City of San Diego

AUDIT REPORT

METROPOLITAN WASTEWATER DEPARTMENT CONTRACT COMPLIANCE AUDIT

July 24, 2009

Office of the City Auditor
Eduardo Luna, CIA, CGFM, City Auditor

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THE CITY OF SAN DIEGO

July 24, 2009

Honorable Mayor, City Council, and Audit Committee Members
City of San Diego, California

Attached is our Metropolitan Wastewater Contract Compliance Audit. Metropolitan Wastewater's and Purchasing & Contracting's responses to our audit recommendations can be found after Appendix II, page 18, of the report. The audit staff responsible for this audit report are Sonja Thorington and Kyle Elser.

We would like to thank the Metropolitan Wastewater and Purchasing & Contracting Department staff for their assistance and cooperation during this audit. All of their valuable time and efforts spent on providing us information is greatly appreciated.

Respectfully submitted,

Eduardo Luna
City Auditor

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EXECUTIVE SUMMARY

In response to a request from the Metropolitan Wastewater Department (Department), we have audited a selection of contracts for general compliance in billing. Specifically, we reviewed the Olin Chlor Alkali Products (Olin Chlor), US Peroxide, and AmeriPride Uniform Services (AmeriPride) contracts. We conducted this audit in accordance with Generally Accepted Government Auditing Standards and limited our work to those areas specified in the Scope and Methodology section of this report.

Based on our audit testing of two purchase orders for the supply of chemicals as well as a contract for the provision and laundry service of uniforms to the Department, we found that the Department could improve the review and approval of invoices to reduce the risk of inaccurate billing and payment.

We found the following issues during our review:

OLIN CHLOR

- The Department inappropriately paid an estimated $80,500 in sales tax for the purchase of chemicals that should have been purchased tax free.
- The Department does not have sufficient safeguards to ensure invoices are paid using appropriate funds.

US PEROXIDE

- The Department's Accounts Payable section does not adequately verify the delivery amount of chemicals charged by vendor.

AMERIPRIDE

- Invoices contained small inaccuracies and inappropriate charges.
- The Purchasing & Contracting Department does not maintain all appropriate pricing lists to ensure accurate vendor billing.
- Department staffs' processing and records management of vendor invoices are inconsistent and should be enhanced.

We made twelve recommendations for corrective action to be considered and/or taken. The details of our findings can be found in the Audit Results section of this report.

INTRODUCTION

In response to a request from the Metropolitan Wastewater Department, we have audited a selection of contracts for general compliance in billing. We conducted this audit in accordance with Generally Accepted Government Auditing Standards and limited our work to those areas specified in the Scope and Methodology section of this report.

Background

The Metropolitan Wastewater Department (Department) collects, treats, and disposes of nearly 180 million gallons of wastewater every day. Its mission is to provide the public with safe, efficient, and effective regional wastewater service. The Department serves a 450 square mile area with a population of approximately 2.2 million people, which includes the treatment of wastewater from 15 other cities and sanitation districts (called Participating Agencies). Representatives from these Participating Agencies comprise the Metro Wastewater Commission (Commission), established in 1998, which serves as an advisory body to the San Diego City Council on the operation of the Metropolitan Sewerage System. In Fiscal Year 2009, the Metropolitan Wastewater Department's budget was approximately $500.3 million.

In meeting these goals, the Department operates through five divisions: Wastewater Treatment and Disposal, Wastewater Collection, Environmental Monitoring and Technical Services, Engineering and Program Management, and Administrative Services. In Fiscal Year 2009, these divisions had approximately 840 budgeted employees. The Department also requires many different vendors that provide goods and services.

In an effort to increase efficiency, the Metropolitan Wastewater Department and the Water Department consolidated and currently report under the Public Utilities Department. In an added effort to identify and eliminate inefficiencies that may be present, the departments approached the Office of the City Auditor and requested an audit of a sample of contracts; two of its larger contracts for the provision of treatment chemicals and one contract for the provision and laundry service of employee uniforms.

Audit Objective, Scope, and Methodology

The audit objective was to assess the level of compliance for three contracts identified by the Department, specifically relating to the appropriateness of vendor billing.

The three vendors identified were Olin Chlor Alkali Products (Olin Chlor), US Peroxide, and AmeriPride Uniform Services (AmeriPride). Specific purchase orders were identified for review for each of two chemical contracts - Olin Chlor and US Peroxide. The Department requested a broader review of the AmeriPride invoicing, as some department staff had raised concerns about the frequency of inappropriate charges being billed to the City.

The following audit methodology was used to achieve our audit objectives:

- Obtained and reviewed original bid documents and up-to-date pricing agreements.
- Interviewed department staff that review invoices, determining standard policies and procedures in invoice approval and payment.
- Verified appropriateness of charges in Olin Chlor November 2008 invoices for purchase order 5200928.
- Verified appropriateness of charges in US Peroxide November 2008 invoices for purchase order 5200501.
- Verified appropriateness of charges in November 2008 invoices for four (4) of the Department's 14 AmeriPride purchase orders; 5200772, 5203097, 5201557, and 5200771, representing service to 10 different Department locations.

We also included a review of the two chemical contracts in regard to the State of California Board of Equalization Sales and Use Tax Regulations related to water additives. Regulation 1525 applies to property used in manufacturing. The regulation states that "tax does not apply to sales of tangible personal property to persons who purchase it for the purpose of incorporating it into the manufactured article to be sold, as, for example, any raw material becoming an ingredient or component part of the manufactured article." The objective of this additional review was to assess the appropriateness of sales tax paid in relation to purchases of sodium hypochlorite and ferrous chloride.

The following audit methodology was used to achieve our extended objectives:

- Interviewed department staff regarding use of sodium hypochlorite and ferrous chloride.
- Contacted the California Board of Equalization to verify eligibility of chemicals for tax exemption and statute of limitation for recovery of inappropriately paid sales tax.
- Obtained listings of purchase orders for sodium hypochlorite and interviewed staff about the use of chemicals for each purchase order.
- Obtained and reviewed invoices for the two purchase orders of sodium hypochlorite added to water that is resold.

