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Missouri State Auditor

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City Utilities of Springfield, Missouri

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Missouri State Auditor
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YELLOW SHEET

The following findings were included in our audit report on City Utilities of Springfield, Missouri.

City Utilities (CU) customers may be paying too much for some utility services as a result of subsidization of non-utility activities of the city, subsidization of other utility departments from electric revenues, questionable spending, and granting public funds in possible violation of the Missouri Constitution. The Electric Department continues to have a significant increase in operating income each year, and CU has not complied with its own rate policy standards, which requires an outside consulting firm to review rates and report the findings to the board at least every five years. Rates for utility services should be set to cover the costs of producing and delivering services, and utility services should not generate profits to fund (through subsidization) other services provided by the city or other utility departments or provide the opportunity for CU to spend monies unnecessarily.

CU has provided several millions of dollars to the city for various projects over the past few years. As a result, CU's customers are being required to subsidize the cost of some city services through the payment of their utility bills. Also, some utility departments need continued financial support from the electric department to cover their cost of operations. The electric department provided funding totaling over $6.3 million during the year ended September 30, 2006 to the transit department, gas department, and SpringNet® to cover the cost of operations.

Numerous disbursements and contributions of services totaling at least $259,000 do not appear to be a prudent, reasonable, or necessary use of utility funds and some may violate the Missouri Constitution. Some unnecessary spending included a 2006 Family Day Picnic held to show appreciation for the employees and their families with costs totaling over $19,000. Monies were spent for catering, decorations, and party supplies. Numerous other examples of unnecessary spending were noted in the report. Safety and service awards valued at over $52,000 have been given to employees, which do not appear to be prudent, reasonable, or a necessary use of utility funds, and CU paid employees $26,050 in finder's fees for identifying and reporting illegal use of utility services. Such identification would appear to be part of their regular job duties. Further, CU contracted with various entities to provide funding totaling at least $321,000 without ensuring all contractual requirements were met or requiring adequate documentation of how those monies were used.

CU suffered a financial loss of more than $2.7 million during the 2007 natural gas hedging season, and the financial information presented to the Board of Public Utilities regarding the loss was incomplete. In addition, documentation of the effect of a policy

(over)

change that significantly increases CU's possible liability in the natural gas hedging market was not presented to the board. CU uses natural gas hedging as a financial tool to help reduce the risk of increasing natural gas prices. CU buys natural gas options at a specified market price to be exercised during the peak heating season. If the market price rises above the option price paid, CU can exercise the option and recognize a financial gain; however, if market price decreases below the option price paid, the utility suffers a financial loss.

CU did not prepare a cost benefit study before entering into a contract with The Energy Authority (TEA) in 1998, has not adequately documented their continued investment on an annual basis, and has not taken full advantage of every opportunity to provide oversight to TEA operations. TEA is a nonprofit corporation, and CU has a 7.14 percent ownership interest. CU has a current investment in TEA of more than $2.4 million and has guaranteed more than $9.6 million in cash reserves to TEA as of September 30, 2006. CU also paid an initial membership fee of $867,360 in 2000 to become an owner, and additional costs totaling over $4.7 million to trade energy were incurred by the utility from 2001 through 2006.

SpringNet® is a division of CU, which offers telecommunication services. SpringNet® has failed to comply with several provisions of a Public Service Commission (PSC) order regarding the necessity to operate without continued financial assistance from the rest of the utility, and has failed to comply with state law which limits term agreements on telecommunications services to five years. CU's internal auditor had noted this same issue. SpringNet® has not followed the terms of its service contracts with customers regarding delinquent accounts and has developed more lenient practices. CU has spent over $6 million on SpringNet® Underground, which provides computer operations hosting services within a local underground mine, without performing preliminary feasibility studies and developing a formal ongoing business plan for this activity.

CU uses alliances, standing purchase orders, and blanket orders as purchasing tools for significant expenditures without the use of annual competitive bidding for supplies. For example, CU spent over $6.1 million during 2006 in four alliances to purchase supplies. These alliances allow the utility to purchase items that are only bid in the first year of the alliance and extended for up to four years without annual competitive bidding.

Proposals were not always solicited for legal services, a contract for legal services was approved without any review of the compensation to be paid, and legal contract renewals were sometimes signed by law firms several days after the effective date of the contract.

Meals and food purchased with procurement cards appear excessive, and CU lacks a comprehensive food policy. CU spent approximately $80,000 in 2006 for meals and food provided during employee meetings, training sessions, retirement receptions, employee recognition events, board meetings, public marketing events, and other external meetings. Numerous procurement card expenditures did not appear to be a prudent and necessary use of public funds including a barbeque grill, toy store gift cards, mint tins, and dishes, glassware, and flatware used by the board and general management for meals.

CU paid approximately $342,000 for corporate and individual membership dues. Several employees were reimbursed for the same civic organization memberships, and several employees were reimbursed for multiple individual memberships. Additionally, numerous employee reimbursements for expenses did not appear to be a prudent or necessary use of public funds.

CU provides incentives to some developers that are not addressed in the utility's extension policy. CU did not always enter into written contracts for developer reimbursements, did not require the developer to submit documentation of actual costs incurred to support reimbursements made, did not inspect and audit the developer's records in accordance with CU's extension policy, and some reimbursements were not calculated in accordance with policy. CU paid over $1.35 million in reimbursements and incentives to developers during the year ended September 30, 2006. Reimbursements are based on a written extension policy and occur when CU reimburses costs to developers who install electric, gas or water service to newly developed areas.

CU did not perform or update cost benefit studies to evaluate the necessity for some marketing and communication services, print shop services, or the onsite health clinic. CU's marketing and communication costs totaled over $1.1 million. Several print shop projects including commemorative picture books of the 2007 ice storm (given to the employees) and commemorative books of the 50th anniversary of James River Power Station and water system did not appear to be a prudent or necessary use of resources.

CU used varying market standards to establish a salary plan for its General Manager and Associate General Managers resulting in significantly higher salaries for these positions. Salaries for these positions were paid according to a different marketing standard than other employees and ranged from $124,359 to $326,484. Additionally, the General Manager's contract provides for a severance package valued at over $517,000.

Several controls and procedures over cash handling at the main office, TecHouse, and with door-to-door collectors are in need of improvement. CU collected approximately $366.8 million in utility payments during the year ended September 30, 2006.

The pumps at the Stockton Lake Pumping Station failed in 2005 and 2006, and CU has not fully implemented the recommendations made by a consultant regarding the pump station failures.

While CU has a tree trimming management policy, the utility has not developed procedures to measure its performance of this policy. Various utility industry publications have indicated the lack of tree trimming and brush removal is the number one cause of controllable power outages.

Also included in the report are recommendations related to bidding and purchasing policies, utility system controls and procedures, transit department, fleet management and vehicle allowances, and closed meeting minutes and accounting procedures.

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CITY UTILITIES OF SPRINGFIELD, MISSOURI

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STATE AUDITOR'S REPORT

SUSAN MONTEE, CPA
Missouri State Auditor

To the Members of the Board
of City Utilities of Springfield
and
the Honorable Mayor and
Members of the City Council of the
City of Springfield, Missouri

The State Auditor was petitioned under Section 29.230, RSMo, to audit the City of Springfield, Missouri. City Utilities of Springfield (CU), a component unit of the city, engaged KPMG, LLP, Certified Public Accountants (CPAs), to audit its financial statements for the year ended September 30, 2006. To minimize duplication of effort, we reviewed the report and substantiating working papers of the CPA firm. The scope of our audit of City Utilities of Springfield included, but was not necessarily limited to, the year ended September 30, 2006. The objectives of this audit were to:

1. Perform procedures to evaluate the petitioners' concerns.

2. Review internal controls over significant management and financial functions.

3. Review compliance with certain legal provisions.

To accomplish these objectives, we reviewed minutes of meetings, written policies, financial records, and other pertinent documents; interviewed various personnel of City Utilities of Springfield, as well as certain external parties; and tested selected transactions. Our methodology included, but was not necessarily limited to, the following:

1. We obtained an understanding of petitioner concerns and performed various procedures to determine their validity and significance.

2. We obtained an understanding of internal controls significant to the audit objectives and considered whether specific controls have been properly designed and placed in operation. However, providing an opinion on internal controls was not an objective of our audit and accordingly, we do not express such an opinion.

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3. We obtained an understanding of legal provisions significant to the audit objectives, and we assessed the risk that illegal acts, including fraud, and violations of contract, grant agreement, or other legal provisions could occur. Based on that risk assessment, we designed and performed procedures to provide reasonable assurance of detecting significant instances of noncompliance with the provisions. However, providing an opinion on compliance with those provisions was not an objective of our audit and accordingly, we do not express such an opinion.

Our audit was conducted in accordance with applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and included such procedures as we considered necessary in the circumstances. The work for this audit was substantially completed by September 2007.

The accompanying History, Organization, and Statistical Information is presented for informational purposes. This information was obtained from CU's management and was not subjected to the procedures applied in the audit of CU.

The accompanying Management Advisory Report presents our findings arising from our audit of City Utilities of Springfield.

Additional reports, No. 2007-30, *Thirty-First Judicial Circuit, City of Springfield, Missouri, Municipal Division*, and No. 2007-74, *City of Springfield, Missouri,* were issued in August and December 2007, respectively.

Susan Montee, CPA
State Auditor

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MANAGEMENT ADVISORY REPORT -
STATE AUDITOR'S FINDINGS

1. Utility Rates

Utility rates charged to customers may not be set at a level consistent with the costs of providing the related services. City Utility (CU) customers may be paying too much for some utility services as a result of activities discussed throughout this report including: subsidization of non-utility activities of the city; subsidization of some CU departments from the revenue of others; questionable spending; and granting public funds in possible violation of the Missouri Constitution. The following table shows operating income (loss) by department for the last several years:

	Year ended September 30,				
Department	2006	2005	2004	2003	2002
Electric	$ 25,386,712	19,623,089	14,037,013	8,990,409	238,991
Gas	(678,508)	(726,090)	(1,392,390)	8,370	(809,353)
Water	2,164,851	4,038,865	1,998,042	1,652,104	1,537,243
Telecommunications(1)	204,117	(490,282)	(587,654)	550,173	313,748
Transit	(4,209,118)	(4,026,364)	(3,536,211)	(3,476,898)	(3,230,037)

(1) Includes internal telephone services, trunked radio system, SpringNet® and SpringNet® Underground.

As this table indicates, the electric department continues to have a significant increase in operating income each year. Additionally, the water department has had small increases in operating income each year, while some other departments consistently incur an operating loss. The customer base of the departments varies, and some customers are charged more for electric utilities which has offset the cost of some other services which they may not receive. Subsidization is discussed more in detail at MAR number 2.

The chart below illustrates how rates for the electric, gas, and water departments have changed over the last several years:

	Year ended September 30,				
Department	2006	2005	2004	2003	2002
Electric per thousand residential kilowatt hours	$ 71.40	66.80	61.70	61.70	58.35
Gas per sixteen therms	19.15	23.34	19.70	16.96	16.61
Water per thousand cubic feet	23.55	22.85	22.15	21.50	20.90

According to the city charter, it is the responsibility of the Board of Public Utilities to set rates to be charged for services, subject to the approval of the City Council. Electric and gas rates are based on basic charges and are adjusted periodically through out the year for fuel costs to the utility. While electric has had three percent base rate increases in 2006 and 2003 and gas has had a two percent base rate increase in 2006, rates have continued to change annually because of the adjustments for fuel costs. The base rate for water service has steadily increased each year from 2002 to 2006. In addition, bus fares have remained the same since 1998.

CU regularly cites public rate studies to demonstrate that their rates are low compared to other utilities nationwide; however, CU has not complied with its own rate policy standards which state that an outside consulting firm should review rates and report their findings to the board at least every five years. An outside evaluation was last performed and reported to the board in August 2001. CU has scheduled an outside evaluation to be performed during the year ending September 30, 2008. CU personnel indicated that their utility rates are low in part because of decisions made in the 1950's to 1970's to build low cost coal power stations to generate power that are now paid for. While CU has internally reviewed and adjusted electric, gas, and water rates, it is essential that the utility perform a comprehensive review of all rates to ensure they are set at a level consistent with the costs of providing of each specific utility service.

Utility revenues should only be used to fund the operations of the related utility services. Rates for utility services should be set to cover the costs of producing and delivering services (including administrative costs). In addition, these utility services should not generate profits to fund (through subsidization) other services provided by the city or other utility departments or provide the opportunity for CU to spend monies unnecessarily.

WE RECOMMEND the Board of Public Utilities ensure utility rates are set to generate revenues as necessary to produce and deliver the related service.

AUDITEE'S RESPONSE

The Board of Public Utilities actively reviews CU services and associated costs. CU consistently has one of the lowest rates in the state and nation, which does not happen by accident. Management works to provide reliable, affordable and responsible services that add to the quality of life in Springfield. The CU rates, with the exception of transit fares, are designed to yield the revenue necessary to provide the level of services required by utility customers. Actual revenues, however, are subject to weather, customer growth, and, in the case of off-system electric sales, the availability of excess electricity and market conditions.

Since electric, natural gas, and water utilities sales volumes are weather dependent and significant variances occur in weather patterns in CU service area, it is impossible in any given year to generate the exact revenues required to produce and deliver a given service. Expenditure patterns also change, which makes identification of exact revenue requirements *impossible for any given year. The rating agencies have viewed CU very favorably in creating a Rate Stabilization Fund to accommodate these year-to-year changes.*

During the annual budget and five-year outlook process, analysis is performed to assure that each utility service is projected to fund its respective burdens over time. For example, revenues generated for each utility service must be adequate to cover operating and maintenance expenses, capital replacement and expansion, and debt service. In addition, electric and natural gas utilities must also generate adequate income to fund the transit shortfall. It is through this process that a determination is made for 1) timing of increases and, 2) percentage of increases necessary for funding a shortfall within a given commodity.

The Board will continue to adopt and set utility rates that are designed to generate appropriate revenues.

2. Utility Revenues Used for Subsidization

CU has provided several millions of dollars to the city for various projects over the past few years. As a result, CU's customers are being required to subsidize the cost of some city services through the payment of their utility bills. Also, some utility departments need continued financial support from the electric department to cover their cost of operations. The electric department provided funding totaling over $6.3 million during the year ended September 30, 2006 to the transit department, gas department, and SpringNet® to cover the cost of operations.

A. CU has provided financial support (subsidies) to the city worth millions of dollars, and as discussed in MAR number 1, the utility needs to consider the impact of these subsidies on customer utility rates, especially electric rates. CU provides these subsidies at the request of the City Council. Some examples of financial support provided to the city are as follows:

- CU has agreed to share certain revenues with the city in excess of Payment in Lieu of Taxes (PILOT) established by the city charter. CU paid $1,240,550 to the city during the year ended September 30, 2006 for (PILOT) on water revenues. These payments are not required by the city charter, but are based on a resolution passed in October 1998 by CU to pay the city 4 percent of water revenues. Water services were not provided by CU at the time the city charter was established. CU paid the city PILOT amounts for electric, gas, and transit totaling $11,238,428 and provided utility services totaling $7,678,430 during the year ended September 30, 2006 which are required by city charter.

- CU entered into an agreement with the city in July 2002 to provide an annual discount of $645,000 for telecommunication services. Telecommunication services were not provided by CU at the time the city charter was established.

- CU sold land to the city in November 2005 for $265,000 less than market value. The land is located near the Blackman water treatment facility and will be used by the city to build a fire station.

- CU entered into two 25 year leases of land to the Springfield-Greene County Park Board at no cost to the city, one in June 2006 and another in December 2006. The land in the first lease is located near Springfield Lake, is used for a park, and according to CU is valued at approximately $1.47 million. The other land is located near the Blackman water treatment facility, will be used for a future park and a family recreation center, and according to CU is valued at approximately $1.2 million. The leased land was purchased by CU as buffer land for CU's facilities. CU indicated they do not incur maintenance costs for these properties due to these lease agreements.

- CU has agreed to share equally future revenues from the Landfill Gas to Energy Project located at the city's landfill with the city. The revenues from this project during the city's fiscal year ended June 30, 2006 totaled approximately $994,000. In addition, CU will be required to pay a 3% PILOT on these revenues to the city based upon the city's charter. CU also agreed to repay the city's costs to construct the Gas Collection and Condensate System (GCCTS) component of the project (approximately $1.5 million); however, the city will retain ownership of all assets associated with the GCCTS.

