



INTERNAL AUDIT

Department of Public Utilities, Solid Waste Division Non-Exclusive Franchise Agreement for Roll-Off Collection Services

Report 2018-01

June 2018



June 29, 2018

Honorable Mayor and Audit Committee Members
City of Fresno, California

Internal Audits presents this audit report regarding the Public Utilities Department, Solid Waste Division and its administration of the Non-Exclusive Franchise Agreements for Roll-Off Collection Services for the audit period of FY15 – FY17. The Audit Results are presented on page 2. Audit Objectives, Scope, and Methodology are presented on page 12. Management's and Contractor's responses to our audit recommendations are presented immediately following the recommendations in the report.

Internal Audits will perform a follow-up audit six months after this report is issued to verify that each recommendation has been implemented or that the findings documented have been resolved in a manner that addresses the cause of the issue or risk identified.

We would like to thank the staff from the Solid Waste Division for your assistance and cooperation during the course of the audit.

Respectfully submitted,

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Background

California law declares that it is in the public interest to authorize and require local agencies to make adequate provisions for solid waste collection within their jurisdiction. One of the ways that solid waste is collected in the City of Fresno (City) is through roll-off services. Waste management companies provide customers with roll-off bins—a container with capacity of one to eight cubic yards, with a hinged lid, and wheels that is typically serviced by a front end-loading collection vehicle—that are used to get rid of waste. Roll-off bins are commonly used to contain loads of construction and demolition waste from sites where something is being built, renovated, or demolished. The bins can also be utilized by residents or businesses for large amounts of trash, recycling services, or other dumpster needs.

In order to regulate this business, ensure its orderly operation, and to minimize the potential for adverse effects it may have on the local environment, the City requires all haulers providing roll-off collection services in the City to obtain a Non-Exclusive Franchise Agreement for Roll-Off Collection Services (agreement). The agreement defining non-exclusive rights is awarded to qualified contractors with demonstrated experience, reputation, and capacity to ensure public health, safety, and well-being.

The Public Utilities Department's (Public Utilities) Solid Waste Management Division is responsible for the oversight and management of the roll-off services agreements. As part of the agreement, the City receives franchise fees from the contractors for the City's administration of the agreement and for the contractor's use of the City streets, alleys, other public right-of-way, and infrastructure. Each month, the contractors must submit to the Utilities Billing and Collection (UB&C) Division of Public Utilities a report of revenues received for all roll-off services conducted within the city limit and pay the City franchise fees equal to ten percent (10%) of their actual gross rate revenues. The franchise fees collected by the City are put into the General Fund.

The City began non-exclusive franchise agreements for roll-off services in 2011 and now has agreements with 25 different contractors that generated over \$2 million in revenue for the City during fiscal years 2015 to 2017. However, the Solid Waste Management Division in 2016 became concerned that contractors were not adhering to the contract. Specifically, there was a concern that contractors were not accurately reporting their revenues received for roll-off services performed in the City and consequently were not paying the appropriate franchise fees owed to the City. Therefore, Internal Audits reviewed the roll-off reports and financial documents for a judgmental selection of five contractors for the period of July 1, 2014 to June 30, 2017 (fiscal years 2015 to 2017) to ensure they accurately reported their revenues and franchise fees.

AUDIT RESULTS

Finding 1A: Western Solid Waste Underreported Its Revenues Resulting in the City's Loss of \$4,200 in Revenue

According to the Non-Exclusive Franchise Agreement for Roll-Off Collection Services (agreement), the contractor shall pay franchise fees to the City each month for roll-off services provided by the contractor. The agreement also states that the contractor is responsible for paying all expenses related to the provision of services required by the agreement including, but not limited to, franchise fees, taxes, regulatory fees, collection costs, transportation costs, processing costs, disposal costs, utilities, etcetera. However, per review of Western Solid Waste's roll-off reports, Internal Audit confirmed the selected contractor deducted their expenses from the franchise fees owed to the City. As a result, Western Solid Waste placed the responsibility of paying their expenses onto the City. Therefore, the City was underpaid by the selected contractor. Western Solid Waste pays one of its commercial customers for cardboard that it recycles. At the beginning of the audit period in 2014, Western Solid Waste subtracted the amount it paid to the customer for the cardboard from the hauling fee revenue it received and reported the difference to the City as its revenue. Consequently, Western Solid Waste under reported its revenues and did not pay the appropriate amount of franchise fees to the City. In 2015, Western Solid Waste began to subtract the amount it paid for cardboard from their monthly gross revenue and reported the difference to the City as negative revenue. As a result, the contractor under reported its revenue twice over -

1. Actual gross revenue received from customers for load hauling was unreported
2. Negative amounts were deducted from total reported revenue

In 2016, Western Solid Waste reported the total amounts it paid to the commercial customer for cardboard as negative revenue, thereby continuing to underreport its revenue. In June of 2016, the contractor began reporting negative total revenues when the negative revenues for the one customer were greater than the amount it was reporting for its other customers. As a result, they did not pay franchise fees. In fact, Western Solid Waste did not pay any franchise fees in FY17 (July 2016 to June 2017).

