

**Franchise Fees Follow-Up Audit
August 2011**

Patrice Randle, City Auditor
Craig Terrell, Assistant City Auditor
Lee Hagelstein, Internal Auditor

Table of Contents

	<u>Page</u>
Executive Summary	1
Audit Scope and Methodology	2
Status of Prior Audit Recommendations	3

Franchise Fees Follow-Up Audit



Office of the City Auditor
Patrice Randle, CPA
City Auditor

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Executive Summary

*Outside vendor to
review/monitor
franchise fees*

Fully Implemented

- *Requested payment for unpaid and underpaid telephone fees*
- *Analyzed taxicab payments*
- *Employee assigned to monitor franchise revenue*
- *Centralized receipt of telephone checks*
- *Controls over street use decals*

Partially Implemented

- *Compared telephone payments to PUC*
- *Recalculated telephone payments due to City*

The City Auditor's Office has completed a follow-up to the October 2010 Franchise Fees Audit. The follow-up audit was conducted in accordance with generally accepted government auditing standards, except for peer review. 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. The objective of the follow-up was to determine the implementation status of prior audit recommendations.

There were ten recommendations in the initial audit report. Management concurred with seven of those recommendations, partially concurred with two and did not concur with one. The City Auditor's Office concluded that seven of the prior audit recommendations have been fully implemented and two have been partially implemented.

With regard to the prior audit recommendations, management has performed the following:

- signed an agreement with MuniServices, LLC to review and monitor franchisee fee compliance for the City's major franchisees;
- mailed letters to telephone franchisees requesting payment;
- analyzed unpaid/underpaid taxicab franchise fees;
- assigned an employee the responsibility of working with the third party contractor to oversee the monitoring of franchise fee compliance;
- taken steps to ensure that all checks, except for taxicabs, are mailed to the Financial Services Division for processing; and,
- taken appropriate steps to purchase the proper number of street use decals and control decal issuance and destruction.

Audit Scope and Methodology

The City Auditor's Office reviewed various documents relating to this follow-up audit. The following methodology was used in completing the audit.

- Reviewed initial audit report and management's responses
- Reviewed departmental documentation related to implementation of recommendations
- Reviewed service agreement between the City of Arlington and MuniServices, LLC
- Reviewed Public Utility Commission (PUC) access line reports
- Reviewed City deposit records
- Reviewed Handitran taxicab decal records

Status of Prior Audit Recommendations

Recommendation:

The Chief Financial Officer (CFO) should require that staff compare telephone franchise payments received to the PUC website, on a quarterly basis, to confirm that franchise fees were received from all companies that reported access lines to the PUC.

Management's Response:

Partially Concur. As an alternative to this recommendation, the Mayor and City Council have authorized hiring a third party to review and monitor franchise fees.

Target Date: January 1, 2011

Responsibility: Mike Finley, Assistant Director of Financial and Management Resources

Audit Comment:

Since the third party contract relates to only two of the 60 telephone franchisees (AT&T and Time Warner), management may still want to consider at least an occasional review of compliance by telephone franchisees other than AT&T and Time Warner. Comparative analysis would have required minimal effort to identify the 23 companies that provided access lines to Arlington citizens, but did not forward fee payments to the City as required.

Implementation Status:

Partially Implemented. The City has entered into an agreement with MuniServices, LLC to monitor and perform franchise fee compliance reviews for some of the City's larger franchisees. However, the agreement does not include monitoring the numerous telephone franchisees that provide access lines to Arlington citizens. The City Auditor's Office compared PUC records to checks that were received based on access lines reported to the PUC during the 4th Quarter of 2010. As of June 24, 2011, the City had not received payments from eight of the 55 PUC-listed franchisees. The City Auditor's Office estimated that these eight franchisees should have submitted \$2,536.62 based on the number of access lines reported.

Recommendation:

For telephone companies that did not submit payment, based on the comparison mentioned above, the CFO should seek payment.