- CU agreed to provide $275,000 in funding to the city in April 2004 to convert traffic signal lamps owned by the city to more energy efficient lamps. According to CU personnel, this will reduce future free services provided to the city.

- CU provided $1 million in funding for a city water feature at Jordan Valley Park from September 2000 through August 2001.

While many of these items provide benefit to city residents, it is questionable whether the city and CU should fund these services from utility revenues. Customer utility payments represent user charges which are intended to cover the cost of providing the related services. It does not appear appropriate to subsidize other city operations from these monies.

B. Some departments need continued financial support from the electric department to cover their cost of operations. The electric department subsidizes other utility departments as follows:

- The transit department does not generate sufficient revenues to cover the costs of operations. Revenues generated from bus fares and advertising covered only 10 percent of total operating expenses for the year ended

September 30, 2006. Electric department revenues provided approximately $4.2 million to operate the transit department.

The city charter requires CU to operate and fund the public transit system. CU has operated the public transit system for the City of Springfield since 1945, when it was common for utilities to operate the public transit system because the system consisted of mostly electric streetcars, and it was convenient for electric companies to operate the streetcars. As transportation has evolved and moved to bus transportation, most cities have abandoned the utility owned transit system in favor of a transit authority operated by an independent board. According to CU personnel, CU is the only municipality in the United States which operates a public transit system.

The transit department has historically operated at a loss and has been subsidized by other utility departments. In addition, federal funding of this system is expected to decline significantly in 2008 and in future years because of the department's ineligibility to receive funding due in part to the growth of the city. CU has also made tentative plans to build another transit facility and expand the transit bus storage building that will accommodate larger buses which may require additional subsidies by electric funds.

CU needs to continue to closely monitor the ongoing financial condition of the transit department and work with the city to consider alternative funding sources. If CU and the city desire to continue the current level of services, they should consider methods of increasing revenues or reducing costs.

- The gas department relies upon electric department revenues to subsidize its operations. For the year ended September 30, 2006, the gas department had an operating loss of $678,508, which had to be offset by revenues of the electric department.

- SpringNet® relies upon electric department revenues to subsidize its operations. SpringNet® provides telecommunication services and operates an underground data storage known as the SpringNet® Underground. Electric department revenues provided approximately $1.5 million to operate SpringNet® during the year ended September 30, 2006. (See MAR number 7 for other concerns related to SpringNet®)

Revenues of the electric department represent user charges which are intended to cover the cost of providing the related services. It does not appear appropriate to subsidize the transit and gas departments, and SpringNet® and SpringNet® Underground from these monies.

As a result of these situations, utility rates may be set higher than necessary to provide the related service (as noted in MAR number 1) and CU's electric customers are being required to subsidize the costs of other city services and these departments through the payment of their utility bills.

WE RECOMMEND the Board of Public Utilities closely monitor the ongoing financial condition of each department, and limit expenditures from utility funds (electric, gas, and water) to only those which are necessary to operate those specific utilities. In addition, work with the city to consider alternative funding sources for the transit system.

AUDITEE'S RESPONSE

The Board manages CU as a community utility and asset, providing utilities and services to add to the quality of life in the Springfield area. The Board of Public Utilities closely monitors cash and services provided to the City of Springfield to ensure CU is in line with contributions provided by other public utilities. The Board and management balance fiscal responsibility with the community's desire for an effective public transit system. In addition, the Board and City Council have addressed the need for additional revenues for the transit system.

The Board will continue to monitor the financial condition of each utility department and the level of cash and services provided to the city.

3. Expenditures

Numerous disbursements or contribution of services totaling at least $259,000 were made that do not appear to be a prudent, reasonable, or necessary use of utility funds and some may violate the Missouri Constitution. CU contracted with various entities to provide funding totaling at least $321,000 without ensuring all contractual requirements were met or requiring adequate documentation of how those monies were used. Also, procedures have not been established to ensure operating costs of the trunked radio system are properly allocated. CU does not have adequate controls and procedures over the usage of its cellular telephones, and does not follow a consistent policy for hiring executives.

A. Some disbursements or contributions of services did not appear to be prudent, reasonable, or a necessary use of utility funds. Some of these disbursements or contributions of services may also violate the Missouri Constitution. Examples of some of these are as follows:

Name		Amount	Purpose
Downtown Community Improvement District	$	89,091	Capital and annual operating expenditures for wireless internet service provided to downtown area
American Public Gas Association		40,000	Research and development
Springfield Business Development Corporation (SBDC) and Springfield Chamber of Commerce		21,064	Five year pledge in the Partnership for Prosperity Program, legislative and annual meetings, meals, and other sponsorships
Springfield Public Schools Foundation		19,297	Science institute, partners in education, teacher appreciation banquet, and students go to work
Urban District Alliance		16,000	Festival of Lights-annual contribution and institutional sponsorship
Central High School		6,500	Annual donation
Battlefield Mall's Safe Halloween		3,750	Annual media and mall signage costs
Hawthorne Foundation		3,200	Funding of private foundation promoting state economic development and for dinner costs
Rotary Rock'n Ribs		3,100	Shuttle bus service
Leadership Springfield		2,500	Purchased "space" on the *Springfield on Board* game (similar to the board game *Monopoly*)
Home Builders Association		2,220	Home shows, banner, golf hole, and bowling sponsorships
Wonders of Wildlife		1,725	Poster contest and clean water tour
Springfield Police Department		922	Traffic control for Kitchen 5K run and safety fair participation
Unite of Southwest Missouri		550	Multicultural festival
Missouri Chamber of Commerce		540	High school business symposium
Big Brother/Big Sisters		500	Sports Hall of Fame banquet
Midtown Neighborhood Association		500	Sponsorship
Ozark Trails Council Boy Scouts of America		500	Distinguished citizen award ceremony for City Councilman
United Way Local Campaign		492	Meeting costs
Springfield Contractors Association		450	Golf hole and meeting sponsorship
American Red Cross, Junior Achievement of the Ozarks, Ozarks Literacy Council, The Kitchen, Salute to Construction, Downtown Springfield Association, Coalition for a Better Tomorrow, and Ozarks Science and Engineering Fair		1,580	Bowl-a thon annual contribution, high school transitions program, bottled water provided for the 5K run, awards banquets, parade and golf hole sponsorships, and fundraising breakfast

In addition, employees are allowed to work for charitable causes during their normal working hours. For example, over 50 employees were excused from their normal duties to participate in the United Way Day of Caring. Based on the wages paid to the participating employees, the utility estimated this event alone cost approximately $12,373. The utility excused employees from their normal duties to participate in several other similar events.

The utility is very active in supporting various community events. Our review was limited and the items discussed above may not be an exclusive listing of all similar activities.

The Missouri Constitution prohibits the use of public money or property to benefit any private individual, association, or corporations except as provided in the constitution. Without a written contract that clearly indicates the benefit to CU, these uses could be in violation of the constitution. In addition, some of these expenditures were to organizations and/or charities associated with some CU employees or board members. CU has not established procedures to determine whether these payments and contributions are appropriate. When utility funds are paid to organizations and/or charities they are affiliated with there is an appearance of a conflict of interest.

Disbursements for employees and vendors were as follows:

- A 2006 family day picnic was held to show appreciation for the employees and their families. For this event CU spent $8,178 for catering, $7,245 for party supplies such as a temporary tattoo parlor and an inflatable slide similar to those used by traveling carnivals, $2,103 on ice cream and beverages, and $1,924 for decorations. Our review of this event was limited and the items discussed above may not be an exclusive listing of the total cost.

  The 2007 family day picnic schedule included entertainment such as children's carnival games, bucket truck rides, linemen demonstrations, a digital scavenger hunt, a home-made salsa contest, a local band, a pie walk, and bingo games.

- CU spent $3,125 annually for a suite at the Springfield Cardinal's baseball stadium.

- Flowers and monetary contributions were purchased by CU totaling $2,992. CU has a policy that allows flowers or other monetary contributions to be made for employees and retirees in the event of an illness or death.

- Dedication ceremony supplies such as a tent, chairs, food, and plaque for the Noble Hill Landfill Renewable Energy Center costing $1,891 were purchased by CU.

- CU spent $725 for a "Thank You" lunch for employees of the purchasing and inventory departments.

- Other questionable items were noted and more examples will be discussed in MAR numbers 4, 10, and 11.

These expenditures do not appear necessary or essential to the operation of the utility. The utility has a fiduciary duty to ensure funds are expended in a manner that provides the greatest benefit to the utility. It is unclear what, if any, benefit these expenditures provided.

B. CU contracts with various entities to provide funding without ensuring all contract requirements are met or requiring adequate documentation of how those monies were used. For example,

- CU contracts with the SBDC, an economic development subsidiary of the Springfield Area Chamber of Commerce, for economic development and advertising services for $165,000 annually.

The SBDC only provides an annual report detailing the general accomplishments of the SBDC and their audited financial statements, while the contract requires SBDC to provide semiannual reports to the General Manager dealing with promoting: the benefits of low cost utility services, retention and expansion of existing quality business, and benefits of Springfield as a location for quality businesses.

- CU contracted with the Watershed Committee of the Ozarks to provide funding for community water education and water quality studies for $156,000 during the year ended September 30, 2006. Funding was provided without requiring this entity to provide documentation to support how those monies were used. CU pays 60 percent of the Watershed Committee of the Ozarks operating budget while the city and county pay 20 percent each.

CU should ensure the SBDC provides all information required in the contract. In addition, to ensure the proper use of utility funds, CU should establish formal procedures to monitor the use of these monies and require detailed information (such as detailed financial reports, invoices for specific activities, audits, etc.) from the Watershed Committee of the Ozarks to document how these funds are used.

C. Procedures have not been established to ensure operating costs of the trunked radio system are properly allocated based upon usage of each entity. CU in conjunction with the City of Springfield and Greene County implemented a trunked radio system in 2000 to provide improved law enforcement and public safety communications among various agencies and departments, including emergency and non-emergency communications. The original contract did not provide for costs to be shared based upon usage, and the following chart illustrates the current level of usage and proportionate share of the costs for the year ended September 30, 2006.

	Current Subscriber Units	Proportionate Share of Costs
CU	450	$ 495,000
City of Springfield	1,000	495,000
Greene County	1,500	590,000

CU tracks the operating cost of the system and any additional capital costs incurred and bills the city and county quarterly. In addition, CU has entered into an agreement with Missouri State University (MSU) to provide use of the system at no cost to the university from June 15, 2005 until August 2008. The allocation of operating costs does not appear reasonable based upon the level of subscriber units (usage) and MSU's use of the system at no cost. Finally, the utility does not receive any administrative fees for tracking the costs and billing the various entities for the use of the system.

Usage of the trunked radio system should be reviewed and costs allocated in a more proportionate manner. In addition, CU should consider tracking and billing the administrative costs incurred.

D. CU needs to improve its controls and procedures over the usage of its cellular telephones. The utility uses three separate carriers and paid $77,467 for the year ended September 30, 2006 for providing cellular phones to approximately 205 employees. While CU has procedures to review cellular telephone usage monthly, these review procedures were not always adequate.

Many employees incurred costs for calls that were not covered by their cellular telephone service agreement including charges for additional minutes, roaming, directory assistance, and text messaging. For example, a SpringNet® employee incurred $304 for roaming charges one month. In another example, a meter reader incurred $94 for additional minutes in one month. Although some changes were made to the plans subsequent to our review, several employees continued to incur considerable additional monthly costs.

To ensure the efficient and effective use of cellular telephones, CU should routinely monitor cellular phone usage patterns and ensure the most cost-effective plan is being used.

E. CU does not follow a consistent policy for hiring executives. CU hired and paid an outside recruiting firm $49,793 between September 2005 and January 2006 to advertise, evaluate, and conduct preliminary interviews of candidates for the Associate General Manager-Chief Operating Officer position. Three of the eight candidates that were selected for the final interviews were internal CU employees, and CU subsequently hired two of these internal employees to fill the position (after separating the duties and creating two associate general manager positions).

In other instances where executives were hired, CU advertised nationally or conducted only internal interviews. CU does not consistently use a recruiting firm to hire executives, and it is unclear why a recruitment firm was used in this situation.

WE RECOMMEND the Board of Public Utilities:

A. Ensure disbursements are necessary and prudent uses of public funds, and provide a benefit to the utility and do not violate the state constitution. In addition, avoid the appearance of a conflict of interest.

B. Improve the control and accountability over the use of utility funds spent by other organizations.

C. Review usage of the trunked radio system and allocate operating costs in a more proportionate manner, and documentation supporting the methods of allocation of the trunked radio system should be retained. The utility should also consider tracking and billing the administrative costs related to the system.

D. Revise current controls, policies, and procedures regarding cellular telephones to include a thorough review process and to adapt to new technology.

E. Develop consistent procedures for hiring executives.

<u>AUDITEE'S RESPONSE</u>

A. The Board and management contend that all expenditures of the utility are legal and necessary. To allege expenditures "may" or "could" be in violation of the constitution is a serious accusation that should be substantiated or removed from a public report. To make such an allegation without substance or evidence casts unfounded doubt on legitimate business activities. The Board will direct legal counsel to review future expenditures like those noted in the State Auditor's report to ensure legality.

B. The Board and Management will continue both formal and informal review of various organizations funded by utility expenditures to assure the appropriate benefit levels are maintained.

C. The Board believes the trunked radio system is a perfect example of how county and city agencies have worked together to improve the safety of all citizens in the Springfield area. Systems such as the trunked radio system are only achievable due to the cooperation among various parties. CU considered the benefits received from the partnership and negotiated an agreement accordingly. The terms of the agreement will continue to be followed in tracking costs and billing partners appropriately.

D. CU continuously reviews the various options for providing employees with cellular telephones to do their jobs. Internal Auditing performs periodic audits and reviews of the billings.

E. CU will review the established policies and clarify all recruitment procedures, including those for hiring executive staff.

4. Employee Awards and Payroll Policies

Over $52,000 of safety and years of service awards have been given to employees, which do not appear to be prudent, reasonable, or a necessary use of utility funds. In addition, CU paid employees $26,050 in finder's fees for identifying and reporting illegal use of utility services, which would appear to be part of their regular job duties. CU policy also does not require employees to disclose and obtain approval for outside employment and business activities.

A. CU purchased safety awards totaling $25,647 during the two years ending September 30, 2007. Annually, the utility gives safety awards for every five years (from five years to forty years) based upon employees who have reached safety milestones by not experiencing a lost-time injury. The awards include: executive pen and pencil sets, pewter belt buckles, marble bookends, windbreaker jackets, clocks, collegiate style gold and silver rings, weather stations, and pocket watches. Some of these safety awards have significant values. For example, the collegiate style gold ring, pocket watch, and wall clock are purchased for $475, $240, and $205 each. In addition, safety awards are presented to all utility employees regardless of the duties assigned. For example, safety awards are given to human resource and purchasing employees.

In addition, CU purchased years of service awards totaling $26,964 during the two years ending September 30, 2007. Lapel pins with blue sapphires, rubies, emeralds, and diamonds are given for every five years of service (from five to thirty-five years of service).

These expenditures do not appear necessary or essential to the operation of the utility. The utility has a fiduciary duty to ensure funds are expended in a manner that provides the greatest benefit to the utility. It also appears questionable why some utility employees such as clerical or administrative should receive safety awards.

B. CU pays employees, such as meter readers and field technicians, a $25 finder's fee for identifying and reporting illegal use of utility services. CU paid employees $26,050 in these fees during the two years ending September 30, 2007. Identifying and reporting illegal use of utility services would appear to be part of these employee's regular job duties, and the payment of such fees should be reconsidered.

C. CU does not effectively monitor outside employment and business activities of employees. While CU policy addresses outside employment and business activities of employees, the policy does not require employees to disclose and obtain approval for outside employment and business activities.

To effectively monitor outside employment and business activities, CU's policy needs to be revised to include requirements to disclose and obtain approval for outside employment and business activities.

WE RECOMMEND the Board of Public Utilities:

A. Ensure disbursements are necessary and prudent uses of public funds.

B. Reconsider the practice of paying finders fee to employees.

C. Require employees to disclose and obtain approval of outside employment and business activities.

AUDITEE'S RESPONSE

A. *The Board supports management's efforts to encourage a safe workplace. Since it is well documented that safety awareness results in fewer work-related accidents and in turn, fewer customer dollars spent on workers' compensation costs, and because employees in all types of jobs incur job related injuries, City Utilities' safety program includes recognition for all employees who have excellent safety performance.*

Similarly, the Board supports management's efforts to recognize the value of employees' service. The service award program helps reduce turnover costs to CU and saves our customers money, as this program assists CU in motivating, recognizing, and retaining its most valuable resource – its employees.