Per discussion with the Office Manager of Western Solid Waste, it was management's understanding that they could deduct the expenses of the cardboard they collected from the revenue it reported. However, the Assistant Director of Public Utilities contacted Western Solid Waste via e-mail in July 2016 to clarify the negative revenue. Western Solid Waste's Office Manager responded and stated that because they had to pay their customer for recyclables, they should be able to deduct it from income made. In August 2016, the Assistant Director explained to the Office Manager of Western Solid Waste

that the franchise fee is payable regardless of the market variables and included the language from the agreement stating that the contractor is responsible for paying all expenses related to roll-off services. Yet, the contractor continued to report negative revenues and the City did not take any action to rectify it. As a result of the contractor reporting negative revenues, the City did not receive \$4,014.55 in franchise fees revenue owed to it from July 1, 2014 to June 30, 2017.

Additionally, Western Solid Waste charged customers rental per day or moving charges for roll-off services, however they did not report the revenue on its roll-off reporting form or pay the applicable franchise fees. As a result, they did not pay the City \$240.20 in franchise fees owed. Per discussion with the Office Manager, management was unaware that they had to report those revenues to the City. However, the agreement states that gross revenues earned on all roll-off container collection, transportation, processing, recycling, composting, and/or disposal services must be reported.

Recommendations

Department of Public Utilities should require UB&C to review the roll-off reports and franchise fees submitted by Western Solid Waste since July 1, 2017 to calculate the fees due, in addition to the \$4,254.75 due from the audit period, and bill Western Solid Waste the total due to be paid within 30 calendar days in accordance with the agreement.

Management Response: UB&C will invoice Western Solid Waste for \$4,254.75 within the next 10 working days.

Management Response: The owners of Western Solid Waste had no response to the findings.

Finding 1B: Western Solid Waste Did Not Ensure It Accurately Reported Tonnage

Internal Audit found two instances in which Western Solid Waste inaccurately reported tonnage. One of the selected roll-off services should not have been included on the roll-off reporting forms because it was for services performed for a customer outside of Fresno city limits. The team also identified an instance in which the tonnage did not reconcile with the contractor's weight ticket. Internal Audit found that these errors likely occurred because Western Solid Waste does not effectively verify the accuracy of the information it reports. Specifically, the Office Manager explained that Western Solid Waste does not have a process in place to review the roll-off reports before it submits them to the City. This creates a risk that these are not the only two instances in which

Western Solid Waste reported inaccurate tonnage to the City. As a result, the tonnage information the Assistant Director of Public Utilities utilizes to complete State mandated tonnage reports could be inaccurate

Recommendations

Western Solid Waste should create a procedure to have a separate individual review the roll-off reports for accuracy before they are submitted to the City.

Management Response: The owners of Western Solid Waste had no response to the findings.

Finding 2A: Bairos Recycling Does Not Maintain Sufficient Financial or Customer Records

The agreement requires that the contractor maintain accurate and complete accounting records containing the underlying financial and operating data relating to and showing the basis for computation of all revenues associated with providing collection, transportation, processing, recycling, composting, and disposal services. All of Bairos's roll-off services records are hard copy documents. However, Bairos Recycling, Inc. (Bairos) was unable to provide records for its roll-off services for five months in 2014. Bairos also could not locate its records for 2015 in a timely manner and did not provide them to Internal Audit until after the audit fieldwork had been completed. As a result, Internal Audit could not conduct its testing of those documents. Additionally, although the contractor must maintain accurate and complete records containing the number and types of accounts served by the contractor to comply with the agreement, Bairos does not have the ability to provide a list of Fresno customers to which it provides roll-off services. Therefore, Bairos cannot ensure that it is reporting the revenue and tonnage for all customers within Fresno as required. Management has explained that they are currently updating their tracking system of documents and plan to do things differently moving forward.