- Extrapolated dollar amount of sales tax paid by the City for two identified purchase orders of sodium hypochlorite for Fiscal Years ending June 30, 2007, 2008, and 2009.

We evaluated internal controls related to the audit objectives. Our review focused on controls related to the verification of services rendered prior to the payment of invoices. Our conclusions on the effectiveness of these controls we reviewed are detailed in the following audit results.

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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Our audit work was limited to areas specified in the Objective, Scope and Methodology section of the report.

AUDIT RESULTS

THE DEPARTMENT COULD IMPROVE THE REVIEW AND APPROVAL OF INVOICES TO REDUCE THE RISK OF INACCURATE BILLING AND PAYMENTS.

We reviewed three contracts for goods and services – Olin Chlor Alkali Products (Olin Chlor), US Peroxide, and AmeriPride Uniform Services (AmeriPride). We found issues related to invoicing with all three contracts. Based on our testing of two purchase orders for the supply of chemicals, and the provision of laundry service to the Department, we found that the Department could improve its invoice review and approval processes. By doing so, the Department could reduce the risk of incorrect billing and payments.

Olin Chlor Contract

The Department purchases sodium hypochlorite (12.5% solution) to treat wastewater and for odor control. Olin Chlor maintains nine purchase orders with the City for the supply of sodium hypochlorite 12.5% solution. Two of the purchase orders are for deliveries to the City's North City Water Reclamation Plant and South Bay Water Reclamation Plant, both of which maintain contracts for the resale of its reclaimed water. Between Fiscal Years 2007 and 2009, the Department purchased an estimated $2,182,000 in sodium hypochlorite from Olin Chlor for use at its Water Reclamation Plants.

The Department inappropriately paid an estimated $80,500 in sales tax for the purchase of sodium hypochlorite that should have been purchased tax free.

Certain chemicals that are purchased and are used as components in a good that is resold may qualify for sales tax exemption. California Sales and Use Tax Annotation 275.0420 of Regulation 1525 states that sodium hypochlorite is a water additive which, if added to and remains in water that is resold, may be purchased ex tax.[1] During fiscal years 2007, 2008 and 2009, we estimate that the Department has inappropriately paid approximately $80,500 in sales tax to Olin Chlor.[2]

There appears to be a lack of understanding and/or lack of communication between the Purchasing & Contracting Department (Purchasing), the entity that enters contract agreements, and the Wastewater Department, as to the processes of wastewater and its variety of uses.

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[1] "Ex tax" means tax free. See Appendix II for Annotation 275.0420.

[2] Estimate based upon review of Calendar Year 2008 invoices for purchase of sodium hypochlorite to the City's North City and South Bay Water Reclamation Plants. As 100% of sodium hypochlorite purchased is not added to the reclaimed water, a Department analysis of the total amount of sodium hypochlorite added to water during Calendar Year 2008 was used to determine the percentage of sales tax recoverable. An estimate of sales tax paid during Fiscal Year 2008 for applicable sodium hypochlorite purchases was extrapolated to estimate total recoverable payments for Fiscal Years 2007 to 2009.

According to Purchasing, which is aware of the possibility of tax exemption for sodium hypochlorite, the purchase of this chemical does not qualify for tax exemption because potable water is resold and wastewater is not. On the contrary, the City maintains three wholesale contracts and approximately 450 retail contracts for the sale of its reclaimed water.

A disconnect existing between the Department - which employs subject-matter experts regarding the use of chemicals, some of whom are familiar with tax exemption regulations - and Purchasing resulted in the creation of a contract that fails to prevent unnecessary costs to the City and, if not remedied, will continue to cost the City thousands of dollars more than is necessary for its purchase of chemical supplies.

As the statue of limitations for sales and use tax refunds from the State is three years, the City may request that Olin Chlor credit the amount of the three years during which sales tax was inappropriately paid. Olin Chlor would then be able to file a refund with the State Board of Equalization to recover the excess paid on its tax returns to the State during the same time period.

Recommendations:

1) The Department should periodically review contracts for tax exempt chemicals to ensure that they are not paying unnecessary sales tax. As part of this review, the Department should ensure that Purchasing & Contracting is aware of the use of chemicals purchased for each purchase order.

2) The Department should request reimbursement from Olin Chlor for sales tax paid on tax exempt purchases of sodium hypochlorite for the past three years. Upon further review, the Department should request refunds for any other tax-exempt chemicals identified.

The Department does not have sufficient safeguards to ensure invoices are paid using appropriate funds.

In reviewing invoices and payments made to Olin Chlor for the purchase of sodium hypochlorite, we found a payment of approximately $4,000 for a chemical that is contracted to be paid under a different purchase order. In a later review of sales tax paid to Olin Chlor for the purchase of caustic soda, another chemical that is identified by the State Board of Equalization as being tax exempt if added to water that is resold[3], we found several instances where payment was posted to the wrong purchase order.

In one instance, we were reviewing the purchase order for the provision of sodium hypochlorite. Included in payments made in Fiscal Year 2009 was a payment of approximately $3,900 to Olin Chlor for the purchase of caustic soda, which is to be provided under another purchase order. Again, when later reviewing the City's payments

[3] Our review of a sample of the Department's purchase orders for caustic soda found that the caustic soda purchased was not added to water that was resold, and was therefore ineligible for sales tax exemption.

to Olin Chlor for the purchase of caustic soda, we found four payments for approximately $4,200 each made for the purchase of sodium hypochlorite. Altogether, these four misposted sodium hypochlorite invoices represent a potential recovery of approximately $1,225 in sales tax that might easily have been excluded.

There were no errors noted on any of the invoices; they stated the correct purchase order numbers and the charges billed were appropriate. However, they were posted to incorrect purchase orders. These appear to be manual input errors caused by City staff.

The Department's Accounts Payable section invoice approvals were not reviewed prior to submission for payment to the Comptroller's office.