B. *Paying a union employee a finder's fee for finding and reporting illegal services was negotiated with the International Brotherhood of Electrical Workers (IBEW). This is a common practice in the industry to detect fraud and eliminate theft of services.*

C. *Although no violations were cited by the State Auditors, CU will consider modifying the current policy regarding outside employment.*

5. **Natural Gas Hedging**

CU suffered a financial loss of more than $2.7 million during the 2007 hedging season, and the financial information presented to the Board of Public Utilities regarding the loss was incomplete. In addition, documentation of the effect of a policy change which significantly increases CU's possible liability in the hedging market was not presented to the board. Formal procedures for the buying and selling of natural gas options have not been established, and employees with access to natural gas market analysis are not required to submit personal disclosure statements to document that they are not personally taking the same or opposing positions as CU in the natural gas financial market. Also, minutes are not always maintained and have not been signed for some of the Natural Gas Options Committee meetings.

CU uses natural gas hedging as a financial tool to help reduce the risk of increasing natural gas prices during the peak heating season, December through March. CU buys natural gas options at a specified price per dekatherm (the unit of measure for purchasing natural gas) based upon decisions made by the Natural Gas Options Committee. If the market price rises above the price per dekatherm paid for the option, the utility can exercise the option and recognize a financial gain and therefore, keep natural gas rates lower. However, if the market prices decrease below the price per dekatherm paid for these options, the utility suffers a financial loss. The utility started hedging natural gas in the 2003 season. The annual gain or (loss) from hedging activities since 2003 are as follows:

Hedging Season	Gain or (Loss)
2003	$ 665,489
2004	333,192
2005	58,935
2006	($758,402)
2007	($2,725,468)

A. Improvements are needed in how hedging activity is presented to the board. CU suffered a financial loss of more than $2.7 million during the 2007 hedging season, and the financial information presented to the Board of Public Utilities regarding this loss was incomplete. A former Associate General Manager presented a report of the 2007 natural gas hedging season to the board in February of 2007 with the following information:

Funds Invested	$ 2,789,266
Quantity Hedged	2,600,000 dekatherms
Proceeds	$ 63,798

The hedging activities are presented to the board as "insurance" on pricing. The report did not indicate that the "proceeds" only represented monies received from the few options that were exercised (sold), and did not clearly indicate that CU suffered a financial loss of $2,725,468 (the difference between the "funds invested" and "proceeds". This loss was a result of the utility allowing the remaining options purchased to expire because the natural gas market prices fell below the option price. The Associate General Manager told the board at the meeting that CU "spent about $2.7 million net" during the season. Given the significant financial loss, complete information regarding the loss should have been presented to the board.

In addition, in July 2006 the Natural Gas Options Committee requested a policy change to increase the maximum net annual exposure for hedging transactions from $1 million to $4 million. There was no evidence to indicate the board was informed of what the effect of a possible loss of $4 million due to natural gas hedging would have on natural gas rates.

Complete and detailed financial information regarding natural gas hedging transactions and policy changes is essential to the Board of Public Utilities to make informed decisions while managing the resources of the utility.

B. While a general policy regarding natural gas activity has been established, formal procedures for the buying and selling of natural gas options by the Natural Gas Options Committee have not been established. To ensure natural gas hedging activity is properly handled and accounted for, formal written procedures regarding the buying and selling of natural gas options should be established and documented.

C. While CU policy states that employees with access to analysis tools and information acquired by CU shall be prohibited from taking the same or opposing positions as CU in the natural gas financial market, CU does not require these employees to file a personal disclosure statement of this type of market activity. Requiring these employees to submit an annual personal disclosure statement would allow CU to monitor policy compliance.

D. Minutes are not always maintained and have not been signed for some of the Natural Gas Options Committee meetings (including those in which option purchases were approved). Minutes serve as the only official permanent record of decisions made by the committee. Minutes should be prepared and approved for all committee meetings.

WE RECOMMEND the Board of Public Utilities:

A. Require complete and detailed financial information regarding natural gas hedging transactions and policy changes to be presented to the board.

B. Establish and document formal procedures for the buying and selling of natural gas options.

C. Require all employees with access to market analysis to submit an annual personal disclosure statement.

D. Ensure minutes are prepared and approved for all committee meetings.

AUDITEE'S RESPONSE

A. The Board has been fully informed of the natural gas hedging transactions on a continuous basis. Reports to the Board included financial statement footnotes which completely described purchase prices, market values, sales prices, and increases / decreases to natural gas expenses. Presentations were made monthly to the Board, and these presentations all included updates on present market values and expenses associated with this program. The TEA Natural Gas Financial Transactions Policy approved by the Board of Public Utilities states that the intent of these financial transactions is to provide protection against upward natural gas price movements for customers, as well as afford them the opportunity to participate in the benefits of market price declines. The policy also states, "It is fully understood that under certain market conditions, financial hedging programs will have net costs to CU and customers – not unlike the analogy of the cost of insurance coverage." These options have provided the desired protection from potential higher prices.

As recommended by the State Auditors, CU management will take every opportunity to continue to improve the information provided describing natural gas hedging transactions through monthly financial statements and Board presentations. Any *necessary policy changes will continue to be fully explained to the Board when requesting approval.*

B. *The Natural Gas Options Committee will verify there is sufficient documentation of current procedures.*

C. *The Board will consider the need for modification to the current policy.*

D. *The Natural Gas Options Committee will continue to prepare minutes for meetings involving option purchase decisions.*

6. The Energy Authority (TEA)

CU did not prepare a cost benefit study before entering into a contract with TEA in 1998 for energy trading and risk management services. In addition, CU has not adequately documented their continued investment in TEA on an annual basis. While CU's ownership affords them the ability to audit the books, records, and accounts of TEA, CU has only participated in one audit in the past seven years and additional monitoring procedures of TEA activities have not been established.

In 1997, the Federal Energy Regulatory Commission started allowing municipal utilities to sell excess electricity in the wholesale energy marketplace. In response to this new regulation, CU established the Restructuring and Competition Task Force (RCTF) to evaluate potential electric marketing and trading alliances. The RCTF met with 15 firms in 1997 and 1998 to establish such an alliance, and subsequently entered into a contract with TEA in September of 1998. Under this original agreement, CU paid a monthly fee and a percentage of the amounts billed to all TEA participants in exchange for TEA's marketing and trading services of the utility's excess electricity.

TEA is a nonprofit corporation organized and operated under the Georgia Nonprofit Corporation Code. It maintains its headquarters in Jacksonville, Florida, with two additional offices in Bellevue and Vancouver, Washington. TEA was organized in 1997 to enhance the use of its owners' electric generating assets in the wholesale electric power market, optimize power purchases from the wholesale market for its owners, create economies of scale and reduced operating costs with respect to energy trading and marketing, and to assist owners with managing risks in the wholesale energy marketplace. TEA serves public power utilities across the United States with a variety of services. Thirty-nine public power utilities across the nation are TEA participants and only six of the public power utilities are owners (CU has a 7.14 percent ownership interest).

In February of 2000, the Board of Public Utilities granted the General Manager the authority to establish ownership in TEA. In May of 2000, the Chief Financial Officer (CFO) reported that sufficient funds were available in the 2000 annual operating budget to invest in TEA, and therefore CU did not obtain additional approval from the

Springfield City Council. At this time, the CFO prepared a limited analysis of ownership in TEA. This study estimated an initial outlay of cash, and it also compared the expected annual return on their investment (given in equity only) to the amount of fees paid to TEA prior to becoming an owner.

CU has a current investment in TEA of more than $2.4 million and has guaranteed more than $9.6 million in cash reserves to TEA as of September 30, 2006. CU also paid an initial membership fee of $867,360 in 2000 to become an owner and additional costs to trade energy were incurred by the utility annually as follows:

Year ended September 30,	Amount
2001	$ 472,312
2002	785,662
2003	1,050,975
2004	710,173
2005	740,113
2006	1,013,220

In 2005, CU compared the costs to trade energy by being an owner to the fees that would have been charged to participants, but a detailed cost benefit study tracking the full cost of CU's relationship with TEA has not been performed.

Considering the extent of CU's investment in TEA, a detailed cost benefit study of its relationship with TEA should be performed and continually updated to facilitate the decision-making process and to provide assurances that the investment in TEA is in the best interests of the utility. The utility should take full advantage of the benefit of ownership and regularly audit and monitor the financial records of TEA.

WE RECOMMEND the Board of Public Utilities ensure a detailed cost benefit study is performed and continually updated and that full advantage is taken of every opportunity to provide oversight of TEA operations.

AUDITEE'S RESPONSE

The Board cites TEA as a great example of where City Utilities management has outsourced services requiring specialized expertise in order to lower costs and risk for our customers. Further, the utility exercises ongoing and appropriate oversight of TEA and its work. Since TEA's inception, CU management has and continues to play an important oversight role at both the TEA Board and committee levels. CU sought membership in TEA to furnish our customers with cost-effective services from an organization positioned with national market knowledge. Benefits from investment in such an organization do not equate with a "return" that would be earned from an investment in a stock or bond. One must also look at the accomplishments of the organization over time in context with the rest of the market. During the time CU has utilized TEA's services, the energy markets have experienced widespread volatility in prices, market manipulation, the rise and fall of many marketing organizations (ENRON, Dynegy), utility *companies in and out of the market (many of which lost millions of dollars), a natural gas generator boom and bust, transmission deficits, a major blackout affecting millions of Americans, and major new environmental regulations. During that same time, CU through its affiliation with TEA has always provided reliable power, has never defaulted on any third party purchases or sales, and has maintained low customer prices (both regionally and nationally).*

7. SpringNet ® Compliance and Controls

SpringNet® has failed to comply with several provisions of a Public Service Commission (PSC) order regarding the necessity to operate without continued financial assistance from the utility, and has failed to comply with state law which limits term agreements on telecommunications services to five years. SpringNet® has not followed the terms of its service contracts with customers regarding delinquent accounts and has developed more lenient practices. In addition, failure to establish policies requiring security deposits and to perform routine credit checks on prospective customers exposes CU and SpringNet® to unnecessary financial risk. CU has spent over $6 million on SpringNet® Underground without performing preliminary feasibility studies and developing a formal ongoing business plan for this activity.

SpringNet® is a division of CU which offers telecommunication services and also provides computer operations hosting services within a local underground mine as SpringNet® UnderGround. CU was authorized to enter the telecommunications market by order of the Public Service Commission (PSC) in July 1997. Prior to this order, CU provided internal telecommunications services to the utility and the city. CU's Telecommunications department and SpringNet® continue to provide internal services. For the year ended September 30, 2006, SpringNet® had operating revenues of approximately $6.2 million.

A. SpringNet® has failed to comply with several provisions of the PSC order related to telecommunications services. For example:

- SpringNet® does not generate sufficient revenues to cover expenses and required subsidization from other CU operations of approximately $1.5 million during the year ended September 30, 2006 (subsidization was discussed in more detail in MAR number 2). This is specifically prohibited by PSC order.

- SpringNet® has relied upon other utility operations to obtain financing for capital investments and this is not allowed by PSC order. CU entered a master lease agreement with a local bank for the Public and Water Utilities, which included receipt of $1.2 million in financing proceeds in October 2006 for SpringNet®. This financing was backed by resources of the entire utility and not just those of SpringNet®.

- SpringNet® does not operate as a stand-alone entity as required by PSC order. CU's internal auditors recommended in September 2004 that SpringNet®'s cash position should be monitored separately to ensure compliance with the PSC order; however, this recommendation had not been implemented as of March 2007. Upon our request, cash funding reports were prepared by SpringNet®; however, these reports were not accurate. For example, the $1.2 million financing proceeds discussed above were inaccurately reported in the three month period ending March 31, 2006 instead of October 2006 when the funds were actually received. This inaccuracy caused their financial position to appear more positive than it actually was for the year ended September 30, 2006.

- SpringNet® has failed to comply with the provision of the PSC order that requires the utility to operate its telecommunications services within a two-mile area surrounding the utility's electric service area. SpringNet® provides internet type services to clients outside of the allowable boundaries. For example, services are provided to a hospital in Osceola, Missouri, and to companies in Poplar Bluff, Missouri and Springdale, Arkansas, which are significant distances outside of CU's service area.

CU and SpringNet® should ensure compliance with provisions of the PSC order. Also, cash funding reports prepared by SpringNet® should accurately reflect the financial position, and internal audit recommendations should be implemented.

B. SpringNet® has failed to comply with Section 392.200, RSMo, which limits term agreements on telecommunications services to five years. For example, in October 2006, SpringNet® entered into a ten year contract with an out of state client to provide underground data storage services. An audit report issued by CU's internal auditors in September 2004, recommended that SpringNet® comply with the five year contract limitation; however, this audit recommendation was not implemented.

C. SpringNet® has not enforced the terms of its service contracts with customers regarding delinquent accounts and instead has developed more lenient collection practices. For example, service contracts indicate that invoices not paid within ten days will be charged a late penalty; however, SpringNet® personnel indicated the late payment charge is not applied until the bill is over 90 days delinquent. SpringNet® has not developed policies requiring customer security deposits similar to what is required from other utility customers, and routine credit checks are not performed for prospective customers prior to entering into contracts for services.

SpringNet® should enforce the delinquent account contract provisions. Failure to follow contract terms on late payment charges, as well as, failure to establish policies requiring security deposits and to perform routine credit checks on prospective customers exposes CU and SpingNet® to unnecessary financial risk.

D. CU did not perform an adequate feasibility study or develop an adequate business plan on SpringNet® Underground before entering this market. SpringNet® Underground continues to expand despite their inability to generate sufficient revenues to cover costs related to this venture. CU entered into a lease agreement in April 2002 with a local Springfield company for space in a privately owned underground facility for ten years at $18,598 per month or approximately $2.2 million. CU amended the original lease agreement twelve times between April 2002 and March 2007 and spent an additional $4.4 million in construction costs at the privately owned underground facility, for the use of SpringNet® Underground. Most of the $4.4 million spent on construction will remain the property of the lessor when the agreement expires. SpringNet® Underground continues to rely on other utility services to fund operations.

Good business practice requires a reasonable formal analysis of future plans, anticipated revenues, and projected expenditures to be performed and updated to support the board's continued decision making process. Given the current financial position of SpringNet® it is important that decisions made do not place this activity in a position requiring continued subsidization from the rest of the utility.

WE RECOMMEND the Board of Public Utilities:

A. Ensure compliance with the PSC order and ensure adequate monitoring of cash funding position is performed to demonstrate compliance.

B. Ensure compliance with state law regarding length of contracts.

C. Ensure contract terms for handling of delinquent customer accounts are followed. Develop policies regarding security deposits, and establish procedures to routinely perform credit checks on prospective customers.

D. In the future, ensure a formal analysis of future plans, anticipated revenues, and projected expenditures is performed and updated, and closely monitor SpringNet® Underground's financial condition.

AUDITEE'S RESPONSE

A. City Utilities has discussed the State Auditor's statements with the PSC. According to the PSC, it has no evidence of a failure to comply. CU will continue to monitor SpringNet's cash funding position and will move toward tracking the funding position of the services that are regulated by the PSC. SpringNet did complete its financing under the CU master lease; however, the $1.2 million financing for SpringNet was backed entirely by telecommunications assets owned by SpringNet. CU voluntarily requested the PSC certification prior to Missouri Law that also allows CU to offer telecommunications services and will continue to monitor compliance with the certificate requirements.

B. *CU complies with all applicable laws. In fact, underground data storage services are not considered a telecommunications service under Missouri law, therefore the contract for these services would not be subject to the 5-year limitation. Since this service is not one for which a PSC certificate applies, CU will continue to follow applicable Missouri law.*

C. *There is a procedure for checking utility credit history when establishing a new SpringNet customer; however, SpringNet will consider the benefit of performing credit checks beyond the verification of utility payment history in selected cases.*

D. *As evident in SpringNet's 2001, 2003, and current business plan updating efforts, good business practices are being followed. SpringNet has a history of analysis and planning. An independent review was conducted to structure and assist Telecommunications' unbundling from the Utility in 1998. The first business plan was prepared in 2001 and the plan was updated in 2003. Internal Audit conducted a business audit in August 2004 and Internal Audit hired a security consultant to conduct a network security audit in September 2004. SpringNet meets with the Risk Oversight Committee on a quarterly basis to review the financial impact of new contracts, and SpringNet is currently working on updates to the business plan for 2008 and will ensure that future updates are on a more consistent basis as recommended by the State Auditors.*

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AUDITOR'S COMMENT

A. CU has no documentation from the PSC to support the claim that they are in compliance with these provisions of the PSC order.

