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# OFFICE OF THE CITY AUDITOR

## PERFORMANCE AUDIT OF THE PROCESS AND PROCEDURES FOR ACCOUNTS RECEIVABLE AND NON-SUFFICIENT FUNDS CHECKS

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**March 15, 2002  
Report No. 353**

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Memorandum



March 15, 2002

Honorable Mayor and Members of the City Council  
City of Dallas

We have conducted a performance audit of the process and procedures for accounts receivable and non-sufficient funds checks.

As a result of our inquiries, examinations, and tests, we conclude that there are some areas in the accounts receivable process that could be improved. Related opportunities for improvement and recommendations are presented in this report.

We appreciate the cooperation shown by City staff during our examination.

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for  
Thomas M. Taylor, CPA  
City Auditor

c: Teodoro J. Benavides, City Manager

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**PERFORMANCE AUDIT OF THE PROCESS AND PROCEDURES FOR  
ACCOUNTS RECEIVABLE AND NON-SUFFICIENT FUNDS CHECKS**

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## INTRODUCTION

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### Authorization

We have conducted a performance audit of the process and procedures for accounts receivable and non-sufficient funds (NSF) checks. We conducted this audit under the authority of Chapter IX, Section 2 of the Dallas City Charter, and in accordance with the Annual Audit Plan approved by the City Council.

### Scope and Methodology

We performed our audit in accordance with generally accepted government auditing standards and included tests of the accounting records and other audit procedures that we considered necessary in the circumstances.

The objectives of our audit were to determine whether:

- The City Controller's Office is in compliance with City regulations for accounts receivable and NSF checks.
- Selected City departments are in compliance with Administrative Directive (AD) 4-10 and AD 4-11 regarding aged accounts and NSF checks.
- Collection efforts of individual departments are effective and efficient.

Our audit covered October 1999 through June 2000. However, we examined certain events and transactions occurring before and after that period. We reviewed the City's General Ledger and individual entries by departments. Furthermore, we examined the data supplied to the City Controller's Office by individual departments and the data the City Controller's Office supplies to the Finance and Audit Committee. Our audit did not include the Dallas Water Utilities accounts receivable activities. These activities will be addressed in a subsequent report.

To develop an understanding of relevant control structure policies and procedures, we reviewed the following:

- AD 2-1, *Administrative Directives*
- AD 4-10, *Delinquent and Uncollectible Accounts Receivable*
- AD 4-11, *Processing NSF Checks*
- Individual departmental policies and procedures
- Resource Information Guide (RIG)

## INTRODUCTION

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Additionally, we interviewed management and staff concerning relevant internal controls. We examined individual departmental related reports and analyzed historic results. We also compared data of various reports and observed operating procedures.

### **Overall Conclusion**

As a result of our inquiries, examinations, and tests, we conclude that there are some areas in the accounts receivable process that could be improved.

### **Background**

The City of Dallas reported \$117.9 million in accounts receivable during fiscal year 1999. Of this amount, \$88.4 million (75%) was in the General Fund and the enterprise funds. The remaining receivables were reported in the *trust, fiduciary, internal service, and special revenue funds*. Posting of accounts receivable is decentralized to the individual departments. With the exception of Dallas Water Utilities and Ambulance Service, all departments with billing and collection responsibilities are to report their accounts receivable to the City Controller's Office monthly. As requested, the City Controller's Office reports these accounts receivables to the City Council's Finance and Audit Committee.

The following paragraphs provide a synopsis of each of the ADs that we reviewed to determine compliance.

AD 2-1 establishes the authority to issue ADs. ADs are issued under the authority and by the signature of the City Manager and/or under the authority and by the signature of other City Council appointed officers (i.e., City Manager, City Attorney, City Auditor, and City Secretary). The City Manager or his designee has the authority to assign to department directors the responsibility to prepare ADs, unless the responsibility is otherwise assigned to another Council appointed officer, or delegate department assignment responsibility to the Director of Budget and Management Services (currently the Director of Financial Services).

The Director of Financial Services (FS) has the responsibility as the legal custodian of the AD and is responsible for authentication, publication, indexing, maintenance, and distribution to department directors, revisions, change notice documentation, and preparation of current page checklist of approved draft ADs.

## INTRODUCTION

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In addition, each year the Director of FS is responsible for requesting directors to review and forward any needed revisions to ADs.

AD 4-10 addresses uncollectible accounts, efforts for delinquent account collection, and procedures for removing uncollectible accounts from the City's records. Written off accounts are reported annually to the City Council's Finance and Audit Committee.

AD 4-11 establishes standard procedures for collecting NSF checks and proper accounting treatment for recording returned check amounts and collection fees.

## **OPPORTUNITIES FOR IMPROVEMENT**

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We identified certain policies, procedures, and practices that management could improve. Our audit was not designed or intended to be a detailed study of every relevant system, procedure, and transaction. Accordingly, the opportunities for improvement presented in this report may not be comprehensive of the areas where improvements may be needed.