In March 2009, in an effort to ensure timely vendor payments, the Accounts Payable section in Public Utilities implemented a procedure in which invoices are reviewed by supervisory staff prior to invoice payments being forwarded to the Comptroller's Office. Prior to this implementation, there was no policy or procedure requiring supervisory review of vendor payments, and so review of invoice approvals were not consistent. In some cases, approvals for vendor payment were sent directly from Department staff to the Comptroller's office, which does not review approvals. According to the Department, the goal of these new procedures is to ensure invoice details are correct, goods and services have been received as purchased, invoices are paid timely and duplicate invoice payments are not made.

Best practices require payment of obligations from their pre-approved authorized funds, as well as multi-level review of payments to be made. Strong internal controls regarding vendor payments not only deter fraud and the misuse of funds, but also allow management to accurately determine how funds are spent and when savings can be made, which affects both monetary and policy decisions.

Recommendations:

3) Management should document and periodically review the success of the newly implemented procedures as it pertains to the effectiveness of the process in reducing the risk of inaccurate payments.

4) The Department should consider periodically reviewing a sample of purchase orders and invoices for its larger contracts to proactively identify and rectify issues in contracting, billing, and payments.

US Peroxide Contract

The Department maintains a contract with US Peroxide, a vendor that supplies ferrous chloride to the City's Point Loma Wastewater Treatment Plant (Point Loma). Ferrous chloride is a chemical used for odor control. Deliveries occur almost daily, and invoices are sent to the Department randomly. Invoices received and paid for one purchase order for the supply of ferrous chloride during November 2008 totaled approximately $210,500.

We found that the Department's Accounts Payable section does not adequately verify the delivery amount of ferrous chloride charged by the vendor.

Deliveries of ferrous chloride are requested and made on an as-needed basis to Point Loma. Upon delivery, drivers submit a Weight Certificate and Bill of Lading to Department staff responsible for receiving deliveries. The staff member signs the Bill of Lading – essentially a delivery receipt - signifying the delivery of the chemical. Prior to delivery, a chemist analyzes the chemical to determine its specific gravity and the percentage of ferrous chloride in the solution delivered, which differs from load to load. This analysis results in the creation of a document called the Certificate of Analysis which is kept on file at Point Loma. The Weight Certificate and Bill of Lading are subsequently forwarded to Accounts Payable.

When invoiced, Accounts Payable staff use the Bill of Lading to match delivery chemical and date of delivery. While the employee signature on the Bill of Lading serves as proof of the delivery date, it does not identify the quantity of ferrous chloride delivered in a unit of measure that can be easily verified by Accounts Payable staff.

According to Accounts Payable staff, this verification of quantity is not performed because the Bill of Lading identifies the chemical delivered in pounds whereas the invoice bills the City in units of dry tons, which is also the unit of measure identified in the original contract and in the pricing agreement. Accounts Payable does not have a formula or chart supplied by either the vendor or the Department that allows a conversion from pounds to dry tons, to ensure that the delivery amount equates to the amount billed by the vendor.

Upon our request, Department staff at Point Loma were able to provide a simple formula which, when accompanied with information contained in the Bill of Lading and the Certificate of Analysis, proved successful in converting the Bill of Lading's pounds of ferrous chloride delivered into dry tons. Using the formula, our review showed appropriate billing to the Department for all of the invoices reviewed.

While our audit review of invoices from US Peroxide showed appropriate billing to the City, we consider the invoice approval and payment process by the Department's Accounts Payable staff to be inadequate. Without this essential check between the actual amounts of ferrous chloride delivered compared to the invoiced quantity, there is a potential risk of the City being charged incorrectly.

Recommendations:

5) Point Loma staff should forward a copy of the Certificate of Analysis for each delivery with each corresponding Bill of Lading to allow invoice approval staff to verify appropriate billing.

6) Accounts Payable staff should utilize the formula provided by Point Loma staff to verify that the Department is being billed appropriately for deliveries.

AmeriPride Contract

The City maintains a contract with AmeriPride Uniform Services (AmeriPride) for the provision and laundering of employee uniforms and various other items. The contract identifies 68 items to be provided to employees from various City departments, including Metropolitan Wastewater, Fleet Services, and Parks and Recreation. Items include garments such as coveralls, shirts, pants, jackets, and lab coats. Other items provided or serviced are floor mats, towels, and City-owned horse blankets. The Department maintains 14 purchase orders for AmeriPride services to employees throughout the Department. As of June 17, 2009, the Department has paid approximately $121,000 to AmeriPride for Fiscal Year 2009.

Based on our review of the Department's AmeriPride contract, we found the following issues:

- Invoices contained small inaccuracies and inappropriate charges.
- None of the invoice totals reviewed agreed with auditor calculations.
- AmeriPride repeatedly billed the City for unauthorized charges.
- AmeriPride inappropriately billed the City for sales tax on 28 percent of reviewed invoices.

Invoices contained small inaccuracies and inappropriate charges.

AmeriPride personnel noted that errors on their company's invoices are likely a result of AmeriPride's invoicing system which operates on a DOS-based computer system. According to AmeriPride, this system is generally reliable but can produce small and infrequent errors that can be corrected quickly.

AmeriPride bills the Department for services provided to each location on a weekly basis. The invoices reviewed ranged from 1 to 11 pages, each page with a potential 38 individual charges[4], identified by employee name and a vendor-provided identification number. Total invoice amounts ranged from approximately $66 to $780. [5]

Each invoice entry details an employee name and the garments serviced on behalf of that employee the previous week. Garments are identified by a vendor code and inventory amount. Each entry is concluded with a billed amount for each employee. The inventory number on the invoice is not the number used in determining charges. According to Purchasing, the inventory number is the total number of a particular garment provided to an employee. However, the City is billed only for those garments being serviced that week, which is half of the inventory amount. Therefore, in determining the actual number of garments serviced, the inventory number is divided in half and rounded down to the nearest whole number. This billing method was also confirmed by Department staff.

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[4] Each invoice page contains 19 lines, each of which allows for two separate charges.