B. Since underground data storage services are provided through CU's telecommunication's division, SpringNet®, it is unclear why CU does not comply with Section 392.200 RSMo.

8. Bidding and Purchasing Policies

CU uses alliances, standing purchase orders, and blanket orders as purchasing tools for significant expenditures without the use of annual competitive bidding. In addition, CU did not obtain bids through public advertising for several large projects and purchases. Also, the utility issues purchase orders and contracts interchangeably, but no formal policy has been established to provide employees guidance on these.

CU purchasing policies and procedures require competitive bidding to be completed for all purchases in excess of $2,000. CU expended over $260 million in operating expenses during the year ended September 30, 2006.

A. CU uses alliances, standing purchase orders, and blanket orders as purchasing tools without the use of annual competitive bidding for supplies. CU has not established written policies or procedures for the establishment and monitoring of such purchasing tools. We noted the following examples:

- CU participates in four alliances to purchase supplies. These alliances allow the utility to purchase items that are bid in first year of the alliance and extended for up to four years with pricing increases based on national price indexes which are reviewed annually. For example, underground electric supplies were originally bid in December 2001 and the alliance was extended each year without rebidding until May 31, 2007. The types of products purchased with these alliances and the approximate amounts paid during the year ended September 30, 2006 are as follows:

Underground electric supplies	$ 1,900,000
Overhead electric supplies	1,700,000
Utility line transformers	1,500,000
Water Line Supplies	1,000,000

- When the utility purchased a natural gas monitoring system, they entered into a standing purchase agreement with the vendor to provide replacement parts at five percent below the manufacturer's list price. This standing purchase agreement began in 1994 and will not expire until the equipment is no longer used. CU has not solicited bids for these items since 1994, and it appears competitive bidding should have been considered. CU has expended approximately $76,000 with this vendor during the year ended September 30, 2006.

Given the use of these purchasing tools and the magnitude of these types of expenditures, annual competitive bidding should be considered. Bidding procedures for major purchases provide a framework for the economical management of utility resources and help assure the utility that it receives fair value by contracting with the lowest and best bidder. In addition, competitive bidding ensures all interested parties are given an equal opportunity to participate in utility business. Written policies and procedures for establishing, approving, and monitoring all purchase tools are necessary to provide guidance, and avoid misunderstandings.

B. CU's bidding policy does not address obtaining bids through public advertising. Employees are allowed to use their judgment as to whether or not to publicly advertise for a particular project or purchase. Advertising was not completed for the following:

- The construction of the Propane to Air Peak Shaving Plant totaling $6,221,333.
- Purchase of a coal loader costing $656,100.
- Purchase of a substation transformer totaling $554,330.
- Purchase of radio software totaling $143,400.

While CU did solicit bids from select vendors on the above expenditures, CU did not publicly advertise to help assure itself that it received the lowest and best price on the expenditures. Considering the extent of these expenditures, it appears that advertising for bids would have been a good business practice.

Including advertising requirements in the formal bidding procedures would provide a framework for economical management of CU resources and help ensure the utility receives fair value by contracting with the lowest and best bidders. Public advertising requirements would also help ensure all parties are given equal opportunity to participate in the utility's business.

C. The utility issues purchase orders and contracts interchangeably, and no formal policy has been established to guide employees on whether to use a purchase order or a contract. Purchase orders used by CU are not signed by all parties involved. During our review of expenditures, we found the following large purchases were made using purchase orders when contracts may have been more appropriate. These items include:

Part for a turbine	$8,259,063
Construction of the Landfill Gas to Energy Plant	3,619,812
Rental of water pumps	1,251,810
Voltage equipment for power plant	980,362
Transformer for substation	554,330

The items purchased above were special order items that were manufactured to fit CU's needs. As a good management practice, the utility should establish guidelines on whether to use a purchase order or a contract. Written agreements, signed by both parties, should specify the services to be rendered, the manner and amount of compensation, and the time period for which the agreement remains in effect. Such agreements would lessen the opportunity for misunderstandings between the parties involved. In addition, Section 432.070 requires local government contracts to be in writing.

D. Several contracts and purchase orders were significantly increased in amount and term of service through change orders, and bids or proposals were not solicited for any of the change orders. Examples include:

- The original contract for the construction of the Propane to Air Peak Shaving Plant totaled $5,266,928. CU spent more than $1 million additionally as a result of five change orders related to the project. Most of the construction change orders were for ground preparation work such as grading that had not been included in the scope of the original project for some reason.

- The original contract for the remodeling of the transit and fleet maintenance building totaled $726,349. CU spent an additional $136,238 as a result of five change orders for the remodeling project. Change orders were incurred to add security cameras and other modifications to the design plans.

- Numerous change orders were issued to extend the term of the contract for health insurance administration. CU solicited bids for this service in 1999 and used the selected provider until January 2006.

CU's purchasing policy allows for change orders for making minor changes without taking additional bids, but it appears consideration should have be given to rebidding some of the major changes discussed above.

Change orders are normally used to make adjustments for minor problems that are unknown when projects and purchases are originally bid. They should not be used to make significant changes to existing contracts. If the scope of a project changes substantially, consideration should be given to rebidding those parts of the project. CU also used change orders for professional services as discussed in MAR number 9.

WE RECOMMEND the Board of Public Utilities:

A. Develop written policies and procedures for establishing, approving, and monitoring all purchasing tools. This should include a provision that provides for annual competitive bidding of all utility purchases.

B. Develop a comprehensive bidding policy which addresses public advertising.

C. Establish guidelines on whether to use a purchase order or a contract, and enter into written contracts for services which clearly outline the responsibilities of both parties for all current and future arrangements.

D. Ensure adequate planning is performed to reduce the number of change orders, and, if substantial changes are needed, consideration should be given to rebidding the applicable projects.

AUDITEE'S RESPONSE

A. All utility purchases are competitively bid, unless they are specifically exempted by policy. City Utilities has extensive written policies and procedural tools for competitive bidding of materials, equipment, and services. CU policy recognizes the value of bidding multiple years at the same time.

B. *CU procedures follow the city charter which states, " . . . there shall be given ample opportunity for competitive bidding . . .". Written internal procedures include and allow for several methods of public advertising. Vendors for solicitations of materials, equipment, and services are typically selected from the thousands of vendors on file with CU who have requested to bid on materials, equipment, and services. Additionally, competitive bid documents are publicly advertised in the public lobby of the CU Purchasing Department. When appropriate for the purchase, public advertising is also placed in local and regional newspaper publications and plan rooms. Plan rooms are clearing houses which notify potential local, regional, and national bidders of current bidding opportunities. One such plan room is operated by the Springfield Contractors Association.*

CU does not consider it to be necessary to advertise in newspapers when the product is unique or when the marketplace has limited bidders known to operations, purchasing, consultants and others, and it is felt that advertising in local and regional newspapers would not generate any additional bidders.

C. *CU contracts and purchase orders are all written, "formal" legal contracts and comply with all statutes according to our Legal Counsel. All contracts for services are written legal documents and outline the responsibilities of both parties.*

The decision of what format a contract takes is dependent upon the complexity of the item or service being purchased, the number and type of regulations and requirements that must be followed (e.g., environmental, insurance, federal), necessary attachments such as plans and drawings, special conditions of the work, and special capital projects (e.g. Southwest 2). All of these items and criteria are discussed between the requestor and the Buyer with reviews and input from Purchasing Management, Legal, Risk Management, Environmental, Safety and other departments as needed. As recommended by the State Auditors, CU management will consider developing guidelines to be used in determining whether a purchase order or contract is applicable.

D. *When a change to an existing contract is determined to be necessary, and that change is substantial or outside the original scope of the project and the situation is appropriate to bid, consideration is given to bid that change.*

On major construction projects, such as the two mentioned in the State Auditor's report, it is typically the project manager/engineer's responsibility to determine if a change will affect the continuity or timeline of the project, whether it is within the original scope of the project, and whether re-bidding would adversely affect the project.

9. Professional Services

CU needs to improve its process of procuring and monitoring some of its professional services. Proposals were not always solicited for legal services, a contract for legal service was approved without any review of the compensation to be paid, legal contract renewals were sometimes signed by law firms several days after the effective date of the contract, and documentation was not always adequate to support amounts paid for legal, consulting, and lobbyist services. Change orders were regularly used to avoid the professional selection process, and CU pays annual "relationship fees" to two bond credit rating firms used for utility bond issuances, which presents an appearance of a conflict of interest.

CU has established procedures and policies to select professionals on the basis of qualifications and competence for specific types of services. The utility's professional selection policy requires the general manager to select three or more utility employees for the professional selection committee. For major projects, the general manager will request one or more board members to serve on the committee. The selection committee will select an appropriate number of persons or firms capable of performing the required services and make a recommendation to the general manager. If the general manager approves the award to the chosen professional, a contract is executed and the purchasing department will issue a purchase order to that person or firm. The policy requires the professional selection process to be repeated every two years for blanket contracts.

A. Improvements are needed over legal fees paid by the utility. In addition, to having three attorneys on staff, the utility spent over $522,000 during the year ended September 30, 2006 for outside legal counsel.

- The utility did not always solicit proposals for legal services in accordance with their policy and has used six different law firms routinely for several years.

- Contracting procedures with the primary law firm used by the utility need improvement. Each year the utility will send the law firm a letter representing the contract. The letter asks the law firm to sign and return the letter (which does not include compensation to be paid to the firm) and to submit the names, titles, and rates of the employees that will be working on CU matters. This information is subsequently provided by the law firm. Given this situation, CU agrees to continue the contractual relationship without any review of the compensation to be paid to this firm.

- Legal contract renewals were sometimes signed by law firms several days after the effective date of the contract. For example, a contract covering the period of June 1, 2005 through May 31, 2006 was signed by a law firm on July 20, 2005 or fifty days after the contractual period had begun. All contracts should be finalized and signed by all parties involved before the effective date of the contract.

- The invoices submitted by some firms did not always provide documentation related to the expenses being billed to the utility. For example, supporting documentation for mileage and meals was not always provided by the law firms.

- One of CU's law firms contracted with an outside consultant on CU's behalf to serve as an expert witness in a lawsuit regarding an air permit for the Southwest II Power Plant. The utility paid a 10 percent markup fee to the law firm on expenses billed by the consultant. A thorough review of the invoices was apparently not performed as CU's General Counsel indicated he was not aware of the markup.

While professional services, such as attorneys, consultants and engineers may not be subject to the standard bidding procedures, the utility should solicit proposals for professional services to the extent practical. Soliciting proposals and subjecting such services to a competitive selection process does not preclude the utility from selecting the vendor or individual best suited to provide the service required. Such practices help provide a range of possible choices and allow the utility to make a better-informed decision to ensure necessary services are obtained from the best qualified vendor at the lowest and best cost. The utility should ensure complete written contracts are prepared, adequate supporting documentation is provided, and all invoices are thoroughly reviewed prior to payment.

B. Change orders were regularly used to change the scope of work, to increase contract amounts, or to extend contracts beyond the two year period allowed by the professional selection policy. Examples include:

- A consultant was hired to perform a power supply study to determine CU's need to generate more power for $200,000. A change order was later issued to this same vendor for $500,000 to perform a second power study to determine how additional power could be generated.

- An opinion research consultant was selected through the utility's professional selection process in 2003 to perform various surveys. In 2005, the research contract was extended another year through use of a change order. This consultant was paid $95,170 during the year ended September 30, 2006.

Change orders are normally used to make adjustments for minor problems that are unknown when projects are originally bid. They should not be used to make significant changes to existing contracts or to avoid CU's professional selection process. When change orders materially change the amount of the original contract, scope, or extend the length of the contract continuously, the utility should re-select the professional services to ensure the utility receives the best price for the services.

C. Payments totaling approximately $110,374 were made to CU's five different lobbyists during the year ended September 30, 2006. The contracts require each lobbyist to promote utility interests and advise the utility on legislative, executive, and administrative matters at the state and national level. Concerns with these payments include:

- The contract with each lobbyist does not require documentation to support the specific services being provided, and invoices submitted by the lobbyists did not adequately detail the work performed. For example, contract terms with a lobbyist required the utility to pay a $4,629 monthly retainer for up to 50 hours of work plus any expenses incurred. The invoices submitted did not include the number of hours worked by the individual and did not include a description of the services provided.

- The contract with each lobbyist specifies that the lobbyist will not enter into other agreements that would present a conflict of interest, but does not require the lobbyist to disclose or to obtain written permission from the utility prior to performing any lobbying activities for other entities.

- Several of CU's memberships to organizations such as Springfield Area Chamber of Commerce, Missouri Chamber of Commerce, American Public Power Association, Transmission Access Policy Study, American Public Gas Association, and the Missouri Public Utility Alliance, provide lobbyist services as a benefit to membership. The participation in such memberships is discussed in more detail in MAR number 11. The utility needs to evaluate all of the resources devoted to lobbying activities to evaluate the necessity of such payments.

Detailed documentation of services provided is necessary to evaluate the reasonableness of payments for services rendered. Procedures should be developed to monitor lobbyist activities.

D. CU paid an annual $25,000 "relationship fee" to one bond credit rating firm used for utility bond issuances and $4,000 to another bond credit rating firm. CU pays these annual "relationship fees" whether or not they will be issuing bonds or will need the services of the credit rating firms. CU personnel indicated these fees were routine; however, similar fees were not paid by the city, and CU does not pay these fees to other bond credit rating firms. These payments present an appearance of a conflict of interest. Credit ratings are an important factor in the interest rate a bond issuer is offered for their bonds. The credit ratings involve a judgment about the future risk potential of the bond. It is the general expectation of credit rating agencies and bond issuers alike that credit ratings will help to reduce the interest rates applied to bond issues.

The utility has a fiduciary duty and should avoid situations that represent the appearance of conflicts of interest.

WE RECOMMEND the Board of Public Utilities:

A. Solicit proposals for legal services to the extent practical. In addition, complete written contracts should be prepared (including ensuring all contracts are signed before the effective date of the contract), and adequate supporting documentation should be received for all charges.

B. Take steps to reduce the number of change orders, and, if substantial changes are needed, consideration should be given to rebidding the applicable services.

C. Require detailed documentation of the services provided to ensure payments are reasonable and in compliance with contract terms, and develop procedures to monitor lobbyist activities.

D. Avoid payments that present the appearance of conflicts of interest.

AUDITEE'S RESPONSE

A. Hourly rates for outside legal services are reviewed annually. Invoices received for legal services are consistent with industry practice. Major law firms, along with CU, have concerns about conflicts of interest. By maintaining relationships with a select group of law firms, CU is able to ensure competitive rates, retain quality outside counsel, and minimize the risk of conflicts of interest.

B. CU has policies and procedures in place to ensure effective purchasing and contracting processes according to the city charter and state law. When a significant change to an existing contract is determined, and that change is outside the scope of the original project and the situation is appropriate to bid, CU will bid that change. However, when those conditions do not exist, CU will do a change order according to policy. CU will consider modifications to the current policies to provide more specific guidance for employees as recommended by the State Auditors.

C. CU closely monitors its lobbyists' activities, including monthly and annual reviews. Lobbyists file monthly reports with the Missouri Ethics Commission. This reporting includes a general description of legislation proposed and any action taken by the Executive Branch of government, as well as a list of clients represented and assurance that interests of these clients do not conflict. CU will continue to closely monitor its lobbyists' activities.

D. The payment of an annual fee to rating agencies is not a conflict of interest and is consistent with industry practice. Services and benefits received for this fee include surveillance of bond market ratings, discount pricing on new bond issuances, access to credit agency public power analysts, on-going correspondence with analysts to discuss industry outlooks, discussion of specific issues related to CU credit market activity, and public finance power research reports.

10.	Procurement Card Expenditures

Meals and food purchased with procurement cards appear excessive. CU lacks a comprehensive food policy, meals were provided at a private association meeting, and adequate documentation of food expenditures was not always retained. In addition, numerous other procurement card expenditures did not appear to be a prudent or necessary use of public funds. Cardholder use has not been adequately analyzed leaving CU with unnecessary liability. Some cardholders were circumventing purchase limits by splitting purchases, and other cardholder transaction limits were exceeded. Various CU procurement card policies and procedures were not followed, and reward points from a local hunting and sporting goods store were given to an employee for personal use.