### **1. AD 2-1 has not been consistently applied.**

AD 2-1 is the foundation for the authority to issue ADs. This AD designates the Director of FS as the legal custodian of the ADs. The Director is responsible for authentication, publication, indexing, maintenance, distribution to department directors, revisions, change notice documentation, preparation of current page checklist of approved and draft ADs, and records retention of historical, current, approved, and interim ADs. In addition, each year the Director of FS is responsible for requesting directors to review and forward any needed AD revisions.

AD 2-1 also places responsibilities on departmental directors for preparation, content, and timeliness of the requirements contained within an assigned draft AD. Further, it requires departmental directors to ensure departmental compliance with approved ADs. Departmental directors are required to conduct an annual review of ADs issued by their departments and report to FS whether changes, including deletions, are required. If changes are required, the director is to ensure that the changes are made in a timely manner. The AD does not specify when the review is to be conducted or when it is to be completed.

During the course of this review, the Director of FS has taken action to initiate the annual review of ADs in accordance with AD 2-1.

**We recommend** that the Director of FS:

- Establish the time period of the annual review and incorporate it into AD 2-1.
- Establish internal controls to ensure directors annually review each AD issued by their departments.

### **Management's Response:**

Management concurs. AD 4-9 (Internal Controls) has been revised to include this annual review of departments' AD during their annual internal controls and vulnerability assessments. This annual review, which provides direct reporting to the City Manager, will provide the departments with needed information and insight for any needed revisions to their ADs.

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Performance Audit of the Process and Procedures for Accounts Receivable and Non-Sufficient Funds Checks

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## **OPPORTUNITIES FOR IMPROVEMENT**

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### **2. AD 4-11 needs updating.**

Procedures to streamline collection efforts have not been incorporated in AD 4-11.

AD 4-11 addresses NSF checks. Strict adherence to the AD may actually inhibit the recovery process. The AD requires notifying the check issuer by telephone and first class mail. Checks over \$750 require notification by telephone and a registered letter prior to referral to the City Attorney's Office (CAO). The latest revision of this AD was October 2, 1995.

In a December 4, 1996, memo to department directors, the City Controller's Office recommended procedures for processing NSF checks; however, only two of the departments we reviewed were using the recommendations. The memo lists instructions, forms to use, and procedures to streamline collection efforts by using a Justice of the Peace (JP), thus eliminating the first class letter and referrals to the CAO. These procedures have not been incorporated into AD 4-11.

The procedures of using JP courts were jointly developed by the City Controller's Office and the City Attorney's Office and are in compliance with Section 31.06 of the Texas Penal Code - Presumption for Theft by Check.

**We recommend** that the Director of FS incorporate the recommended procedures for processing NSF checks into AD 4-11.

#### **Management's Response:**

Management concurs. The City Controller's Office has revised AD 4-11 to incorporate new procedures for processing NSF checks.

### **3. Recorded accounts receivable balances are outstanding.**

When reviewing the General Fund and selected enterprise funds, we found accounts with outstanding balances in excess of one year. The table on the following page shows the accounts with balances greater than \$100,000 and outstanding greater than one year.

## OPPORTUNITIES FOR IMPROVEMENT

Selected Departments with A/R Balances Greater than \$100,000 and Amounts Outstanding Over 1 Year						
Department	Total A/R at 6/30/00	Over 1 Year	% of Total	Over 2 Years	% of Total	Total %
Equip & Bldg. Svcs.	135,976	33,895	24.9%	61,564	45.3%	70.2%
Planning & Dev.	282,527	14,010	5.0%	14,551	5.2%	10.2%
Aviation	558,117	80,734	14.5%	272,125	48.8%	63.3%
Event Services	1,482,838	94,229	6.4%	33,204	2.2%	8.6%
Ambulance Svcs.	23,088,383	10,337,312	44.8%	N/A*	N/A*	44.8%

\*Note: Ambulance Svcs. did not note balances over 2 years.

The City Controller's Office has periodically informed the departments about the importance of identifying delinquent accounts and related accounts receivables information. On August 26, 1999, the City Manager issued a memorandum to all department directors informing them that the departments have final responsibility for collection of receivables.

AD 4-10, Section 4.5 defines uncollectible accounts as: "Accounts for which all-reasonable collection efforts have failed, and there is no knowledge of probable subsequent collection." Section 5.1.3 states that department directors shall annually record uncollectible accounts and write off uncollectible accounts.

**We recommend** that the Director of FS review the outstanding balances noted on the previous page and throughout other departments to ensure that the accounts receivable balances accurately reflect potential revenue realization.

### Management's Response:

Management concurs. The Office of Financial Services will review the account listings on a semi-annual basis and recommend to departments proper action for the dormant accounts (i.e., establish or increase allowance or write off).