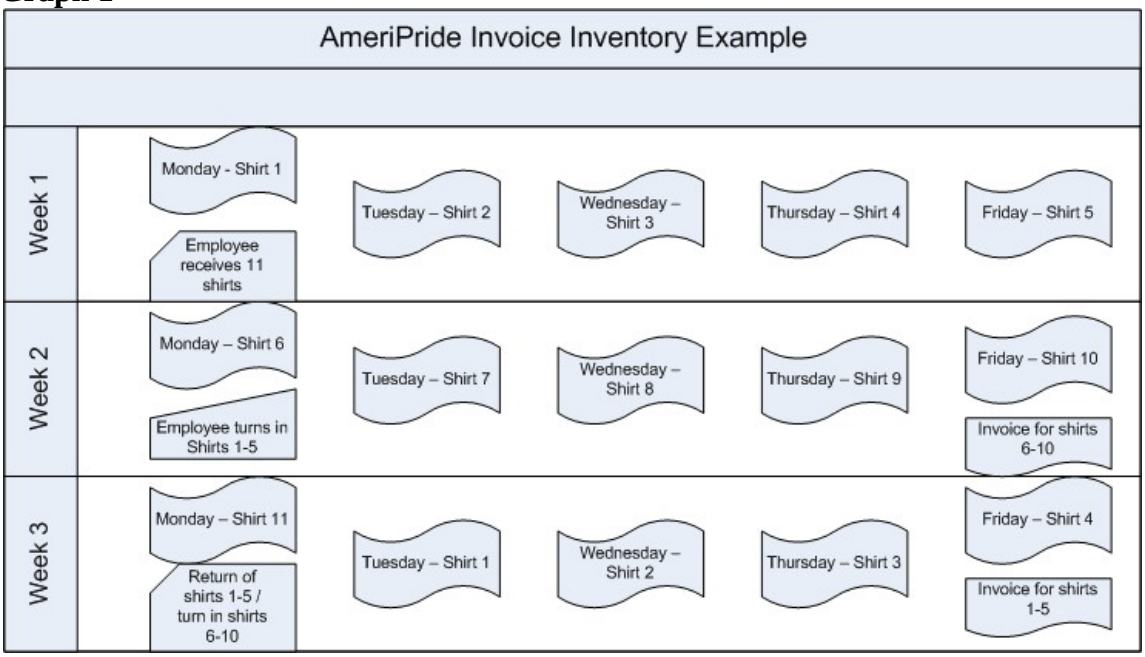
[5] For a sample AmeriPride invoice, see Appendix I. Also, see Graph 1 on page 11 for illustration of the AmeriPride invoicing process.

Our review of a sample of 40 invoices found that the amounts charged by AmeriPride for garments were consistently incorrect based on methodology provided by Purchasing staff and the Department's invoice reviewers. There were instances where identical inventory and inventory quantities among employees resulted in non-identical charges.

Three Department staff are responsible for reviewing and approving AmeriPride invoices for its 14 purchase orders; one account clerk is responsible for the two purchase orders for the Treatment and Disposal division, another for all of the Department's 11 purchase orders for the Environmental Monitoring and Technical Services division (EMTS), and the third for the Operations division purchase order. We found AmeriPride invoices initially difficult to interpret; two of the three staff members charged with invoice approval were unable to accurately instruct audit staff on how to read or review invoices.

According to Purchasing, each employee is provided garments to last for a two-week period and the City is billed for those garments of which employees are in possession. For example, a new employee might be given 11 shirts on Monday. The employee will wear a new shirt each day of the work week and is expected to return those five garments for laundering on the following Monday. The second week, the employee is in possession of six shirts; five to be worn that week and the last to be worn on the third Monday, at which time he will pick up the newly laundered shirts worn his first week. Graph 1 below illustrates this process.

Graph 1



Source: Auditor Generated using information provided by the Purchasing & Contracting Department

Therefore, in interpreting the invoice, while the invoice may state that the employee has 11 shirts, reviewers divide this amount in half and round down to 5, as this would signify those items that are not in AmeriPride's possession. This adjusted number is multiplied by the per-unit cost of service for that item, and all items attributed to this employee are calculated for a total sum.

None of the invoice totals for the invoices reviewed agreed with auditor calculations.

Our review of invoices related to AmeriPride purchase orders corresponded to 4 (29%) of the Department's 14 purchase orders, and included deliveries to 10 locations including Metropolitan Operations Center (MOC I), Operations Maintenance, Pump Station #2, and Alvarado Lab. Of the invoices we reviewed, 33 percent included one or more instances of overcharging the City. 94 percent of the invoices included one or more instances where the City was undercharged. Undercharges tended to be immaterial. For one purchase order, it appeared that AmeriPride was using an outdated version of the pricing agreement in billing the City, resulting in the Department being undercharged and AmeriPride underpaid. With all undercharges and overcharges considered, the sum of discrepancies for reviewed invoices resulted in an overcharge to the Department of approximately $450 in November 2008. However, it should be noted that the great majority of inappropriate charges were caught and adjusted by Department staff prior to payment approval. Therefore, while AmeriPride's invoices demonstrate a sum overcharge, this amount was not realized.

Additionally, we noted that 53 percent of invoices reviewed included adjustments to invoice totals made by Department staff that noticed inaccuracies or inappropriate charges. These adjustments only represented overcharges to the City. Discrepancies may be due to slight variances caused by calculation of charges for vendor services, the use of incorrect pricing agreements in vendor calculations, and/or adjustments made by Department staff.

AmeriPride repeatedly billed the City for unauthorized charges.

The City's contract with AmeriPride states that "there shall be no additional charges for adding or deleting personnel, transferring accounts, original set-up charges, size changes, and replacement." It also states that unit pricing "…shall include all delivery and freight charges." We found that 36 percent of invoices reviewed included one or more charges to the City for service charges, prep charges, size changes, and delivery charges.

In addition, we noted four charges by the vendor for services rendered on behalf of an employee who was no longer employed. Department staff made adjustments to a number of the reviewed invoices where inappropriate charges had been billed. According to one Department staff member, drivers will sometimes note inaccurate charges and change them by hand at the time of delivery. We also noted that Department staff will make the adjustments directly to the invoice prior to requesting payment for the adjusted invoice totals.