Management's Response:

Concur. Following completion of this audit, these findings will be sent to the respective franchisees as official documentation of under or over payment. Financial and Management Resources will send a letter seeking payment or providing a rebate for the telephone companies that did not submit accurate payment based on the audit findings.

Target Date: December 1, 2010

Responsibility: April Nixon, Director of Financial and Management Resources

Implementation Status:

Fully Implemented. The Financial and Management Resources Department (FMR) sent a letter to each of the 23 telephone companies requesting payment for unpaid franchise fees in the amount of \$44,355.39. As of June 24, 2011,

- the City received payments totaling \$3,063.84 from six of the franchisees, who had been sent payment requests totaling \$2,846.39;
- four payment requests, totaling \$3,547.12, were returned to sender;
- one franchisee (New Talk, Inc. dba Get a Phone) indicated that they had made the requested payment (estimated at \$5,692.08 by the City Auditor's Office) under another name. During the initial audit, review of FMR records and internet websites, including the PUC's, did not indicate a name change. During the follow-up review, the City Auditor's Office was able to confirm that the franchisee had paid the City \$6,214.64 for the periods reviewed; and,
- no response was received from the remaining 12 franchisees, which represent the remaining \$32,269.80 requested.

Management stated that they do not have sufficient resources to continually monitor and mount collection efforts for all the many small telephone franchisees. In management's opinion, the cost of such an undertaking outweighs the potential benefits, and using MuniServices to monitor the largest franchisees allocates FMR's limited resources to the areas with the greatest recovery potential.

Of the 23 companies identified for not making payments in the initial audit report, 14 reported access lines to the PUC for the 4th Quarter 2010. As of June 24, 2011, six of the 14 companies had not submitted payment.

Recommendation:

The CFO should recalculate, on at least a sample basis, telephone franchise payments received. Based on sample results, management should pursue companies that have underpaid, if deemed cost effective.

Management's Response:

Partially Concur. Based on results of third party franchise fee monitoring, FMR will attempt to recover underpayments from all the City's major utility franchisees.

Target Date: January 1, 2011

Responsibility: Mike Finley, Assistant Director of Financial and Management Resources

Implementation Status:

Partially Implemented. The third party's review is not intended to identify smaller telephone franchisees that do not make payments. The City Auditor's Office recalculated telephone fees due for the 4th Quarter of 2010 based on the PUC-reported access lines and the associated rates. Of the 55 telephone vendors that reported access lines in Arlington, it appeared that eight vendors that would not be included in the third party's review underpaid by a total of \$862.20.

Recommendation:

The CFO should consider billing telephone companies for unpaid franchise fees totaling approximately \$75,000.

Management's Response:

Concur. Following completion of this audit, these findings will be sent to the respective telephone franchisees as official documentation of under or over payment. Financial and Management Resources will send a letter seeking payment or providing a rebate for the telephone companies that did not submit accurate payment based on the audit findings.

Target Date: December 1, 2010

Responsibility: April Nixon, Director of Financial and Management Resources

Implementation Status:

Fully Implemented. During the initial audit, 23 franchisees were identified as not making payments and five were identified as making under-payments. FMR sent payment requests to each of the franchisees. As of June 24, 2011, the City had received \$3,063.84 from six of the franchisees that did not pay, and \$268.27 from one franchisee identified as having underpaid. Twelve franchisees did not respond, four payment requests were returned to sender and one franchisee paid under another name.

Based on a Local Government Code requirement that CTPs pay municipalities based on the number of access lines and rates established by the PUC, the initial audit noted \$35,532.95 in underpayments from AT&T. AT&T responded that their payments were less than that calculated because monthly write-offs were allowed from the amount owed to the City. The City Attorney's Office reviewed the Texas Administrative Code and concluded that AT&T could deduct uncollectible amounts from their franchise fee payment to the City. While FMR does not require AT&T to submit documentation to support the amount of write-offs/calculation of franchise fee payments, the City Auditor's Office obtained AT&T's quarterly write-off schedule which supported AT&T's franchise fee payments.

The remaining three companies that were identified as making under-payments did not respond to FMR's request for payment.