CU has approximately 100 procurement cards that are issued to various employees of the utility. The procurement card is an official VISA credit card which is designed to provide a more convenient procurement method than the purchase order system. The individual cards have individual transaction limits of $500 to $2,000 and monthly cycle limits of $500 to $20,000. During the year ended September 30, 2006, procurement card purchases totaled approximately $1.2 million.

A. Meals and food purchased with procurement cards appear excessive. CU spent approximately $80,000 in calendar year 2006 for meals and food provided during employee meetings, training sessions, retirement receptions, employee recognition events, board meetings, public marketing events, and other external meetings. A food request form documenting the purpose of the event is prepared by an employee, approved by their supervisor, and normally given to the facilities management staff assistant for purchase. Concerns noted with procurement card activity include:

- CU has not established a comprehensive food policy or regulations regarding utility provided food.

- Meals purchased were sometimes excessive. For example, meals such as lobster and lobster bisque were purchased by two SpringNet® employees for a marketing meeting with four employees of a prospective customer. The average cost per meal was $60.

- Meals were provided at a Springfield Contractor's Association Meeting totaling $1,670. The reason to use CU funds to provide meals at a private association meeting was not documented.

- CU did not always include a list of attendees or general information that stated who was served, and did not always document the business purpose when purchasing food.

- Food request forms were not always signed by the requestor or their supervisor.

While it is sometimes necessary to incur food expenditures related to employee training, such costs should be kept to a minimum. In addition, it appears that some meetings and events may be scheduled around meal times, resulting in additional food expenses. A policy limiting food expenditures for employee training sessions and meetings and providing price guidelines would likely result in significant savings to CU. It also does not appear necessary to pay external business association food costs from CU funds. Adequate documentation of food purchases including a list of attendees and/or general information that stated who was served should be provided to substantiate food costs. Food request forms should be signed by the requestor and their supervisor to document proper approval of food purchases.

Considering the extent of utility-provided food expenditures, it appears CU should develop comprehensive policies regarding food purchases in an effort to control and reduce expenditures in this area.

B. Of 45 procurement card expenditures reviewed, 25 did not appear to be prudent and necessary uses of public funds.

- A barbeque grill at a cost of $1,382 used for safety meetings at the Southwest Power Plant.

- Toy store gift cards totaling $1,070 given to children of CU employees for contests. Other instances were noted where gift cards were purchased and documentation of the recipient was not maintained.

- Coffee mugs totaling $1,047 given to prospective telecommunications customers.

- Tins of mints totaling $808 given to attendees of a legislative lobbying event.

- Skeet ball and inflatable games totaling $695 used at the employee family day event. Additional items such as finger puppets, games, and decorations were purchased for family day totaling $248. Additional expenditures relating to family day are noted at MAR number 3.

- Deli trays and other gifts totaling $635 given to select commercial customers at Christmas.

- Dinner dishes, glasses, and flatware totaling $622 used by the board and general management during dinner meetings.

- Christmas cards from the General Manager totaling $559 given to board members, organizations, and select CU customers.

- Tablecloths and centerpieces totaling $520 for a Springfield Contractor's Association meeting.

These expenditures do not appear to be a prudent and necessary use of public funds. The Board of Public Utilities should ensure public funds are spent only on items which are necessary and beneficial to the utility. City residents have placed a fiduciary trust in their public officials to spend utility revenues in a prudent and necessary manner.

C. Cardholder use has not been adequately analyzed leaving CU with potential unnecessary liability. During the year ended September 30, 2006, CU had issued approximately 100 procurement cards to employees. Although employees can be held accountable for purchasing personal or unauthorized items using CU's procurement card, the utility is ultimately liable for all purchases made on these cards. We found some cardholder accounts had not been used, and some cardholder account limits were excessive based upon their past use. Sound business practices dictate CU personnel review procurement card usage to evaluate each employee's continued need for a card and excessive procurement card limits.

D. Cardholders were circumventing purchase limits by splitting purchases, and cardholder transaction limits were exceeded. While monthly procurement card statements of each cardholder are normally reviewed by the cardholder, cardholder's supervisor, and the procurement card committee, some cardholder's transaction limits were exceeded.

Some cardholders exceeded card transaction limits by splitting purchases to the same merchant on the same day. Two instances involved the same cardholder, whose single transaction limit was $2,000, but by splitting purchases to the same merchant, on the same day for automotive parts, the cardholder succeeded in exceeding purchase limits by $921 and $775.

Other instances were found where employees charged amounts in excess of their approved card transaction limits of $500. A formal review of employee card transaction limits filed with VISA was not performed by CU. As a result, the credit card company has provided these cardholder's greater transaction limits than those approved by the procurement card committee.

To ensure established procurement card spending transaction limits are followed, monthly statements should be reviewed more thoroughly by supervisors and the procurement card committee. In addition, a formal review of employee card transaction limits filed with VISA should be performed.

E. Various CU procurement card policies and procedures were not followed. For example:

- Purchases were returned to the vendor on two occasions, and supporting documentation for the reason of the return was not maintained as required by CU policy. The procurement card policy manual states "documentation should be kept explaining each credit received for returns or exchanges."

- Chemicals were purchased in violation of procurement card policies. The procurement card policy specifically states that chemicals and hazardous materials can not be purchased with procurement cards. CU's purchase order system provides greater control over these types of purchases.

- A supervisor provided her procurement card number to the department secretary to allow her to make purchases. The procurement card policy states the only person allowed use of the card is the employee to whom the card is issued.

Cardholder supervisors and the procurement card committee should more closely review procurement card transactions to ensure compliance with CU policy.

F. Reward points received through the use of procurement cards at a local hunting and sporting goods store were given to an employee for personal use. The utility should establish procedures with vendors to ensure any reward points are remitted directly to CU.

WE RECOMMEND the Board of Public Utilities:

A. Develop comprehensive policies regarding utility-provided food purchases. These policies should establish more specific guidelines regarding proper and allowable expenditures in this area, along with documentation requirements for these expenditures. In addition, CU should be more vigilant in its review of such expenditures to ensure public funds are used properly and efficiently.

B. Ensure all disbursements of utility funds are a necessary and prudent use of public funds.

C. Review procurement card limits for reasonableness and adjust employees' transactions limits based on their past procurement activities and their need to perform assigned duties.

D. Ensure procurement card statements are more thoroughly reviewed to ensure transaction limits are not exceeded. In addition, a review of employee procurement card transaction limits filed with VISA should be performed to prevent purchases from exceeding approved limits.

E. Ensure procurement card policies are followed.

F. Develop procedures to ensure all reward points are remitted to CU.

AUDITEE'S RESPONSE

A. Through the Board of Public Utilities, CU management has established procedures and protocol to manage procurement card use. Less than ten of the cardholders have the ability to purchase food. All transactions are reviewed monthly, as they have been since the inception of the program.

B. Every month the procurement cardholder prepares a reconciliation of purchases during the month. These reconciliations are reviewed and approved by at least one member of management. Additionally, the Procurement Card Committee reviews all transactions monthly. CU will continue to actively monitor procurement card transactions to ensure prudent and necessary purchases.

C. Some cards are held for emergency use and, therefore, may have higher card limits than their purchasing activity would appear to dictate. The contract negotiated with the issuing bank eliminates CU's liability for fraudulent purchases and therefore CU is not accepting excessive liability.

D. The Procurement Card Committee monitors transactions monthly and addresses transaction limit issues with the cardholders when they occur. In addition, CU has already implemented a control to verify the transaction limits implemented by the bank.

E. The majority of items noted in the State Auditor's report were discovered by CU prior to the state audit and were addressed immediately upon discovery. The Procurement Card Administrator meets with the Procurement Card Committee every month to review all purchase card transactions. Card transactions are reviewed to ensure compliance with policies and procedures. When situations are encountered that do not follow policy, appropriate steps are taken and are documented. Based upon the State Auditor's report, the procurement card manual will be changed to delete additional documentation requirements for returns.

F. This was changed in the July, 2007 revision of the Procurement Card Policies and Procedures manual, with the addition of a statement to prohibit employees from earning these points.

11. Memberships and Employee Reimbursements

CU paid approximately $342,000 for corporate and individual membership dues and should consider the necessity and related benefits received. Several employees were reimbursed for the same civic organization memberships, and several employees were reimbursed for multiple individual memberships. Numerous employee reimbursements did not appear to be a prudent or necessary use of public funds, more stringent guidelines to address dollar limits for meal reimbursements or meal per diems need to be established, and travel policies were not always followed.

A. CU needs to consider the necessity and benefits received from corporate and individual membership dues. CU paid corporate and individual membership dues totaling approximately $294,500 and $47,500 during the year ended September 30, 2006, respectively. For example, corporate memberships to organizations such as the Chamber of Commerce, Better Business Bureau, Downtown Springfield Association, and Springfield Apartment and Housing Association may not provide a necessary benefit to the utility. In addition, CU spends significant amounts on some corporate memberships to support lobbying efforts. These are in addition to the direct payments to the lobbyist discussed in MAR number 9. Several employees were reimbursed for civic organization memberships such as the Rotary Club and Kiwanis Club.

Several employees were reimbursed for multiple individual memberships. CU's policy allows reimbursement for one professional organization annually, and reimbursement for additional memberships can be approved by management. We noted 31 individuals had more than one membership reimbursed during the year ended September 30, 2006. For example, three directors/managers were reimbursed for five to seven memberships.

While a certain level of corporate and individual membership may be beneficial, CU should assess the importance compared to other critical needs of the utility.

B. Numerous employee reimbursements did not appear to be a prudent or necessary use of public funds. CU should consider revising their employee reimbursement and travel policies to establish more stringent guidelines to address dollar limits for meal reimbursements or meal per diems. While CU's meal reimbursement policy states that "it is still the employee’s responsibility to use good judgment and common sense in the selection of where and what meal choices to make when eating out," excessive meal costs were still incurred. These expenditures included:

- The General Manager treated representatives of the three major credit rating firms to dinner while they were in town to rate the Southwest II Power Plant bonds. The General Manager was reimbursed $1,252 for providing dinners at a private dining club and at a Springfield Cardinals baseball game. (CU's suite as discussed in MAR number 3 was used) Most of the individuals attending these functions were CU board members or employees and only a few were from the rating firms.

- Food was provided at Christmas parties for the customer service and meter reading employees totaling approximately $450 annually.

- Food purchases totaling approximately $324 were reimbursed to an employee for taking the Citizen's Advisory Committee members to a Springfield Cardinals baseball game. This committee advises CU on the public's perception of the utility.

- A supervisor was reimbursed $186 for food provided to teachers of a local public elementary school and their spouses at a Springfield Cardinals baseball game. This employee made several similar expenditures on her CU procurement card, and it is unclear why this was handled through employee reimbursement procedures.

- A congratulatory lunch costing approximately $119 rewarding three door-to-door collectors for collecting over $1 million in delinquent accounts. Eight CU managers also attended.

- "Goody Cart" snacks for customer service employees costing approximately $3,400 annually.

Numerous other examples of expenditures that appeared unnecessary were noted. These expenditures do not appear to be a prudent use of utility resources. CU should ensure funds are spent only on items which are necessary to meet the critical needs of the utility. Establishing meal limits or per diems allow for stronger controls over public funds.

C. Improvements are needed with CU travel policies. The employee reimbursement policy states the following when making travel arrangements: "In order to obtain the best rates on airfare, rental cars and hotels, the use of on-line travel websites is encouraged." However, the policy does not require a comparison to determine the most economical mode of transportation or lodging. We noted several employees use online services for making travel arrangements; however, many employees use the same local travel agency. Payments to this travel agency totaled approximately $69,000 during the year ended September 30, 2006.

Without a comparison of the expected costs, the utility has no assurance the most economical transportation or lodging is being utilized.

WE RECOMMEND the Board of Public Utilities:

A. Determine if participation in various organizations provides a direct benefit to the utility. Also, if employee participation in such organizations is not business-related and does not benefit the utility, such reimbursements should be discontinued.

B. Ensure all expenditures are a necessary and prudent use of public funds. Also, consider revisions to the current employee reimbursement policy to include meal cost limits or a reasonable per diem when purchasing business related meals.

C. Ensure travel policies are followed.

AUDITEE'S RESPONSE

A. As a locally owned utility, the Board and Management support employee involvement in organizations that improve employee skills and the quality of life in the community. Prior to any expenditure for membership in an organization, a review is made through a two-step approval process, which takes into consideration the value of the participation to the employee's job responsibilities, as well as to the customers and community City Utilities (CU) serves. As an essential component to business and economic development in this community, as a major employer, and as an important corporate citizen, CU must not only be involved but actively participate in a number of organizations.

B. CU's current employee reimbursement policy provides for reimbursement of business-related meals, provided these are reasonable meal expenses. This policy also gives CU the right not to pay for any part of meals determined to be unreasonable. This policy is fair to both our employees and customers. Additionally, there are typically a minimum of three levels of management review of these reimbursement forms.

C. CU's current policy which encourages employees to use online travel websites and personal credit cards to make travel arrangements does provide for a lower cost than going through Purchasing and using various vendors. CU will continue to review travel related costs and policies to determine the best way to contain these costs. Training is provided on a regular basis to ensure that administrative employees, who assist others in completing required travel documentation, understand all internal travel policies and forms.

12. Developer Reimbursements and Incentives

In an effort to promote extensions of CU's system in areas where the utility has competition in providing utility service, CU provides incentives to some developers that are not addressed in the utility's extension policy. CU incurred unnecessary costs totaling $21,500 related to a developer extension that could have potentially been avoided. In addition, CU did not always enter into written contracts for developer reimbursements, did not require the developer to submit documentation of actual costs incurred to support reimbursements made, and did not inspect and audit the developer's records in accordance with CU's extension policy. Some reimbursements were not calculated in accordance with policy, and the policy does not address the partial payment of developer reimbursements.

CU paid over $1.35 million in reimbursements and incentives to developers during the year ended September 30, 2006. Reimbursements are based on a written extension policy and occur when CU reimburses costs to developers who install electric, gas or water service to newly developed areas. Incentives payments are additional payments to developers that are not addressed in the utility's extension policy. CU's TecHouse staff oversees reimbursement and incentive payments and assists developers with residential, industrial, or commercial construction projects. Services provided by the TecHouse include service connections and fees, engineering design, utility cost estimates, subdivision designs, plat reviews, street lighting requests, security lighting requests, and fire hydrant meter requests.

A. CU provided incentive payments to some developers totaling approximately $127,500 during the year ended September 30, 2006 that were not addressed in CU's extension policy. For example, a developer was paid incentives totaling $41,654 for the cost of electrical lines and rock that were not reimbursable by CU's extension policy. CU provides these incentives in an effort to promote extensions of CU's system in areas where the utility has competition in providing utility service. The manager of developer services is responsible for negotiating these incentives with the developer. The level of approval required is dependent upon the total value of the project extension.

   To ensure equitable treatment of all developers, CU should ensure extension policies are followed and develop polices for incentives. In addition, it appears questionable whether CU should be negotiating and providing developer incentives in an effort to compete with private utility companies.

B. CU does not have a policy to reimburse developers for fiber optic conduit extensions; however, the utility reimbursed a developer a total of $21,500 to extend fiber optic conduit to a newly developed area of northwest Springfield in 2006. This extension was completed in anticipation of securing a large SpringNet® service contract with a nationally recognized cellular phone service provider that was building a call center in the area. While SpringNet® had started negotiations with the company, no agreement was made with the prospective customer before the extension was installed and reimbursement was made to the developer by CU. Ultimately, the customer decided to use a different vendor. This extension of fiber optic conduit remains unused and the costs incurred appear unnecessary. See additional recommendations regarding SpringNet® at MAR number 7. CU should adequately plan and develop a policy for extensions of the fiber optic conduit.

C. CU did not always enter into written contracts for developer reimbursements as required by CU's extension policy. For example, CU has not entered into a written agreement with the developer of an upscale residential community for developer reimbursements of more than $699,000 paid between 1999 and 2007 for system extensions. In addition, incentive payments of more than $214,000 were provided to this developer to cover the costs of rock, electrical lines, and decorative street lighting which was not addressed by CU's extension policy. Usually, staff at the TecHouse work with developers on system extension and then execute written contracts to clarify CU's responsibility; however, a written contract was never executed with this developer.