AmeriPride inappropriately billed the City for sales tax on 28 percent of reviewed invoices.

Additionally, AmeriPride personnel verified that sales tax does not apply to the City's contracted services. During out review, however, we noted that 28 percent of the invoices reviewed for the audit included tax of some kind, although minor in total. This

tax was paid in all instances. According to both Department staff and AmeriPride personnel, some of these charges are likely due to AmeriPride's use of a DOS-based computer system which, while generally reliable, can produce infrequent errors in billing and requires manual correction. A representative of AmeriPride's accounting division stated that in rare occasions inappropriate fees are automatically charged by the system when changes are made to a record, such as the addition of a new employee. If the automatic charge is not caught by vendor accounting staff it may end up on outgoing invoices. The vendor did state, however, that these occurrences are rare and that any inappropriate charges identified would be promptly credited.

In addition to a confusing and time-consuming process required to review AmeriPride invoices, the Department also faces the challenge of ensuring the appropriateness of AmeriPride charges due to the nature of AmeriPride's invoicing system, which requires manual correction to automated changes when records are added or changed in the system. Without the ability to ensure appropriate billing, there is a risk of inaccurate payments to the vendor, resulting either in the Department being overcharged or the vendor being underpaid.

Recommendations:

7) The Department should consider consolidating its EMTS AmeriPride purchase orders for efficiency in review and approval.

8) Invoice approval staff should make unified written requests to AmeriPride for system adjustments for all active Purchase Orders requiring changes. This practice will prevent confusion and multiple inquiries and requests from the Department. Follow-up on these requests should also be conducted.

9) In collaboration with AmeriPride's accounting unit and the City's Purchasing & Contracting Department, the Department's Accounts Payable staff should seek to review a number of invoices containing discrepancies and determine a clear method of invoice review and charge calculation.

10) The Purchasing & Contracting Department should evaluate the benefits of negotiating a flat fee for services based on average expenditure.

The accuracy of the charges to the City for replacement costs, ranging from $15 to $80 per charge, could not be verified.

Per the City's original contract with AmeriPride, "…The City will be responsible for the replacement of Contractor owned items lost or damaged by City employees. Replacement costs shall be based upon pricing provided on pricing pages." Replacement costs for each item listed in the contract are included on the original bid, dated April 2007. Between April 2007 and May 2008, the pricing list has seen at least two updates, prompted by renegotiations in price between AmeriPride and Purchasing. Pricing agreements detail each item's description and the current unit price for service of that garment. An updated list of charges for lost or damaged uniforms does not accompany any updated pricing agreements.

Our review of a sample of AmeriPride invoices found that eight percent of the total amount billed to the City was replacement charges for lost or damaged items. According to Department staff charged with invoice review and payment approval, they have never been provided updated replacement cost prices. While staff may have investigated the appropriateness of an individual charge, they have not investigated the appropriateness of the amount charged.

According to Purchasing, this has been an oversight which will be remedied in the future; they will require updated replacement cost listings with all future pricing agreements. While AmeriPride was able to provide a current list of replacement prices, they were unable to locate a copy of the replacement prices valid during the audit time period.

AmeriPride invoices are extremely detailed and time-consuming to review. The ability of staff to appropriately review and approve invoice payments is contingent upon complete and up-to-date information. The Department has approved payments for invoices that include charges that were unsupported by any official documentation. Our review could not determine the appropriateness of the charges as no parties involved, including AmeriPride, were able to provide a complete list of agreed-upon prices for the replacement of items. It should also be noted that while AmeriPride provided a current list of replacement prices, the list was "hand typed" in an email and is an incomplete listing of the contracted garments and items. Without adequate official documentation to provide guidance to Department invoice approval staff, the City risks paying inappropriate charges.

Recommendation:

11) The City's Purchasing & Contracting Department should ensure that it maintains up-to-date pricing lists of all appropriate possible charges, updated in its files with each new pricing agreement or change to services rendered.

Some AmeriPride invoices were not adequately processed and maintained.

Our review found that the Department's processing and maintenance of AmeriPride invoices is insufficient and inconsistent, and possibly incomplete. As noted, 11 of the Department's 14 AmeriPride purchase orders are for services supplied to its EMTS Division. EMTS invoices have been poorly maintained in the past and the department has charged another employee with the responsibility since the audit began in an effort to better maintain files and to rectify past due invoices. We were only able to secure a month of invoices for one purchase order with reasonable assurance that we had the month and documentation in its entirety. According to one review staff, other job duties do not permit the level of review necessary to adequately review incoming invoices for accuracy and appropriateness of billing, as invoices are complex and can be lengthy and time-consuming.

Procedures related to invoice payments should be streamlined to ensure consistency, appropriateness, accuracy, and promptness of payments, as such procedures reduce the risk of the Department being inappropriately charged for services rendered. Streamlined procedures will help enable account staff charged with AmeriPride invoice review to more easily identify incorrect billing as well as provide prompt and accurate payment to the vendor.

Recommendation:

12) Accounts Payable staff that review AmeriPride invoices should seek consistency in invoice review of charges prior to payment approval and follow procedures for invoice retention.

APPENDIX I

Sample AmeriPride Invoice

AmeriPride UNIFORM SERVICES
5950 ALCOA AVE
VERNON, CA 90058
PH858/621-6671 FX858/621-6675

Route	Day
013	WED

INVOICE

Account No.	Invoice No.
18688-00	L174364
Terms	Date
CHARGE	12/03/2008

ADJUSTMENTS

S. D. -WASTEWATER(MOC 9)
5655 KEARNY VILLA RD.
SAN DIEGO CA 92123

ANGIE BEASLEY
PH858/614-4518

PLEASE NOTE THE ANNUAL PRICE INCREASE ON YOUR INVOICES.