Recommendation:

The CFO should ensure that a standardized form is created and made available to those required to pay telephone franchise fees. The form should include the basis on which the amount paid was calculated and an attestation regarding the correctness of information provided. A copy of the form should be e-mailed, faxed or mailed to franchisees that submit payment without the form.

Management's Response:

Do Not Concur. As the Internal Auditors have pointed out in the first three recommendations, much of the information that would be captured on a standardized form is available on the PUC website, and these companies are required by law to provide the correct amount of franchise fees to be paid. The third party vendor will monitor new and current utilities on the PUC website.

Target Date: January 1, 2011

Responsibility: Mike Finley, Assistant Director of Financial and Management Resources

Implementation Status:

Not applicable.

Audit Comment:

Although management did not concur with this recommendation, the City Auditor's Office would like to note that requiring a standardized form or requiring additional information from franchisees would help verify proper payment in instances where companies deduct uncollectible access lines from their payment due to the City.

Recommendation:

The CFO should consider billing taxicab companies for the approximate \$6,700 in missed revenue.

Management's Response:

Concur. Handitran staff will analyze the make-up of the unpaid and underpaid taxicab revenue and then determine the cost effectiveness of pursuing any amounts owed to the City.

Target Date: January 1, 2011

Responsibility: Bob Johnson, Handitran Manager

Implementation Status:

Fully Implemented. Handitran staff stated that they have completed a review of taxicab companies that failed to purchase street use decals. In Handitran's opinion, taxicab companies that did not purchase window stickers for the period in question, most likely did not operate any vehicles during that period. Taxicab companies are only required to purchase street use decals if they plan to operate during the month.

Recommendation:

The CFO should assign an individual(s) the responsibility of establishing appropriate controls to ensure that all franchise revenue is received in accordance with City requirements.

Management's Response:

Concur. FMR staff will work with a third party to monitor franchise fee revenue and establish appropriate controls to ensure franchise fee revenue is received in accordance with City requirements.

Target Date: January 1, 2011

Responsibility: Mike Finley, Assistant Director of Financial and Management Resources

Implementation Status:

Fully Implemented. Ethan Klos, Treasury Manager, has been assigned as the person responsible for the third party agreement with MuniServices, LLC. He will be the contact person with regard to decisions, information, approvals, and acceptances relating to the agreement.

Recommendation:

The CFO should ensure that franchise fee checks, other than for taxicabs, be mailed directly to FMR for processing. Those companies that mail checks to the City Attorney's Office should be contacted to change the mailing address for their payments.

Management's Response:

Concur.

Target Date: January 1, 2011

Responsibility: David Barber, Assistant City Attorney

Implementation Status:

Fully Implemented. During the initial audit, there were 21 checks that were being received in the City Attorney's Office (CAO) and then forwarded to the Finance Division to be processed. As a result of the initial audit, City staff sent a letter (dated November 16, 2010) to the PUC, requesting that the PUC change the mailing address from the CAO to the Assistant Director of Financial Operations. Follow-up audit results indicate that there were only five checks received by the CAO during 4th Quarter 2010 and 1st Quarter 2011. Since the City's letter was dated November 2010, these five telephone franchisees may not have updated their records prior to submitting payment.

Recommendation:

The Transit Manager should ensure that adequate records are retained concerning all printed decals.

Management's Response:

Concur.

Target Date: January 1, 2011

Responsibility: Bob Johnson, Handitran Manager

Implementation Status:

Fully Implemented. The Transit Manager has taken steps to ensure that all decals are accounted for on a monthly basis. The schedule, which lists decals issued to taxicab companies or unused/shredded, is prepared monthly and signed-off on by two employees.

Recommendation:

The Transit Manager should limit the printing of decals to a reasonable number, thereby decreasing monthly printing costs.

Management's Response:

Concur.

Target Date: January 1, 2011

Responsibility: Bob Johnson, Handitran Manager

Implementation Status:

Fully Implemented. After discussions with the street use decal vendor, the Transit Manager has established the optimal number of monthly decals to be printed and at a reasonable cost.