Recommendations

Bairos should develop a document management system to ensure it retains all required documents and has the ability to produce a report of all of its customers within Fresno's city limits.

Bairos should create a process in which the roll-off reporting forms and weight tickets are reviewed and analyzed to ensure accuracy before the reports are submitted to the City.

Management Response: Bairos Recycling Inc. is working on a spreadsheet to keep track of all the roll-offs within the City and also the County.

Finding 2B: Bairos Recycling Did Not Report All of the Revenues It Received

As stated previously, the agreement states the contractor shall pay franchise fees to the City each month equal to ten percent (10%) of actual gross rate revenues for roll-off services the contractor provides. However, there were 12 instances in which Bairos did not report revenue it received from customers, resulting in it not paying the City \$197.53 in franchise fees owed. In most of those instances, Bairos applied trip charges to roll-off services for cardboard to be recycled but did not report the revenue to the City. Bairos claimed that it did not “charge” the customers, but applied the amount it would pay for the cardboard to the trip charge to even it out and no bills were sent for any of the charges. However, regardless of the way in which the charge is paid for, it is revenue for Bairos and should have been reported. Furthermore, Internal Audit identified there were instances in which the trip charge was applied that the customer paid; however, Bairos still did not report the revenue from the trip charge. In another instance, Bairos did not report any of the revenue it received for the roll-off services it provided for their customer within Fresno city limits. Management explained that it was an error on their part that they did not report the revenue. The audit team found that these errors are a result of Bairos not having a process in place to review and analyze the roll-off documents before it submits the roll-off reporting forms to the City.

Recommendations

UB&C should bill Bairos Recycling, Inc. for the \$191.86 owed to the City.

Management Response: UB&C will invoice Bairos Recycling for \$191.86 within the next 10 working days.

Bairos should do the following:

- Report the revenue it received from trip charges, regardless of the way in which the trip charge is paid for, and pay the appropriate franchise fees moving forward.
- Develop a document management system to ensure it retains all required documents and has the ability to produce a report of all of its customers within Fresno’s city limits.

- Create a process in which the roll-off reporting forms and weight tickets are reviewed and analyzed to ensure accuracy before the reports are submitted to the City.

Management Response: Still not quite sure I agree with reporting the trip charge; since we were doing this from the beginning and the prior Principal Internal Auditor didn't tell us anything different when they came the first time which is why I have been doing it this way from the beginning. I will however, start doing as you say and report it in the future. Thanks.

Finding 3: Katch Environmental was Unresponsive to Audit Requests

As part of the agreement, the City and their auditors have the right to inspect specific documents or records required by the agreement or any other similar records or reports of the contractor that the City deems necessary to evaluate the contractor's performance specified in the agreement. The City has to provide the contractor written notice at least three business days prior to any inspection of these records, and the contractor must retrieve and make available to the City the requested documents and records at that time. However, Katch Environmental was unresponsive to multiple attempts made by Internal Audit via e-mail and phone call to request documents and set a meeting over a two-month period. Therefore, Internal Audit was unable to evaluate Katch Environmental's roll-off performance to ensure it was in compliance with the agreement.

Recommendations

The City should terminate the agreement with Katch Environmental on the grounds that it did not perform its obligations under the agreement.

Management Response: Solid Waste concurs with the findings of the audit. Termination for cause should be initiated immediately and notice sent to the hauler.

Finding 4A: Inadequate Review of Roll-Off Reports and Franchise Fees Resulted in Errors

Utilities Billing and Collections (UB&C) receives the monthly Roll-Off Reporting Forms and franchise fees from the contractors. An Accountant/Auditor II (Accountant) within UB&C documents the receipt of the fees and makes a copy of the documents to file and

maintain. The Accountant also creates a deposit slip that she sends to the Business Tax Unit with the check for deposit. A Customer Services Clerk in the Business Tax Unit verifies that the checks match the information on the deposit slip and posts the checks under the appropriate company's account in the City's financial software system, PeopleSoft. Therefore, the financial reports for roll-off fees should reconcile to the documentation maintained by UB&C. However, of the 106 transactions reviewed, Internal Audit identified nine instances in which the financial reports did not reconcile to the roll-off reports.

Many of the errors the audit team identified were data entry errors, such as entering the incorrect month for the date of receipt of the check. The last of these errors occurred in September 2016. Table 1 below describes the type of errors the audit team found and the number of instances the error occurred during the audit period.