EMPLOYEE		SV	DELIVERY	QUANTITY	ITEM 1 INVENTORY	ITEM 1 DESCRIPTION	ITEM 2 INVENTORY	ITEM 2 DESCRIPTION	AMOUNT	REASON CODE	QTY	CREDIT/DEBIT AMOUNT
DOROTEO CALA	1	W6			11	FLEX 30X26 2403NVY			2.10			
MICHAEL KIMB	3	W6			11	FLEX 38X30 2403NVY			2.10			
CEDRIC MCGOW	5	W6	/	1	2	SHIRT 2XL 2364GBL	.43 4	SHIRT 2XL 2364GBL	.40			
CEDRIC MCGOW	5	W6	/	1	5	T DAC 2XL 2365GBL	.40 11	FLEX 38X34 2403NVY	.42			
CEDRIC MCGOW	5	W6			1	COVER 52T 2415PBL	.91		5.04			
HILARIO OLIV	6	W6			11	FLEX 40X34 2403NVY			2.10			
F. RAMIREZ	7	W6	/		11	FLEX 36X28 2403NVY	.42 4	SHIRT L 2364GBL	.40			.40
FELIPE RAMIR	7	W6			3	T DAC L 2365GBL	.40		3.30			
A. RIVERA	8	W6	/		11	FLEX 34X30 2403NVY	11	T DAC L 2365GBL	4.10			
F. SELDURA	10	W6	3/		10	FLEX 30X28 2403NVY	.42 1	COVER 38 2415PBL	.91 3.01			
DENISE STEEL	11	W6			11	FLEX 42X30 2403NVY			2.10			
RUBEN VITELA	12	W6			11	COVER 54 2415PBL	.91		4.55			
WILFREDO VIT	13	W6	/		3	T DAC L 2365GBL	.40 11	FLEX 32X32 2403NVY	.42 2.50			
REUBEN BARRE	201	W6			11	FLEX 36X30 2403NVY			2.10			
S. BOADILLA	202	W6	/		1.32 6	NVY C 32X28 1403NVY	.44 5	COVER 42 1406PBL	.04 3.40			
BERNARDO DUM	203	W6	/		2	SHIRT M 2364GBL	.40 3	T DAC M 2365GBL	.40			
B. DUMLAO	203	W6			11	FLEX 34X28 2403NVY	.42		2.90			-.80
GONZALO GONZ	204	W6	1/	1	4	SHIRT L 2364GBL	.40 5	T DAC L 2365GBL	.40			

W/ 75 C1.00

Total Before Adjustment
Net Adjustment 1.20
Adj.Tax
FINAL TOTAL

Customer Signature X
ADJ Approval
TOTAL FORWARD

All rental items remain the property of supplier.
We charge for all lost or destroyed merchandise.
This delivery is in accordance with our Rental Service Agreement
PAGE 1
Thank You!

AmeriPride UNIFORM SERVICES
5950 ALCOA AVE
VERNON, CA 90058
PH858/621-6671 FX858/621-6675

Route	Day
013	WED

INVOICE

Account No.	Invoice No.
18688-00	L174364
Terms	Date
CHARGE	12/03/2008

ADJUSTMENTS

S. D. -WASTEWATER(MOC 9)
5655 KEARNY VILLA RD.
SAN DIEGO CA 92123

ANGIE BEASLEY
PH858/614-4518

EMPLOYEE		SV	DELIVERY	QUANTITY	ITEM 1 INVENTORY	ITEM 1 DESCRIPTION	ITEM 2 INVENTORY	ITEM 2 DESCRIPTION	AMOUNT	REASON CODE	QTY	CREDIT/DEBIT AMOUNT
G. GONZALEZ	204	W6	/		.68 9	FLEX 36X30 2403NVY	.42 2	COVER 46 2415PBL	4.19			
NICKOLAS GRE	205	W6	/		1.729	SHIRT L 1364GBL	.43 11	NVY C 38X26 1403NVY	.44-2.2			
NICKOLAS GRE	205	W6			2	COVER 46 1406PBL	1.04		4.96			
VIRGILIO MIR	206	W6	/		11	SHIRT XL 2364GBL	.40 2	FLEX 36X30 2403NVY	.42			
VIRGILIO MIR	206	W6			9	FLEX 38X30 2403NVY	.42 - 1.68		4.10			
R. NETTLES	209	W6	/		8	FLEX 46X32 2403NVY	.42 3	COVER 56 2415PBL	2.59			
HENRY O.	210	W6	/		5	T DAC M 2365GBL	11	FLEX 36X26 2403NVY	2.90			.80
SAMUEL VALEN	211	W6	/		6	SHIRT XL 2364GBL	.42 5	T DAC XL 2365GBL	.80			
S. VALENZUEL	211	W6			11	FLEX 38X30 2403NVY	.2.10		4.10			
PAUL ACOSTA	250	W6			2	COVER 44 1406PBL			1.04			
E. BAUTISTA	251	W6	/		10	FLEX 34X28 2403NVY	1	COVER 42 2415PBL	3.01			
CRAIG BREWST	252	W6			11	NVY C 38X84 1403NVY	.44		2.20			
EDWIN CORPUS	253	W6	3		11	NVY C 32X28 1403NVY			2.20			
EMMANUEL GLE	254	W6	/		1	SHIRT L 2364GBL	.40 4	T DAC L 2365GBL	.80			1.20
E. GLEYO	254	W6			11	FLEX 34X28 2403NVY			3.30			
RODOLFO LIZA	255	W6			11	NVY C 32X30 1403NVY			2.20			
JOHN MAJORS	256	W6	/		3	T DAC 4XL 2365GBL	.40 10	FLEX 48X30 2403NVY	2.10			
JOHN MAJORS	256	W6			1	FLEX 48X34 2403NVY			2.50			
SONNY MERCAD	257	W6	/		1	SHIRT M 2364GBL	11	FLEX 32X28 2403NVY	2.50			

W/ 5 C1.00

Total Before Adjustment
Net Adjustment 2.00
Adj.Tax
FINAL TOTAL

Customer Signature X
ADJ Approval
TOTAL FORWARD

All rental items remain the property of supplier.
We charge for all lost or destroyed merchandise.
This delivery is in accordance with our Rental Service Agreement
PAGE 2
Thank You!