#### 4. Department accounts receivable balances do not match amounts reported on the City's Comprehensive Annual Financial Report (CAFR).

We compared selected General and Enterprise Fund accounts receivable balances to the balances reported on the Fiscal Year 1999 CAFR. The result is summarized in the table on the following page.

## OPPORTUNITIES FOR IMPROVEMENT

Comparison of Financial Statement Data To Departments' Data At Fiscal Year End 1999 (September 30, 1999) (In thousands)				
	Financial Statement	Dept. Verified Data	Variance	% of Over/Under
Sanitation Service	\$1,247	\$1,223	\$24	2%
Park & Recreation	270	209	61	23%
Risk Management	716	0	716	100%
City Attorney's Office	214	0	214	100%
Street	110	0	110	100%
Rev. & Tax	229	229	0	0%
Police Department	46	1	45	98%
Event Service	5,558	5,363	195	3%
Aviation	436	421	15	3%
Planning & Development	450	413	37	8%
Equipment and Building Services	76	0	76	100%
<b>Subtotal of Tested Accts Receivable</b>	<b>\$9,352</b>	<b>\$7,859</b>	<b>\$1,493</b>	<b>16%</b>

We interviewed the twelve departments listed in the table above. Subsequent to the interviews, one department reconciled a majority of their accounts receivable to the General Ledger and one department (Risk Management) corrected the journal entry that set up the erroneous accounts receivable balance. At the time of the audit, the remaining departments had not reconciled the differences.

Most of the departments that we interviewed were unable to confirm the dollar value of their NSF check receivables.

Accounts receivable reported on published financial statements is not fully verifiable by department documentation.

Information should be accurately and promptly collected, analyzed, summarized, and reported. Resource Information Guide Basic Policies, Section 2.3.12 states that monthly reconciliations of accounts receivable subsidiary ledger balances to General Ledger accounts should be performed to ensure all accounts are recorded for the proper amount.

**We recommend** that the Director of FS ensure that accounts receivable balances noted on the CAFR are supported by department verified data. Identify which departments are not adhering to the Basic Policies of periodic accounts receivable reconciliations, aid in the development of procedures to accomplish this task, periodically review implementation of the procedures, and report department progress.

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## OPPORTUNITIES FOR IMPROVEMENT

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### Management's Response:

Management concurs. The City Controller's Office has completed a comprehensive City-wide review of accounts receivables and follow up was done at yearend with those departments who did not submit reconciliations as required in the annual year-end memo; accounts were adjusted accordingly.

### 5. The processing of uncollectible accounts by the City Attorney's Office needs improvement.

AD 4-10 requires departmental directors to submit uncollectible accounts to the CAO for further review and processing. The CAO's responsibilities are: signing and mailing demand letters submitted by departments; reviewing delinquent accounts (in excess of \$1,000) submitted by departments; and exercising recovery efforts where appropriate. If the CAO deems appropriate, accounts are returned to departments for referral to the collection agency. The CAO is to provide a receipt to the delivering department when accounts receivable documents are received.

We found the following:

- The CAO has not been issuing receipts to departments that forward uncollectible account documentation.
- A specific attorney is not assigned to the collection of past due accounts; various attorneys are assigned to perform these duties, and departments are not notified of the attorney assigned to their accounts.
- The CAO has not developed a formalized method to:
  - Track the receipt, progress, and end result of uncollectible accounts.
  - Periodically notify departments of account status.

Without receipts, disputes may arise as to whether departments forwarded uncollectible accounts to the CAO. Departments have difficulty obtaining information and determining the status of uncollectible accounts. Accounts may be lost or inefficiently processed. Interdepartmental cooperation may be hampered.

Subsequent to our review, the CAO has assigned an individual to receive all uncollectible account documentation. The CAO is in the process of formalizing a method to log receipt of this documentation.

## **OPPORTUNITIES FOR IMPROVEMENT**

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### **We Recommend** that the City Attorney:

- Ensure that receipts are issued to departments that forward uncollectible account documentation.
- Consider centralizing the inflow of uncollectible account documentation to a limited number of personnel.
- Design a formalized method to:
  - Track the receipt, progress, and end result of uncollectible accounts.
  - Periodically notify departments of account status.

### **City Attorney's Response:**

In response to processing uncollectible accounts referred to the City Attorney's Office, the following procedures have implemented:

- The City Attorney's Office forwards to the department a memorandum acknowledging receipt of each account referred for collection, including a request for any additional information necessary to assist in the Office's collection efforts.
- The Office has assigned a senior attorney to receive all collection matters referred to the City Attorney's Office. That senior attorney is responsible for supervising all collection cases. In addition, a legal assistant has been assigned, as her primary responsibility, the coordination of all collection cases, under the direct supervision of that senior attorney.
- As noted above, the legal assistant who is responsible for all collection cases tracks their receipt and progress, and is responsible for communicating with departments regarding collection matters referred to this office.