Table 1 – City's Roll-Off Franchise Fees Errors

Error Description	Number of Errors
UB&C did not maintain/update the supporting documentation for a contractor's franchise fee payments.	3
Business Tax Division incorrectly categorized Commercial Solid Waste and Contract Management fees as Roll-Off fees, even though UB&C submitted the deposit slip with the correct Commercial Solid Waste and Contract Management account number.	3
UB&C submitted a Roll-Off fee as a Commercial Solid Waste and Contract Management fee.	1
Business Tax Division made a data entry error in which it entered a franchise fee with the incorrect month.	1
Mid Valley Disposal sent duplicate checks for one month, but the City did not send one of the checks back or credit the contractor.	1

Source: Internal Audits, based on a review of the City's financial reports for franchise fees.

The Accountant could not provide an explanation for many of the errors because they occurred before her employment. However, neither UB&C nor the Business Tax Division have a supervisor conduct a review of the check, supporting reports or documents, deposit slip, or entry in the software system. A review process of the roll-off reporting documents and deposit could have prevented the errors listed above.

Recommendations

UB&C should develop a policy and procedure for a supervisor to review and analyze the monthly roll-off reports, franchise fee checks, and deposit slip to ensure the accuracy of the information.

Management Response: UB&C Manager will sign off on initial payment preparation as a double check and then UB&C's internal auditor will at the end of each month review the PeopleSoft transaction history to ensure posting has occurred as intended. During the balance of May 2018 she will also work to verify and correct the Mid Valley Disposal overpayment dating back to May 2015.

The Business Tax Unit should develop a policy and procedure for a supervisor to review the check received, deposit slip, and PeopleSoft entry to verify the accuracy of the information.

Management Response: The Business Tax Unit in the Finance Department agrees with the auditor's recommendation – with clarification.

1) Business Tax (BT) acts only as a pass-through to for the roll-off revenue and relies on the posting summaries issued by Utility Billing & Collections (UBC) staff. If a posting summary is filled out incorrectly or a duplicate payment is submitted to BT to post, we would not be able to catch those errors.

2) In Sample 41, BT staff did indeed input the incorrect month in the transaction history. During the deposit reconciliation, staff will make sure they review all data entry including dates entered along with the payment amounts and general ledger accounts.

3) The BT clerk entering the payment is not directly posting the charges to PeopleSoft; that happens through a separate process. In Progressive Solutions Inc. (PSI), the correct General Ledger (GL) numbers are hard-coded within the charge codes used to generate the cash receipts. A report that summarizes all cash receipts by GL number is generated daily and the information is posted to PeopleSoft based on that report. If BT staff selects the correct charge code, the amounts will be posted to the correct PeopleSoft numbers. We are again relying on UBC staff to indicate the correct charge code on the posting summary so the correct GL number(s) will be selected.

4) BT's posting to an incorrect GL number for Samples 57, 59, and 61 was based on our incorrect interpretation of the UBC staff's posting summary description of the charge code ("Franchise Fees Comm" was understood to mean the charge code titled "Roll-off Franchise Fees," not the charge code titled

“Commercial Solid Waste” as UBC staff apparently intended.) Three different clerks made the same interpretation in these instances; it isn’t known whether they questioned the mismatched language at the time.

5) Since there was apparently no regular reconciliation of the GL accounts, the interpretation error was not found or corrected and therefore compounded month after month.

In addition to developing a procedure for a Lead or Supervisor to review and verify the accuracy of the data entry, BT’s procedure will include a direction to return to UBC for correction or clarification any posting summary whose wording does not exactly match the PSI charge code descriptions. We will supply the list of correct charge code descriptions to the appropriate UBC staff to help with this. We also recommend that the PeopleSoft GL accounts be reconciled by UBC staff on a regular basis, so that errors of this type can be found in a timelier manner.

Finding 4B: The City Has Not Ensured Accurate or Timely Receipt of All Monthly Roll-Off Reports and Franchise Fees

According to the agreement, the contractor must remit the franchise fees to the City on or before the 20th day of each month. If remittance is not paid to the City on or before the 20th day of any month, the contractor must pay, in addition to the amount owed to the City, two percent (2%) of the amount owed for that month. Furthermore, contractors must submit with its franchise fees a report of gross revenues earned on all roll-off services provided to customers within the City by month on the designated Roll-Off Reporting Form (roll-off reports). However, the City has not enforced these requirements on several occasions. Internal Audit found 15 instances in which contractors submitted untimely franchise fees; however, UB&C did not enforce the applicable late fees. The Accountant explained that when untimely franchise fees are received without a late fee included, a note is created on the deposit slip. However, the contractor is not contacted to collect the late fees. Internal Audit has calculated a revenue loss of \$647.83 during the audit period due to the lack of enforcement of late fees.