riPride UNIFORM SERVICES

5950 ALCOA AVE
VERNON, CA 90058
PH858/621-6671 FX858/621-6675

Route	Day
013	WED

INVOICE

Account No.	Invoice No.
18688-00	L174364
Terms	Date
CHARGE	12/03/2008

S. D. -WASTEWATER(MOC 9)
5655 KEARNY VILLA RD.
SAN DIEGO CA 92123

ANGIE BEASLEY
PH858/614-4518

EMPLOYEE		SV	DELIVERY	QUANTITY	INVENTORY	ITEM 1 DESCRIPTION	INVENTORY	ITEM 2 DESCRIPTION	AMOUNT
ERNESTO REVI	258	W6	1		11	NVY C 32X30 1403NVY			2.20
LARRY SCHWEI	259	W6			11	NVY C 42X30 1403NVY			2.20
STAN HENSLEY	416	W6	2/		9	SHIRT 2XL 2364GBL	4	2COVER 54 2415PBL	.91
STAN HENSLEY	416	W6	3		9	FLEX 40X32 2403NVY	42		4.19
DAVID LECROY	556	W6	2/		5	SHIRT 2XL 2364GBL	40	5T DAC 2XL 2365GBL	.40
D. LECROY	556	W6	/ 1		10	FLEX 38X32 2403NVY		1COVER 48 2415PBL	4.61

Balances as of 12/01/2008	Current	1-30	31-60	61+
	654.89	0.00	2.10	0.00

ROUTE CONTACT: LLOYD MARTIN

NO. 75 C1.00

TAX RATE	SDC 7.75
TAX BASE	
TAX	

TERMS NET 10 DAYS
ADJ Approval

TOTAL 94.29

Customer Signature X

All rental items remain the property of supplier.
We charge for all lost or destroyed merchandise.

This delivery is in accordance with our Rental Service Agreement

PAGE 3 END Thank You!

ADJUSTMENTS

ITEM 1
ITEM 2

REASON CODE	QTY	CREDIT/DEBIT AMOUNT

Total Before Adjustment	94.29
Net Adjustment	3.20
Adj.Tax	
FINAL TOTAL	91.09

Source: Izumi Rhoades, Administrative Aide II, Wastewater Department

APPENDIX II

State of California Use and Sales Tax Regulation 1525 Annotation 275 & 440

(b) WATER ADDITIVES

275.0280 **Chemicals.** The following chemicals added to water which is resold remain in the water and may be purchased ex-tax:

calcium hypochlorite	sodium hydroxide	
quick lime	hydrated lime	
chlorine	sodium hypochlorite	
soda ash	lime	
copper sulfate 4/9/64	sodium silicofluoride	11/21/62.

275.0300 **Aluminum Sulfate.** Ninety-one percent of the aluminum sulfate used in treating water remains in solution and is sold along with the water, so that sales of the aluminum sulfate to the water supplier are exempt sales for resale. 11/29/62.

275.0320 **Anhydrous Ammonia, Ammonium Sulfate, and Sodium Chlorite.** These chemicals may be purchased ex-tax when purchased for treatment of water by a water service company. 6/19/63.

275.0340 **Chlorine** added by a city to its water supply for the purpose of destroying undesirable micro-organisms and objectionable chemical substances becomes part of the delivered product as chloride ions and is bought for resale; consequently, a resale certificate may be furnished to the chlorine supplier even though the sale of the water itself is exempt from sales tax. 5/4/60.

275.0360 **Diatomaceous Earth.** The sale of diatomaceous earth to a water treatment plant is taxable where the product is used as a filtering agent to remove impurities and does not dissolve or become part of the water. 4/27/64.

275.0400 **Ferric Sulphate** sold for use in treating a water supply, is an exempt sale for resale. 10/4/65.

275.0420 **Sodium Chloride** may be purchased ex-tax for resale where it is used in a water softening process whereby its sodium ions are incorporated in the water. 9/5/62.

THE CITY OF SAN DIEGO

M E M O R A N D U M

DATE: July 23, 2009

TO: Eduardo Luna, City Auditor
via Jim Barrett, Director of Public Utilities 7.24.09

FROM: Darlene Morrow-Truver, Deputy Director of Employee Services and Internal Control, Public Utilities Department

SUBJECT: Metropolitan Wastewater Branch (MWWD) Contract Compliance Audit

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The following is MWWD's response to your audit report (Report) dated July 15, 2009, which you undertook and completed at our request. The Report lists twelve (12) recommendations which are restated in this memo followed by our response to each recommendation:

1) The Department should periodically review contracts for tax exempt chemicals to ensure that they are not paying unnecessary sales tax. As part of this review, the Department should ensure that Purchasing & Contracting is aware of the use of chemicals purchased for each purchase order.

   Response: MWWD agrees. We will conduct an analysis of the active chemical contracts periodically to insure that we are paying sales tax in accordance with State law. This practice will begin early in FY2010 and will be added to the Public Utilities Department's Internal Controls Group work-plan. In addition, we will meet with Purchasing & Contracting to review our chemical purchases.

2) The Department should request reimbursement from Olin Chlor for sales tax paid on tax exempt purchases of sodium hypochlorite for the past three years. Upon further review, the Department should request refunds for any other tax-exempt chemicals identified.

   Response: MWWD agrees with the issue cited on page 5, under **Olin Chlor,** "The Department has inappropriately paid an estimated $80,500 in sales tax to Olin Chlor." While we agree that we inadvertently paid sales tax for chemicals that are tax exempt when added to water for sale, we need to analyze further to determine the amount of sales tax that should not have been paid. Before seeking a refund, we would

recalculate the amount based on actual sales taxes paid for this chemical and vendor, at NCWRP and SBWRP only, in FY's 2007, 2008, and 2009, and adjust that amount by the gallons of sodium hypochlorite purchased and used for odor control, hence not added to water, and apply that percentage of usage and cost to those taxes paid. That is, the total refund request should therefore be the sales tax paid on the cited NCWRP and SBWRP PO's, less the amount estimated by percentage for odor control application = amount of sales tax inappropriately paid for application to water sold.