Section 432.070, RSMo, requires contracts of political subdivisions be in writing. A written contract, signed by the parties involved, should specify the services to be rendered and the manner and amount of reimbursement to be paid. Written contracts are necessary to ensure all parties are aware of their duties and responsibilities and to provide protection to both parties.

D. CU does not have adequate procedures in place to review developer reimbursement costs for accuracy. While contracts with developers require disclosure of actual costs incurred, CU does not require the developer to submit this information. In addition, while the reimbursement contracts allow CU to inspect and audit the developer's records such procedures are not performed.

Without proper review of developer costs, CU cannot determine whether the developer reimbursements are reasonable and proper.

E. Not all reimbursements were calculated in accordance with CU's extension policy. For example, while most reimbursements are based on the length of the extension, we noted a reimbursement was based on a percentage of the developers cost to install the extension. An effort should be made to handle these reimbursements in a consistent manner and to follow established extension policies to ensure equitable treatment of all developers.

F. CU's policy on developer reimbursements does not address partial payments for system extensions that are still in progress. For example, we noted a developer was reimbursed $32,973 in May 2006 before the work was completed. A memo prepared by CU documenting the request for the partial payment indicated that the developer did not have the funds in his budget to pay the subcontractor. The remaining $27,020 was reimbursed to the developer after the work was completed. Generally, CU reimburses the developer after all work is completed and ownership of the extensions can be transferred to the utility.

To ensure equitable treatment of all developers, CU should develop a policy for handling partial payments on system extensions.

WE RECOMMEND the Board of Public Utilities:

A. Ensure extension policies are followed and developed for incentives.

B. Develop a policy for handling extensions of the fiber optic conduit.

C. Enter into formal written contracts which specify the services to be provided and the amount of reimbursement. These contracts should adequately detail the rights and duties of all parties to the respective contracts.

D. Consider implementing procedures to periodically review developer costs for accuracy.

E. Handle all reimbursements in a consistent manner.

F. Develop a policy for handling partial reimbursements on system extensions.

AUDITEE'S RESPONSE

A. The extension policy enables CU to compete for the right to serve new customers inside its defined territory in accordance with the city charter and state law.

Developer reimbursements are the agreements CU makes with developers to reimburse them for the costs to install the utility facilities. CU then takes possession of these facilities. Therefore the reimbursement to the developer for a predetermined cost is in payment for what becomes CU property, as directed by the CU extension policy.

CU will consider developing a written policy regarding developer incentives as recommended by the State Auditors.

B. CU will consider a policy for extension of conduit that can be used for extending the fiber optic system as recommended by the State Auditors. The actual fiber optics system is not extended until a customer contract is signed.

C. The Board approved extension policy since 1999 requires all developer reimbursement contracts to specify the services to be provided and the amount of reimbursement. A "Charges and Estimated Reimbursement to Developer" form is prepared before the execution of each contract detailing the reimbursements based on design units. At the end of the contract a "Reimbursement to Developer" form that adjusts the reimbursements based upon finalized as-built units is prepared. In the example cited by the State Auditor, CU did not enter into written contracts with this developer; however, the agreement was initiated prior to the adoption of an extension policy requiring a written agreement.

D. The current CU extension policy requires the developer to provide CU with the actual bids from contractors for utility extensions upon request. CU reviews this data to establish an average cost for utility extensions that is reflected in the extension policy, which is revised and updated every two years. Therefore, a process is already in place to continually review developer costs.

E. Since formal policy inception, developer reimbursements have been handled in accordance with the board-approved extension policy for the applicable period.

F. CU does not reimburse for any work that is not installed. CU will review the extension policy regarding the issue of partial payments.

AUDITOR'S COMMENT

C. CU continues to provide reimbursements to this developer and thus a written agreement would seem appropriate.

D. CU should review documentation of the developer's actual cost as required by contracts.

E. Not all reimbursements were calculated in accordance with CU's extension policy.

13. Cost Benefit Studies

CU did not perform or update cost benefit studies to evaluate the necessity for some marketing and communication services, print shop services, and for the onsite health clinic. Cost benefit studies were not performed or updated in the following areas:

- Marketing and communication costs totaled over $1.1 million during the year ended September 30, 2006, of which approximately $560,000 was for salaries paid to eight employees and $155,100 was to an outside advertising agency. Another local company that provides electric, gas, and water services and has more electric customers than CU indicated marketing and related salary expenditures for their company totaled $298,000 (during 2005 which was the most current information available). In addition to annual marketing and communication costs, CU maintains and operates its own recording studio with assets CU has listed at over $537,000 based on historical cost. CU personnel estimated the annual cost to operate this totals between $6,000 and $8,000 (operating costs would be included in the $1.1 million marketing and communication costs above). The recording studio is used for other purposes than advertising such as recording various meetings and training materials.

  The marketing and communications department manages daily contact with residential and business customers through advertising, media relations, marketing information, community relations, one-on-one contact with large industrial customers, and development of commercial and business programs. CU needs to evaluate the costs and benefits of marketing and communication related activities.

- The utility spent approximately $300,000 to operate the print shop during the year ended September 30, 2006. CU maintains a separate building and printing equipment, and employs five individuals to print various items such as business cards, bill inserts, and other special projects. Several print shop projects did not appear to be a prudent or necessary use of resources, and the cost of each print project is not tracked. For example:

  - A commemorative picture book of the 2007 ice storm costing approximately $5,300 was given to employees.

- Commemorative books of the 50th anniversary of James River Power Station (including DVD) and CU's water system costing approximately $4,900 and $4,500, respectively, was given to employees and available for the public.

The cost of these projects was calculated by CU at our request. These expenditures do not appear necessary or essential to the operation of the utility. The utility has a fiduciary duty to ensure funds are expended in a manner that provides the greatest benefit to the utility. In addition, project costs should be tracked to help evaluate the cost effectiveness and necessity of print shop projects.

- CU performed a cost benefit study of a possible in-house medical clinic in June 2005 prior to entering into a one year contract for these services in August 2005; however, the preliminary cost benefit study was not updated to aid the utility in determining the cost effectiveness of operating the in-house medical clinic and in deciding to extend the contract agreement another year. CU expended $236,577 in physician charges and medical supplies during the year ended September 30, 2006 to operate the in-house clinic. An additional $80,010 in remodeling costs was spent to establish the clinic location. The clinic is open approximately 20 hours each week, and in-house medical services are provided to CU employees, dependents, and retirees.

Given the extent of expenditures in these areas, it is essential that formal cost benefit studies be performed and updated periodically to evaluate the necessity of these services and ensure utility funds are being spent in a cost effective manner.

WE RECOMMEND the Board of Public Utilities perform cost benefit studies and review advertising and print shop costs to ensure they provide a benefit to the utility. The utility should track the cost of each print shop project, and the preliminary cost benefit study of the in-house medical clinic should be updated periodically.

AUDITEE'S RESPONSE

As a multi-service utility providing essential services in a large community, the Board and management of the utility recognize the value of an effective public communications program. CU management will continue to evaluate communications projects on their merits and ensure costs continue to be recorded in a manner that provides the ability for effective tracking and analysis.

Regarding the on-site medical clinic, CU is currently analyzing the financial data for the first two years of clinic operations and will update the cost-benefit analysis and report the results to management.

14. Compensation

CU used varying market standards to establish a salary plan for its General Manager and Associate General Managers. Salaries for these seven positions were paid according to a different market standard than other CU employees and ranged from $124,359 to $326,484 for the year ended September 30, 2006. The General Manager's contract has not been updated for a new salary plan which became effective in January 2005 and provides for a severance package valued at over $517,000. It is unclear whether the General Manager's service on a hospital and bank board is within the scope of his duties, and he is personally compensated by the bank board.

CU contracted with a professional consulting firm to perform an analysis of executive salaries and benefits after local news media coverage, in 2003, which criticized CU's benefits as too lucrative. The consulting firm has subsequently been used to conduct salary studies for non-executive and non-union employees. Union salaries are based on negotiations with the applicable union. CU adopted a new salary plan effective January 2005 to simplify its pay structure and to bring its salaries more in line with the labor market. As of January 2007, CU had 23 employees whose salaries were frozen until such time as they fall within the appropriate pay range for their position. During our review of these studies and the related employment contracts, we identified the following concerns:

A. CU has not consistently applied standards of the salary studies to all employee salaries, and as a result, higher salaries were paid to the Associate General Managers and the General Manager.

While CU chose to use the "Base 50th" category of the comprehensive study for its standard to set CU non-executive employee salaries, it used the Market Average Total Cash Compensation (TCC) as its standard to set salaries of its six Associate General Managers. The TCC standard includes bonuses paid to executives of the other utilities included in the study. CU's Human Resources Director indicated this is done because CU wanted the Associate General Manager's salaries to be comparable to those of executives at other utilities who receive bonuses as part of their compensation. In addition, two of the Associate General Manager's salaries have been frozen based on the TCC standard.

CU used a different category (than was used for its Associate General Managers or non executive employees) as it's standard for setting the salary of the General Manager. CU used the "Base Average Combined Market" standard for this position. CU's Human Resources Director indicated this is the standard that has been historically used by CU to set the General Manager's salary in comparison with what the outside consultants refer to as the "general industry and other utilities" labor market. The dollar amount for this standard is over $53,000 more than the standard being used for the Associate General Managers and is over $85,000 more than the standard being used for CU's non executive employees.

The General Manager's salary for the year ended September 30, 2006 was $326,484 (excluding his vehicle allowance).

Since non-executive employees of other utilities also receive bonuses, CU is applying a salary standard to the advantage of the Associate General Managers. CU is also applying a salary standard to the advantage of the General Manager.

Paying higher salaries to the CU Associate General Managers and General Manager based on varying market standards does not appear to be a prudent use of public monies.

B. CU's employment contract with the General Manager has not been updated for the salary plan that was adopted in January 2005, and provides a severance package which may be excessive. The General Manager's employment contract provides a severance package in an amount equal to 18 months of salary and benefits if he is terminated without cause. The value of the General Manager's severance package was approximately $517,000 as of July 2007. In comparison, the city manager's contract only provides for four months of salary and benefits upon termination.

The employment contract with the General Manager should be updated to include the correct salary grade. Termination clauses are common in employment contracts and if used properly can help provide adequate protection to the utility in the event of nonperformance. The board should consider the necessity of including these excessive severance payments in future employment contracts.

C. The General Manager serves on the boards of a local hospital and a local bank on CU time and is personally compensated by the bank for his service. This compensation is not reported to CU. The amount of compensation was requested during our audit; however, the General Manager declined to provide it. The General Manager is involved with numerous civic and professional organizations. Such involvement is encouraged by the board as is documented in a resolution appointing him to this position. The resolution states that involvement in civic groups in Springfield, and professional utility organizations and associations elsewhere, are within the scope of his duties; however, it is not clear that this would include his service on the hospital and bank boards.

WE RECOMMEND the Board of Public Utilities:

A. Apply a consistent and equitable standard to salary determination and ensure salaries paid represent a prudent use of public monies.

B. Ensure the contract with the General Manager is updated to include the correct salary grade, and consider the necessity of including severance payments in future employment contracts.

C. Review the General Manager's involvement with these boards.

AUDITEE'S RESPONSE

A. The current Board approved policy clearly states the appropriate comparisons to be made with regard to General Manager, Associate General Managers, and all other nonunion compensation. The Board will review the survey benchmarks used for the executive positions during the next comprehensive salary and benefits survey scheduled for the fall of 2008.

B. In order to attract and retain the caliber of employee the Board requires to fill the General Manager (GM) position, it is necessary to compete nationally. The current employment contract between the GM and the Board is valid and binding on each party. The contract has, in effect, been modified by increases in compensation which are a matter of written record, although not incorporated in a new employment contract. Legally, that is not necessary.

The GM terms of employment, including a severance package, are within the authority and discretion assigned to the Board. The severance package is a common and necessary component of the compensation package for the GM position of a large public power utility.

C. The General Manager will continue to obtain guidance from the Chairman of the Board as to the benefit and appropriateness of each board/committee that he serves as a member. He will also continue to report to the Board on an annual basis information regarding his participation on various community boards.

15. Cash Handling and Control Procedures

Controls and procedures over cash handling at the main office, TecHouse, and with door-to-door collectors are in need of improvement.

CU collects utility payments at several cashier stations in the lobby of the main office, through the mail and night depository, at collections sites located in local banks and grocery stores, electronically, and through door-to-door collections. CU collected approximately $366.8 million in utility payments during the year ended September 30, 2006. CU also collects monies for applications for utility service connections or extensions at the TecHouse.

A. CU does not adequately account for some monies received by mail room employees. The mail room employees process most utility receipts through a check processing machine and any monies that do not match the utility statements are taken to a senior customer service representative (senior CSR) working in the vault for processing. Cash received in the mail is transmitted to a senior CSR and then transmitted to a cashier in the main lobby for processing.

To adequately safeguard receipts and reduce the risk of loss, theft, or misuse of funds, monies received in the mail room should be recorded when initially received to ensure the amounts are properly handled.

B. Controls over receipts could be improved by limiting access to cash received in the night depository. Currently, a security guard retrieves monies (cash and checks) from the night depository and transmits the monies to a senior CSR who transmits the monies to the mail room processing employees. Mail room processing employees process the checks received through a check processing machine; however, cash receipts are transmitted to senior CSR's working in the vault (one of these senior CSR's is responsible for receiving the monies from the security guard earlier in the day). The cash receipts are then transmitted to a cashier in the main lobby for processing.

To improve internal controls, access to cash receipts received through the night depository should be limited.

C. Receipt numbers assigned by the electronic accounting system used to process utility receipts in the main lobby are not tracked or otherwise accounted for by the utility. While cashiers and senior CSRs ensure transaction numbers restart each day, no one reviews the receipt numbers assigned to account for their numerical sequence. To adequately account for all utility receipts, the numerical sequence of receipt numbers assigned should be accounted for properly.

D. The security of the password system used by the utility to process utility receipts is dependent upon users properly exiting the system. Each cashier has a confidential password for their assigned workstations; however, workstations are not always shut down by the cashier when they leave for lunch. If the lobby gets busy, one of the senior CSRs will process utility receipts at the "open" cashier's workstations. As a result, there is less assurance utility receipts are handled and accounted for properly. In addition, senior CSRs have an assigned workstation.

E. CU prepares a daily worksheet showing overages and shortages at each cashier's workstation and reviews significant shortages; however, the utility does not document its review or reasons for the shortages. For example, we conducted a cash count of all workstations on May 15, 2007 and a shortage of $80 was identified at one of the workstations. The utility did not document its review of the shortage or possible reasons why the shortage occurred. CU should document its review of shortages and document possible reasons why shortages occur to adequately account for all utility receipts.

F. CU allows employees to cash personal checks from daily cash receipts, and during our cash count, we noted a customer's tax refund check was cashed. Cashing employee personal checks or customer's third-party-checks from daily cash receipts reduces the accountability for monies received. In addition, receipts for utility payments should be deposited intact so that the composition of deposits can be reconciled to the composition of receipts.

G. Controls and procedures over monies collected at the TecHouse need improvement. CU collects monies for applications for utility service connections or extensions at the TecHouse. Applications are sequentially numbered by the utility's electronic job order tracking system. The TecHouse collected approximately $3.3 million during the year ended September 30, 2006. The following concerns were identified relating to TecHouse receipts:

- Receipt slips issued by the TecHouse are not prenumbered. To properly account for all receipts and ensure they are properly deposited, prenumbered receipt slips should be issued for all monies received.

- The method of payment (i.e., cash, check, or money order) is not always recorded on the receipt slips. To ensure all receipts have been recorded properly and deposited intact, the method of payment should be recorded on each receipt slip and the composition of receipts should be reconciled to the composition of bank deposits.

- The numerical sequence of applications is not reconciled to monies received and deposited. To ensure fees for applications are properly collected, recorded, and deposited, the numerical sequence of applications should be accounted for and reconciled with amounts recorded and deposited.

- Application fees are waived by the TecHouse staff without approval of the General Manager or his representative as required by CU policy. CU should ensure all application fee waivers are approved in accordance with utility policy.