Furthermore, there were three contractors that did not submit franchise fees for multiple months. However, UB&C did not contact the contractors regarding the lack of revenues received for roll-off services. Therefore, UB&C was unable to verify that it had received all the revenue owed to the City.

Finally, as discussed previously, there were eight months in which Western Solid Waste reported negative revenues in its roll-off reports submitted to the City. Yet, the City did not contact Western Solid Waste until a year later to notify them that they were inaccurately reporting revenues. Even after the City contacted Western Solid Waste about the error, the City did not ensure the contractor improved its reporting and it continued to report negative revenue. This, as stated previously, resulted in Western Solid Waste not submitting \$4,014.55 in franchise fees to the City.

Recommendations

UB&C should contact contractors when there is non-compliance with the agreement, such as not including appropriate late fees or reporting negative revenues, and require the contractor to take specific corrective action.

Management Response: UB&C auditor will begin making contact with hauling vendors to notice them via email when their payments are not received by the 20th of each month and demand a response which would subsequently include a bill for late fees.

Finding 4C: Training and Improved Communication Are Needed Within the Department

Internal Audit determined that many of the errors or deficiencies found were a result of the City not effectively monitoring and analyzing the contractors' roll-off reports and franchise fees. The Assistant Director of Public Utilities believed that UB&C was conducting analysis of the reports and fees. However, the Accountant does not perform analysis of the reports or fees submitted. The Accountant explained that documented policies and procedures related to roll-off fees do not currently exist and was unaware of who is responsible for analyzing the reports and fees. In addition, adequate training has not been provided to properly review the roll-off fees.

Recommendations

The Department of Public Utilities, Solid Waste Division should create policies and procedures for the monitoring and analysis of franchise fees and roll-off reports. The policies and procedures should, at a minimum, identify the party or parties responsible for monitoring, assessing, and enforcing the requirements in the agreement; and state the actions to be taken if non-compliance occurs (for example, if a payment is received late). In addition, training and guidance should be provided to UB&C staff to adequately review and analyze the franchise fees and roll-off reports.

Management Response: UB&C will initiate email communication with both the Solid Waste Manager, Franchise Haulers and City Internal Audit staff when appropriate to determine continuing compliance with the terms of the Franchise Agreements.

Scope and Methodology

City management directed the Internal Audits Unit to conduct an audit of the non-exclusive franchise agreements for roll-off collection services. The table below outlines the audit objectives and Internal Audit’s methods for addressing them.

Table 2 - Audit Objectives and the Methods Used to Address Them

Audit Objective	Procedures
<p>1. Determine if a selection of five roll-off collection services contractors complied with all appropriate franchise fee requirements, including but not limited to reporting revenue, properly calculating fees due, and remitting the reports and fees to the City in a timely manner, as required by the Franchise Agreement.</p>	<p>A. Selected five roll-off collection services contractors—Allied Waste Services, Bairos Recycling, Katch Environmental, Mid Valley Disposal, and Western Solid Waste—based on revenue amount and potential areas of risk or concern.</p>
	<p>B. Interviewed contractor personnel to determine processes for receiving and reporting revenues.</p>
	<p>C. Reviewed contractor financial reports and supporting documents for revenues received during the audit period.</p>
	<p>D. Determined if the selected revenues reconcile to the reports submitted to the City to assess if the contractor appropriately reported all revenues received to the City.</p>
	<p>E. Obtained a judgmental selection of weight tickets for each of the contractors and reconciled them to the contractors’ monthly reports to the City to confirm their accuracy.</p>
<p>2. Determine if UB&C has established and followed adequate record keeping systems and internal controls related to the timely and accurate receipt of all monthly roll-off franchise fees in accordance with the Franchise Agreement.</p>	<p>A. Interviewed appropriate Solid Waste Management and UB&C personnel to determine the processes for monitoring, receiving, and documenting roll-off reports and franchise fees.</p>
	<p>B. Reviewed UB&C’s documentation of contractors’ reports and roll-off fees paid to determine whether they reconcile.</p>
	<p>C. Reviewed the City’s financial reports to verify fees submitted to the General Fund reconcile with that reported and received by the City.</p>

Source: Internal Audits