly reports to SPU on this information, and for SPU to charge the appropriate penalty fees, in accordance with contract terms. Otherwise, the contract terms should be changed to match current practices.

ACTIONS PLANNED OR TAKEN

SPU tracks complaints and assesses penalties per contract based on customer calls or letters to the City. This practice applies to all types of complaints. (Noise concerns have been the primary complaints found to be out of compliance.)

SPU will also monitor contractor complaint logs beginning in May 2008 for any additional incidents of non-compliance.

APPENDIX 1

Commercial Solid Waste Revenues Data

Year	Commercial Solid Waste Revenues
2002	\$36.7 million
2003	\$38.5 million
2004	\$37.7 million
2005	\$38.1 million
2006	\$38.6 million
2007	\$42.4 million

Source: SPU Accounting

APPENDIX 2

SPU Revenue Cycle Audit – Commercial Solid Waste – Risk Matrix

Risk Level Definitions: Red = High risk – Internal controls should be strengthened as soon as possible; Yellow = Medium risk – It would be ideal to strengthen internal controls; Green = Low risk – Internal controls appear to be adequate.

Scope Area and Issues	Risk Level
Rates and Service Usage - <i>No issues noted</i>	Green
Billing and Account Adjustments	Yellow
<ul style="list-style-type: none"> • Customer Adjustments 	Red
Payment Processing and Remittance of Payments	Green
<ul style="list-style-type: none"> • Contractor Remittance of Customer Payments 	Yellow
Accounts Receivable Management	Yellow
<ul style="list-style-type: none"> • Accounts Receivable Aging Reporting 	Yellow
<ul style="list-style-type: none"> • Customer Delinquency Rates 	Red
<ul style="list-style-type: none"> • Interest & Penalties for Delinquent Accounts 	Red
<ul style="list-style-type: none"> • Contractor/SPU Communications 	Red

Collections, Dishonored Items, and Write-Offs	Red
• Timeliness of Turn-In to Collection Agency	Red
• Monitoring Accounts in Collections	Red
• SPU/City/Contractor Support for Collections Effort	Red
• Collections Rate Performance	Red
• Collection Agency Remission of Customer Payments	Red
• Collection Agency Commission Fees	Red
• Direct Payments	Red
• Customer Account Write-Offs	Yellow
Fund Accounting –Revenues and Receivables	Yellow
• Reconciliation of Receivable Account	Yellow
Information Technology - <i>No issues noted.</i>	Green
Vendor Billing For Services, Contracts, and Performance	Yellow
• Yard and Food Waste Processing Tonnage Charges	Red
• Review & Approval of Yard Waste Processing Services Invoices	Yellow
• Transfer Services Invoicing	Red

<ul style="list-style-type: none">• Recycling Invoicing for Processing Services and Commodity Credit	Red
<ul style="list-style-type: none">• Certification of Scales	Red
<ul style="list-style-type: none">• Customer Complaint Tracking	Red
<ul style="list-style-type: none">• Assessment of Penalties for Customer Service Failures	Red

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