3) Management should document and periodically review the success of the newly implemented procedures as it pertains to the effectiveness of the process in lessening the risk of inaccurate payments.

   Response: MWWD agrees and will add to the Public Utilities Department's Internal Control Group work-plan.

4) The Department should consider periodically reviewing a sample of purchase orders and invoices for its larger contracts to proactively identify and rectify issues in contracting, billing, and payments.

   Response: MWWD agrees and will add to the Public Utilities Department's Internal Control Group work-plan.

5) The Treatment Plant staff should forward a copy of the Certificate of Analysis for each delivery with each corresponding Bill of Lading to allow invoice approval staff to verify appropriate billing.

   Response: MWWD agrees. This practice will be adopted in our accounts payable procedures.

6) Accounts Payable should utilize the formula provided by Treatment Plant staff to verify that the Department is being billed appropriately for deliveries.

   Response: MWWD agrees. This practice will be adopted in our accounts payable procedures.

7) The Department should consider consolidating its AmeriPride purchase orders for efficiency in review and approval.

   Response: MWWD agrees to evaluate the benefits of consolidating AmeriPride purchase orders and will adopt changes as appropriate.

8) Invoice approval staff should make unified written requests to AmeriPride for system adjustments for all active purchase orders requiring changes. This practice will prevent confusion and multiple inquiries and requests from the Department. Follow-up on these requests should also be conducted.

Response: MWWD agrees. This practice will be adopted in our accounts payable procedures.

9) Together with AmeriPride's accounting unit and the City's Purchasing & Contracting Department, the Department's account staff should seek to review a number of invoices containing discrepancies and determine a clear method of invoice review and charge calculation.

   Response: MWWD agrees. MWWD will contact Purchasing and AmeriPride to review invoicing process to determine if enhancements can be made.

10) The Purchasing & Contracting Department should evaluate the benefits of negotiating a flat fee for services based on average expenditure.

    Response: It is our understanding that the Purchasing and Contracting Department will respond to this recommendation.

11) The Purchasing & Contracting Department should ensure that it maintains up-to-date pricing lists of all appropriate possible charges, updated in its files with each new pricing agreement or change to services rendered.

    Response: It is our understanding that the Purchasing & Contracting Department will respond to this recommendation.

12) Account staff that review AmeriPride invoices should seek consistency in invoice review of charges prior to payment approval.

    Response: MWWD agrees. Accounts Payable will review and develop a consistent practice which will be adopted in our accounts payable procedures.

In conclusion, MWWD appreciates your review of these contracts and all of the recommendations in this report. We will adopt changes to our accounts payable procedures and document those changes in written guidelines. As you know, the Public Utilities Department created an Internal Control work group that will be fully implemented in FY2010. This group will insure that we follow up on all of your recommendations as indicated in this response memorandum.

Thank you for your insights and recommendations.

Darlene Morrow-Truver
Deputy Director, Employee Services and Internal Control

ELL/ell

Attachment: Metropolitan Wastewater Department Contract Compliance Audit dated July 15, 2009.

cc: Hildred Pepper, Director of Purchasing & Contracting
Public Utilities Internal Controls Program Manager

THE CITY OF SAN DIEGO

M E M O R A N D U M

DATE: July 2, 2009

TO: Kyle Elser

FROM: Hildred Pepper, Director Purchasing & Contracting

SUBJECT: Responsibilities of Contract Administrators

In response to your request for my review and comments on the report for the Metropolitan Wastewater Department Contract Compliance Audit (Audit), I find the report acceptable. I have the following comments regarding recommendations 9, 10 and 11.

Regarding Recommendation 9, Purchasing & Contracting is always willing to assist the departments in improving vendor performance, including invoice charge discrepancies. However, in keeping with City requirements, we must insure that separation of purchasing and invoicing/bill payment functions remain intact. In an effort to maintain that separation, a method of invoice review and charge calculation should be established prior to the implementation of an Agreement

For Recommendation 10, Purchasing & Contracting (P&C) is in the initial stage of preparing a new solicitation for uniforms. With assistance from the departments, where they can with a high degree of accuracy and specificity determine their requirements, P&C will evaluate different pricing methods, including using the flat fee for service based on average expenditure as recommended in the Audit. It should be noted that this flat fee methodology is not industry standard. Another option being considered is actually buying the uniforms outright and contracting the laundry services. A new solicitation will list the various options as determined by the departments and P&C.

Concerning Recommendation 11, price schedules are up to date based upon the items in the Agreement. Departments should not authorize payments for non-contract items. If a non-contract item(s) is needed, the Department should contact P&C to amend the Agreement to include the item(s). Prior to amending the Agreement, P&C will negotiate the item pricing, delivery, etc. prior to adding the item to the contract. Department Contract Administrators are responsible for ensuring the contractor's billings are in accordance with the approved contract price. Annually this contract is reviewed and pricing is updated in accordance with the appropriate contract provisions contained within the contract.

cc: Wally Hill, Eduardo Luna, Sonja Thorington, Karan Wolff

THE CITY OF SAN DIEGO

M E M O R A N D U M

DATE: July 23, 2009

TO: Kyle Elser

FROM: Hildred Pepper, Director Purchasing & Contracting

SUBJECT: Recommendation 11 from Metropolitan Wastewater Department Contract Compliance Audit

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This memo is in response to your request for my additional comments and clarification on Recommendation 11 in the report for the Metropolitan Wastewater Department Contract Compliance Audit.

I appreciate the opportunity to review and comment on the clarification provided for Recommendation 11. Upon further review of the agreement, Purchasing & Contracting (P&C) has determined that the vendor did not provide P&C with pricing for lost or replacement items. To remedy the lapse, Purchasing and Contracting will confer with the vendor to reach consensus on pricing for lost and damaged items, as well as an amortization schedule detailing the percent clothing is amortized from the date of issue. Copies of the amended agreement will be distributed to all user departments.