- Monies received by the TecHouse Monday through Thursday are not deposited in a timely manner. TecHouse monies are picked up by a courier and delivered to the main CU office to a senior CSR Monday through Thursday. These monies are held until the following day to be deposited. On Friday monies are taken directly to the bank by the courier. In addition, the senior CSR does not reconcile monies received from the TecHouse to the deposit thus it is unclear why these monies are not deposited daily. To adequately account for collections and reduce the risk of loss or misuse of funds, deposits should be made on a timelier basis Monday through Thursday.

H. Controls and procedures over door-to-door collections need improvement. CU has two door-to-door collectors who collect and perform disconnects on delinquent utility accounts. The collectors prepare a monthly report of activity which documents the total collections, the number of bills collected, the number of cutoffs, reminders, and promises to pay for each day of the month. Some delinquent customers are required to pay their utilities in cash; therefore, the door-to-door collectors often collect large amounts of cash. The collectors typically drop off monies collected and the related receipt slips each evening in the night depository (see part B. above). The door-to-door collectors collected approximately $1.3 million during the year ended September 30, 2006. The following concerns were identified relating to door-to-door collections:

- Receipt slips issued by the door-to-door collectors are not prenumbered. To properly account for all receipts and ensure they are properly deposited, prenumbered receipt slips should be issued for all monies received.

- There is no written policy on the minimum amount a customer must pay to avoid being disconnected from utility services. Door-to-door collectors are given discretion as to how much the customer must pay to avoid cutoff of utility services. Formal policies should be established to provide the door-to-door collectors guidance on delinquent amounts to be collected in order to avoid cutoff of utility service.

- Monthly activity reports are not reconciled to amounts collected and deposited. To ensure door-to-door delinquent collections are properly collected, recorded, and deposited, the monthly activity reports should be reconciled with amounts recorded and deposited.

- Monies received by door-to-door collectors are transmitted to several employees before being recorded in the customer's account. For example, on August 22, 2007, one of the collectors received over $7,000 and due to the large amount of cash received, the collector transmitted his collections to a senior CSR during the day rather than carrying around a large amount of cash in his vehicle. This senior CSR transmitted the monies to the senior CSRs that work in the vault who then transmitted the monies to a cashier in the main lobby to be processed. Similar concerns were noted above with access to cash collected in the night depository. To improve internal controls, access to cash receipts received by door-to-door collectors should be limited.

I. Nine local banks and grocery stores act as collection sites for CU, allowing customers to drop off utility payments. These collections sites received utility payments totaling approximately $5.4 million during the year ended September 30, 2006. CU does not have written contracts with three of the collection sites. In addition, CU has not established documented controls and procedures to guide the nine collection sites in handling utility payments. For example, CU reported a deposit in transit from one collection site on the September 30, 2006 bank reconciliation; however, the collection site did not deposit these funds until October 13, 2006.

Written contracts are necessary to ensure all parties are aware of their duties and responsibilities and to prevent misunderstandings. In addition, CU should document established controls and procedures related to collection sites to provide guidance regarding collecting and depositing utility funds, and monitor compliance with established controls and procedures.

J. Controls over utility petty cash funds need improvement. The utility has ten petty cash funds totaling $2,700 which are maintained at various locations throughout the utility. Another petty cash fund handled by the main office totaling $4,000 is used to replenish these funds and make purchases for the main office. The following concerns were noted related to these petty cash funds:

- The balance of the petty cash fund maintained at the main office appears excessive. Reimbursements to this petty cash fund did not exceed $1,386 and totaled only $15,628 during the period October 2006 through July 2007. Lowering the main office petty cash balance would reduce the amount of cash held and the risk of loss or misuse. The petty cash needs of the main office should be evaluated and the balance set at a reasonable amount.

- Documentation of petty cash expenditures made from the other ten funds is not reviewed by the senior CSR responsible for replenishing those funds from the main office petty cash fund. While a log of petty cash fund activity is submitted to the senior CSR, actual documentation including invoices of petty cash expenditures is not reviewed prior to replenishment. The accounts payable department reviews the invoices for the ten funds before replenishing the main office petty cash fund. To ensure accountability of petty cash funds and prevent misuse of funds, documentation of petty cash expenditures, including invoices, should be reviewed by the senior CSR prior to replenishment of the other ten petty cash funds.

WE RECOMMEND the Board of Public Utilities:

A. Ensure all monies received in the mail room are properly recorded.

B. Limit access to cash received through the night depository.

C. Ensure the numerical sequence of receipts slips is accounted for properly.

D. Ensure workstations are properly exited by cashiers when leaving for lunch.

E. Ensure the review of shortages and possible reasons why shortages occur is adequately documented.

F. Discontinue the practice of cashing personal checks for employees and third party checks from customers, and deposit utility receipts intact.

G. Ensure prenumbered receipt slips are issued for all monies received at the TecHouse, the method of payment is recorded on each receipt slip, and the composition of receipts is reconciled to the composition of deposits. Also, ensure the numerical sequence of applications is accounted for properly, and reconcile applications issued to amounts deposited. In addition, application fee waivers should be approved in accordance with utility policy, and monies should be deposited daily.

H. Ensure prenumbered receipt slips are issued for all monies received by the door-to-door collectors, establish formal policies regarding delinquent amounts to be collected in order to avoid disconnection of utility service, reconcile monthly activity reports with amounts recorded and deposited, and limit access to door-to-door collections.

I. Enter into written agreements with all collection sites and also document established controls and procedures over their collection of utility payments.

J. Implement stronger controls over petty cash funds including reviewing the main office petty cash balance to ensure the fund balance is not excessive, and requiring the senior CSR responsible for the main office petty cash fund to obtain and review supporting documentation for petty cash fund expenditures prior to replenishment of other funds.

AUDITEE'S RESPONSE

A. All monies received by City Utilities are accounted for and properly recorded. Additionally, the State Auditor brought no discrepancies to our attention. Effective October 1, 2007, a log of all cash received is maintained by the remittance processing personnel.

B. Effective October 1, 2007, the security guard has been instructed to deliver the night depository envelopes directly to the remittance processing personnel.

C. CU utilizes a software package to control the numerical sequencing of receipts. Sequence numbers will be verified periodically to ensure the software is operating as intended.

D. CU recognized this issue during system testing in 2000 and established compensating controls prior to implementation in 2001. This is a software limitation that CU is actively monitoring for upgrade enhancements to address. Until then, this rarely encountered situation is monitored through additional controls.

E. *At least two senior customer services staff review the cash and daily work in an effort to locate possible reasons for any difference in the cashier drawers. For the year ended September 2007, cash overages totaled $1185 and cash shortages totaled $1533 for a net shortage of only $348 on total receipts of over $445 million, including those taken at the cashier windows.*

F. *Effective October 15, 2007, Policy #2.39 was issued that states customer services representatives will no longer cash employee checks – personal or third party.*

G. *CU is completing efforts on redesigning the customer receipts issued to incorporate pre-numbering and method of payment. The courier has also been instructed to deposit funds directly with the bank daily. CU will evaluate the current waiver policy and adjust if deemed appropriate.*

H. *CU is reviewing controls in this area and will recommend changes as needed. State audit report recommendations will be considered during this evaluation.*

I. *There are currently two remaining collection sites without signed agreements. These sites have been contacted and agreements are in process. The standard collection site agreement already contains language regarding timely deposits. Procedures have been implemented to track deposits and address any issues encountered related to untimely deposits.*

J. *Current controls ensure that petty cash funds are properly handled and expenditures are accounted for in the financial records. Approval of the replenishment form and a review of the attached invoices are the responsibility of the petty cash custodian's department manager, prior to replenishment of funds. Upon receiving an approved replenishment form, the senior customer services representative verifies the approval of the form prior to replenishing the fund and forwards the replenishment form with all attached receipts to accounts payable for an additional detailed review of the receipts for accuracy and appropriateness. Any errors detected in accounts payable are corrected directly through the custodian's petty cash fund.*

16. Utility System Controls and Procedures

Policies and procedures for adjustments, write offs of uncollectible accounts, and customer deposits need improvement. The duties of billing and adjusting large customer accounts have not been adequately segregated.

A. No formal written policies and procedures have been established regarding utility account adjustments. For example, policies and procedures have not been established to discourage employees responsible for collecting and adjusting customer accounts from handling utility accounts of relatives or accounts where the potential for a conflict of interest exists. Over one million adjustments were made during the year ended September 30, 2006. While some adjustments are automatically handled by the computer system, many are processed by cashiers and senior CSRs.

Policies should include dollar limits on adjustments made without prior supervisory approval and monitoring of patterns of adjustments made by cashiers. Written policies and procedures should be established to provide cashiers with guidance and limit the risk of improper adjustments.

While supervisors review a report of adjustments made by employees daily, this review is not adequately documented. Rather than initialing and dating the report to document that they have reviewed and approved all adjustments by employees whom they supervise, supervisors are only required to cross out their initials which are manually added to the first page of the report. All supervisory reviews of adjustments should be adequately documented.

B. The utility does not have a written policy for the write off of uncollectible accounts receivables. Currently, the electronic accounting system generates a query based upon when the fourth delinquent notice is sent to each customer or when the customer's account is approximately 90 days delinquent. Two customer service representatives initiate the write off process. Write offs are reviewed with adjustments as noted in Part A. All write offs are turned over to a collection agency. During the year ended September 2006, the utility wrote off accounts receivable of approximately $1.8 million.

A written policy related to write-off procedures is necessary to ensure consistency and establish adequate internal controls over accounts receivable. A write off policy should include which accounts and how often accounts should be written off, which accounts should be turned over to the collection agency, and the approval procedures for the write off of accounts.

C. The duties of billing and adjusting large customer accounts have not been adequately segregated. The Director of Pricing receives usage information from the power quality department and enters it into the Complex Billing System which allows the director to enter generic customer information that affects the customer's billing. The Customer Information System (CIS), an electronic system, generates a bill for the customer based upon the Complex Billing System. In addition, adjustments are made to customer accounts in this system by a Rates Analyst, who is supervised by the Director of Pricing, and reviewed by the same director. CU collected over $59 million from large customer accounts during the year ended September 30, 2006.

Someone independent of the Complex Billing System should review billings and adjustments of large customer accounts to safeguard against possible loss or misuse of funds.

D. While the utility has a general policy regarding customer deposits, the policy does not specifically indicate the amount required for residential customers, or procedures for refunding deposits prior to termination of service. In addition, the policy does not provide any guidance on waiving customer deposits.

Currently, CU collects a $100 deposit for new residential customers and $150 deposit for a returning residential customer with a bad payment history. In addition, non-residential customers are normally only charged two and one-half times the highest bill for one billing period. Also, if residential customers and non-residential customers have not had their service disconnected for non-payment for approximately 12 and 24 months, respectively, the deposit is refunded. Customer deposits are often waived, and documentation of the reasons for the waiver is not always retained. As of August 31, 2007, the utility was holding deposits totaling $3.7 million.

The utility's policy states that before metered service is connected, it may require its customers to provide evidence satisfactory to itself that all bills for service rendered or to be rendered will be paid promptly; or in lieu thereof, the utility may require the customer to maintain with the utility a cash deposit or security as determined by the General Manager, with the deposit amount on non-residential customers not to exceed three times the highest bill for one billing period for each service or an equivalent amount as estimated by the utility. In addition, the policy indicates such deposits shall be refunded at the termination of service after all charges that may be due and payable by the customer have been paid, or at such earlier times as determined by the General Manager.

A more detailed written deposit policy related to customer deposits is necessary to establish adequate internal controls over deposits and ensure customers are treated in an equitable manner. In addition, to ensure proper accountability over customer deposits, reasons for waiving customer deposits should be documented and reviewed.

E. CU is not adequately monitoring non-cash customer deposits, and the listing of these deposits is not accurate. For example, we noted several deposits included on the listing had expired. A manager of customer services indicated the listing had not been properly updated. CU policy indicates other security (such as bonds and letters of credit) in lieu of cash deposits may be accepted as approved by the General Manager. CU should establish procedures to ensure non-cash customer deposits are accounted for properly and the deposit listing is accurate.

WE RECOMMEND the Board of Public Utilities:

A. Establish formal written policies for adjustments made to utility accounts. These written policies should provide cashiers with guidance and limit the risk of improper adjustments. In addition, all supervisory reviews of adjustments should be adequately documented.

B. Develop written policies for the write-off of uncollectible accounts.

C. Require someone independent of the Complex Billing System to review billings and adjustments of large customer accounts.

D. Establish a more detailed policy for the handling of customer deposits. In addition, documentation should be maintained and reviewed for customer deposit waivers.

E. Ensure non-cash customer deposits are adequately monitored and related records are accurate.

AUDITEE'S RESPONSE

A. Written procedures are given to each CSR during the extensive training process. Adjustment reports have been consistently monitored through various levels of review within customer services, in addition to a review in the finance department. Documentation of these reviews has been changed and is now sufficient. Customer services will also work with internal auditing to explore additional possibilities of monitoring long-term patterns of adjustments utilizing audit software.

B. The majority of the write-off process is automated within the system to safeguard against fraud or misuse of funds. Procedure specifications are delineated in the automated process to remove the judgmental aspect. Additionally, write-offs appear as a separate adjustment code in the adjustments report noted above, that is reviewed by customer services and finance. The effectiveness of current write-off procedures is confirmed by the fact that, historically, CU's write-offs as a percentage of revenue consistently run below industry average. Additional procedures are being written to provide to CSR's during training.

C. Duties are appropriately segregated within the pricing department to prevent one person from adjusting and confirming the adjustment for billing on the same account. Additionally, the monthly journal entries from this area are reviewed and approved by a manager in finance. Furthermore, the customer bills and related adjustments are billed through the Customer Information System utilized for normal customer billings, so the adjustments appear on the adjustments detail report reviewed by both customer services and finance.

D. CU's policy provides general guidance related to deposits, however, detailed procedures are provided to CSR's during the initial training sessions. These procedures cover deposits and the release of deposits. Additionally, released deposits appear as an adjustment and are captured on the adjustments report discussed previously and reviewed by supervisors in customer services and finance. Customer deposits are intended to reduce the risk of non-payment to CU, and vary, dependent on customer payment history and ability to pay for services.

E. *Non-cash customer deposits have been updated and will be routinely monitored for expiring documents.*

17. Transit Department

The transit department's cash handling procedures need improvement. Duties are not adequately segregated, and improvements are needed with the handling of cash collected on the buses. In addition, deposits are not made on a timely basis, the composition of monies received is not reconciled to the composition of monies deposited, and checks are not always endorsed upon receipt.

CU has operated the public transit system for the City of Springfield since 1945. Currently, the transit system has 14 fixed day routes and three night routes, encompassing approximately 175 miles. In addition to these fixed routes, CU offers a paratransit service that provides rides to passengers who require additional resources to facilitate their bus travel.

Customers place cash or a bus pass in the fare box upon entering the bus. The fare box system tracks the amounts received and this information is uploaded nightly and made available to administrative staff at the main transit office. Once a week, the cash and bus passes are removed from the fare box and cash is deposited. Bus passes can be purchased in advance at the main terminal or at various designated locations. Receipts from bus fares and advertising totaling $721,000 were collected during the year ended September 30, 2006.

A. Cash handling and reconciling duties are not adequately segregated in the transit department. For example, the duties of receiving, recording, depositing, and reconciling monies received from designated pass vendors are completed by the office administrator. This individual also handles cash from the fare boxes and is responsible for reconciling amounts deposited to bus fare receipt reports.

   To safeguard against possible loss or misuse of funds, internal controls should provide reasonable assurance that all transactions are accounted for properly and assets are adequately safeguarded. Internal controls would be improved by segregating the duties of receiving and depositing monies received from that of recording receipts. If proper segregation of duties cannot be achieved, at a minimum, there should be an independent review and reconciliations of the recorded receipts to amounts deposited.

B. Some essential accounting and reconciliation procedures were not established or performed by the transit department.

   1. Improvements are needed in the handling of cash that is placed in bus fare boxes by customers. Monies from the bus fare boxes are removed and placed in money bags without being counted or otherwise accounted for

on a weekly basis. Each of these money bags is sealed with a numerical tag to identify the bag for the armored car service; however, these tags are not used in numerical order or controlled in any other way. Also, while the bags of cash are stored in the transit department's vault, several employees have access to this area.

In addition, no procedure exists to ensure that all fare boxes have been removed from the buses before a deposit is made. As a result, frequent overages and shortages are found when comparing the bus receipt reports (a report that shows the information the bus driver has recorded of each passenger type that boarded) to the amounts deposited. For example, none of the five bus reports we reviewed reconciled to amounts deposited with the largest difference totaling $294. Also, transit personnel indicated the difference could be as much as $800 each week.

The transit department does not track the differences on a perpetual basis and does not have formal written policies to guide employees on allowable overage or shortage amounts.

2. Monies received are not deposited in a timely manner. Monies received from the bus fare boxes are removed once a week and held in an outdoor vault overnight until transit employees place the money into bags for deposit. Weekly deposits reviewed ranged between $8,163 and $19,481.

   In addition, monies collected at the main office for bus passes are not deposited timely. For example, a cash count of main office receipts totaling $2,111 performed on January 29, 2007 identified monies on hand dating back to January 22, 2007.

3. Prenumbered receipt slips are not issued, and receipt slips are only issued upon request for monies received from vendors that purchase bus passes in bulk. In addition, the method of payment is not always noted on the receipt slips.

4. Although the method of payment is tracked by the cash register system used at the main transit office where daily and bulk bus passes are sold, personnel do not reconcile the method of payments received to the composition of the deposit to ensure receipts are deposited intact.

5. Checks are not always restrictively endorsed.

To adequately safeguard receipts and reduce risk of loss or misuse of funds, improvements are needed in the handling of cash, monies should be deposited in a timely manner, prenumbered receipt slips should be issued, composition should be recorded and reconciled to deposits, and checks should be restrictively endorsed immediately upon receipt.

<u>WE RECOMMEND</u> the Board of Public Utilities:

A. Properly segregate duties between available employees and/or establish a documented periodic review of receipts by an independent person.

B. Develop procedures to improve the handling of cash that is placed in bus fare boxes by customers, deposit receipts in a timely manner, track overages and shortages perpetually, and reconcile the composition of receipts to the composition of each deposit. Also, ensure checks and money orders are endorsed immediately upon receipt.

<u>AUDITEE'S RESPONSE</u>

A. Transit receipts are handled in a controlled process that involves a segregation of duties and oversight of cash handling. While the existing segregation of duties seems adequate, internal auditing will review again to consider if cost effective improvements can be made.

B. Due to an increase in transit revenue, transit staff will be depositing both the farebox receipts and bus pass sales twice weekly, instead of once a week as is the current practice. CU will ensure that checks and money orders are endorsed immediately upon receipt.

18. Fleet Management and Vehicle Allowances

Fuel usage is not reconciled to fuel purchased and on hand, and usage logs are not maintained for utility owned vehicles. CU allows 47 utility owned vehicles to be taken home daily by utility employees with many of these employees living outside city limits. CU has no documentation to show how vehicle allowance amounts paid to the General Manager, four Associate General Managers, and a director are reasonable compared to actual expenses incurred.

A. Fuel usage reports generated from the utility's automated fuel system are not reconciled to fuel purchases. In addition, usage logs are not maintained for any utility owned vehicles. The utility spent more than $1.8 million to purchase approximately 805,900 gallons of unleaded gasoline and diesel fuel for all departments including transit during the year ended September 30, 2006.

   Fleet management uses an automated fueling system to track fuel usage. Each time a vehicle is fueled, the system documents the vehicle's identification number, the current date and time, the current odometer or hour meter reading and amount and type of fuel dispensed. Reports generated from this system are not reconciled to purchases.

To ensure the reasonableness of fuel expenditures, CU should reconcile fuel usage reports to fuel purchased and on hand. Failure to account for fuel usage could result in theft or misuse. In addition, usage logs are necessary to document the appropriate use of vehicles and to also support fuel purchases. The logs should include the date, driver, purpose and destination of each trip, and the daily beginning and ending odometer readings for vehicles.

B. CU did not document the justification and approval of take home vehicles as required by utility policy. CU allows 47 utility owned vehicles to be taken home by utility employees, 25 are allowed to be taken home daily and 22 are allowed to be taken home when the assigned driver is on call.

The policy manual states that all full time take home vehicles must be justified on an annual basis and approved by the driver's department manager. This justification is to be maintained by the fleet management department. CU should ensure documentation of justification and approval of take home vehicles in accordance with policy.

In addition, over half of all take home vehicles are driven beyond the city limits of Springfield. For example, one employee commutes 79 miles round trip daily from outside city limits. Allowing utility employees living outside the city to take their vehicles home, may result in additional and unnecessary costs to the utility.

An internal audit report completed on January 12, 2006 showed many vehicles are being taken home daily without necessity or justification. According to the audit, CU could save approximately $60,000 annually if the unnecessary take home vehicles were eliminated. CU responded to the internal audit that as the current drivers of these take home vehicles retired or changed positions, they would not offer the benefit to the position's replacement.

C. CU has no documentation to show vehicle allowance amounts are reasonable compared to actual expenses incurred. CU pays a vehicle allowance of $659 monthly to the General Manager, four Associate General Managers, and to a director, who use personal vehicles to conduct utility business. Using the utility's current mileage reimbursement rate of $0.445 the monthly allowance paid to these employees represents approximately 1,481 miles per month. Additionally, it is questionable that all of these city employees should be paid the same vehicle allowance amount based upon the differing job duties and travel requirements. CU should review the reasonableness of the mileage allowances paid and set the allowances to reasonably reflect the actual expenses incurred by the employees.

WE RECOMMEND the Board of Public Utilities:

A. Ensure a documented periodic reconciliation of fuel purchased to amounts used is performed, and investigate any significant discrepancies. In addition, ensure usage logs are maintained for all utility vehicles.

B. Ensure documentation of justification and approval of take home vehicles is maintained in accordance with utility policy. In addition, review the cost effectiveness of allowing employees to take utility owned vehicles home.

C. Review vehicle allowances and set the allowances to reasonably reflect the actual expenses incurred by the applicable employees.

AUDITEE'S RESPONSE

A. Controls currently in place to monitor fuel usage are sufficient and effective. Fuel usage logs are reviewed for reasonableness and accuracy by fleet management personnel. Unusual usage is investigated and corrected if necessary. Individual usage logs by vehicle would be cumbersome and time consuming, incurring significant additional costs. However, as recommended by the State Auditors, CU will consider a more detailed reconciliation regarding fuel totals.

B. "Take home" use of vehicles for other than emergency first responders, has declined in the past two years and will continue to do so through attrition. The ability to respond quickly to emergency situations is deemed extremely important in the utility industry. The value of emergency personnel reporting directly to the emergency site with all equipment necessary to shut off utilities is not measurable when the safety of the public is at issue.

C. The vehicle allowance is intended not only for daily driving between various CU locations, but also for any driving on behalf of CU business. This would include trips within driving distance for education, off-site meetings, and legislative issues. The allowance amount is reviewed periodically for reasonableness.

19. Stockton Lake Pump Failure and Preventative Maintenance

The pumps at the Stockton Lake Pumping Station failed in 2005 and 2006, and CU has not fully implemented the recommendations made by a consultant regarding the pump station failures. Formal preventative maintenance plans for CU's telecommunications system, and SpringNet® have not been established to monitor and identify repair or replacement needs which may prevent or limit future system failures.

All three water pumps at the Stockton Lake Pumping Station failed between August 2005 and March 2006. One pump failed due to lightning damage, another due to overheating caused by a blocked water intake line, and the third failed due to problems with the pump's electrical system. CU incurred costs exceeding $1.9 million between April 2006 and April 2007 relating to the pump failures. These costs included the following:

Item	Amount
Temporary pump rental	$ 1,251,810
Pump repair	258,283
Remove/reinstall pumps	216,309
Security during pump rental	127,492
Consultant study	120,357

A. CU has not fully implemented all of the recommendations made by the consultant to help prevent future pump failures at the Stockton Lake Pumping Station. The consultant was paid over $120,000 to study the system failure.

The consultant issued a report in March 2007 containing 13 recommendations to prevent repeating such an event. Some of these recommendations included having preventative maintenance performed every 5 years, establishing an improved documentation of the monthly monitoring to minimize untimely failures, providing a manually cleaned basket strainer in the intake lines, limiting the maximum flow through any one pump to less than 7,000 gallons per minute, and modifying the control system to display the flow rate and pressure data of the Stockton Intake Pump Station at the Fulbright Water Treatment Plant.

To prevent future system failures, CU should consider fully implementing the consultant's recommendations.

B. While formal preventative maintenance plans have been established for CU's electric, natural gas, and water systems, they have not been established for the telecommunications, and SpringNet® systems. Maintenance plans should be developed to monitor and identify repair or replacement needs which may prevent or limit future system failures. In addition, formal maintenance plans would serve as a useful management tool and provide greater input into the overall budgeting process. These plans also provide a means to continually and more effectively monitor each system and evaluate the progress made in the repair, maintenance, and improvement of these systems throughout the year.

WE RECOMMEND the Board of Public Utilities:

A. Take adequate steps to prevent future pump failures and consider fully implementing the recommendations of the consultant's report.

B. Ensure formal preventative maintenance plans are established to prevent or limit future system failures and to provide greater input into the overall budgeting process.

AUDITEE'S RESPONSE

A. *All consultant recommendations are complete or are in progress. The Stockton Lake Pump Station has provided over 25 billion gallons of water to Springfield over the last 10 years and was able to meet source capacity needs.*

B. *CU mirrors the telecommunications, broadband, and data center industries regarding its maintenance approach and plans. CU will evaluate the necessity to document the current maintenance procedures.*

20. Tree and Brush Maintenance

Various utility industry publications have indicated that the lack of tree trimming and brush removal is the number one cause of controllable power outages. Expenditures incurred for tree trimming and brush removal totaled over $1 million and $5.5 million during the year ended September 30, 2006 and period October 1, 2006 through April 24, 2007, respectively. Expenditures increased significantly due to the ice storm that hit CU's service area in January 2007 leaving 75,000 of 106,000 CU customers without power.

Subsequent to the ice storm, the utility conducted a survey and performed an internal study of their performance during the ice storm. Survey results indicated 86 percent of CU customers were in favor of a more aggressive tree trimming program in the CU service area, and the internal study of CU's performance recommended the following improvements relating to tree trimming:

- Maintain or increase public education on planting trees in the right place.
- Consider increasing the minimum trimming distances from electric lines.
- Consider a separate budget item for customer requested trimming service.
- Consider a minimum accepted trimming cycle for CU.

In addition, CU contracts with companies to provide tree trimming and brush removal services, and while a cost benefit study was performed in 2001 to determine whether it was more cost effective to perform tree trimming and brush removal in-house or to outsource, it has not been periodically updated. Also, while CU has a tree trimming management policy, the utility has not developed procedures to measure its performance of this policy. CU's policy indicates trees and shrubs around distribution lines may be trimmed to obtain safe and responsible clearance of not less than 6 feet. Tree limbs which overhang wires shall be removed. Trees growing under distribution lines, which are completely within right-of-way, may be removed if they are of a specie which will interfere with the lines and limbs can not be cut.

To balance safety and electric system reliability and the aesthetic and environmental concerns of customers, CU should take steps to be more proactive in trimming trees, and implement ice storm recommendations in a timely manner. In addition to safety concerns and outage prevention, tree trimming and brush removal is necessary to reduce unexpected costs to the utility (as experienced during the ice storm). The Public Service Commission is in the process of increasing the minimum trimming distance around power lines. An updated formal cost benefit analysis of the costs related to tree trimming would better support the utility's decision-making process, and the utility should establish performance measurement procedures related to tree trimming policies.

WE RECOMMEND the Board of Public Utilities should take a more proactive approach to tree management and implement ice storm recommendations in a timely manner. In addition, periodically update the cost benefit study to ensure the utility is making the most economical decision, and establish performance measurement procedures related to tree trimming policies.

AUDITEE'S RESPONSE

CU is implementing the recommendations of the Disaster Response Action Committee and CU's formal review including:

1. *Increasing the annual tree trimming budget to $2.5 million throughout the five year plan.*

2. *Moving from a "worst – first" system to a cycle based trimming program.*

3. *Increasing the public education campaign.*

4. *Seeking public input regarding changes to the tree trimming policy, including trimming clearances.*

21. Closed Meeting Minutes and Accounting Procedures

Board minutes did not always publicly disclose the final disposition of applicable matters discussed in closed session, and the board did not document how discussing a pay raise for the General Manager complied with state law. Controls and procedures over pole attachments and inventory duties need improvement.

A. The Board of Public Utilities held six closed meetings during the year ended September 30, 2006. The open meeting minutes did not always publicly disclose the final disposition of applicable matters discussed in closed session. The board generally holds the closed session meetings at the end of an open session meeting and does not reconvene in open session to disclose required matters. Section 610.021, RSMo, of the Sunshine Law requires certain matters discussed in closed meetings be made public upon final disposition.

In addition, the board did not document how discussing a $24,795 pay raise for the General Manager complied with state law. To ensure compliance with the provisions of the Sunshine Law, it would be prudent to discuss pay raises in open session.

B. CU does not track all utility pole attachments provided to other electric and telecommunications companies. One company is allowed to attach lines to CU's utility poles, and in turn, the utility is allowed to attach to their poles. While the utility believes there is an even exchange of pole usage, the utility has not tracked the number of attachments used by each party. CU should track the number of pole attachments by each party to ensure the exchange is equitable. CU collected over $259,478 from other pole attachment agreements during the year ended September 30, 2006.

C. Inventory duties are not properly segregated. Storeroom employees responsible for ordering, receiving, and recording inventory are also involved in conducting the physical inventories. To ensure the integrity of perpetual inventory records, physical inventories should be performed by individuals who are independent of custodial and record-keeping functions.

WE RECOMMEND the Board of Public Utilities:

A. Ensure minutes publicly disclose the final disposition of applicable matters discussed in closed session. In addition, the board should ensure closed meetings are conducted according to state law.

B. Track the relative number of pole attachments to ensure the exchange is equitable.

C. Ensure physical inventory counts are performed by individuals who are independent of the custodial and record-keeping functions.

AUDITEE'S RESPONSE

A. City Utilities will continue to follow the requirements of the Sunshine Law regarding minutes of both open and closed meeting decisions.

B. A utility services contractor hired to assess CU's poles completed their field assessment, including an inventory of pole attachments, in September 2007. This assessment provides the information necessary to ensure that the exchanges with other utilities are equitable.

C. CU considers current inventory controls to be efficient and effective. Physical counts are completed by materials management staff; however, these are blind counts, meaning the person performing the count has no knowledge of the expected units when counting. Additionally, once the counts are entered into the system, the variance report is sent directly to the supervisor for variance analysis and determination of any recounts needed. The supervisors who make the adjustments to the inventory are not doing the *physical counts of inventory. Reports of the cycle counts are sent to management and internal auditing, who review the adjustments made and investigate the reasons.*

HISTORY, ORGANIZATION, AND STATISTICAL INFORMATION

CITY UTILITIES OF SPRINGFIELD, MISSOURI
HISTORY, ORGANIZATION, AND
STATISTICAL INFORMATION

City Utilities of Springfield (CU) is a component unit of the City of Springfield, Missouri, and is responsible for the generation, transmission, and distribution of electric power; the acquisition, transportation, and distribution of natural gas; the acquisition, treatment, and distribution of water; and the operation of the bus transportation system. Telecommunications services are provided internally and as an external business unit operated under the SpringNet® trademark.

The CU service territory covers approximately 320 square miles, which includes all of the City of Springfield, portions of Greene County, and a part of northern Christian County. At September 30, 2006, CU served approximately 105,000 electric, 82,000 natural gas, and 79,000 water customers in the Springfield metropolitan area. City Utilities employed approximately 966 employees at September 30, 2006 of which 589 were union employees.

City Utilities is a publicly-owned utility, governed by an eleven-member Board of Public Utilities, nine who are customers inside the city limits and two outside. Board members are appointed by the City Council for three-year terms and serve without compensation. The Board normally meets on the last Thursday of each month. The Board makes policy decisions for CU and appoints the General Manager, who is the Chief Executive Officer. Members of the board and the positions held during the year ended September 30, 2006 were:

Utility Board	Dates of Service During the Year Ended September 30, 2006
Ronald Reynaud, Chairman	October 2005-September 2006
Virginia Fry, Vice Chairman	October 2005-September 2006
Phil Wannenmacher, Secretary	October 2005-September 2006
Mark McNay, Assistant Secretary	December 2005-September 2006
Dan Manna, Assistant Secretary	October 2005-November 2005
Geoffrey Butler (1)	October 2005-September 2006
Thomas Finnie (2)	September 2006
Fred Marty	October 2005-March 2006
Lisa Officer	December 2005-September 2006
Susan Kirkman	October 2005-November 2005
Patrick Platter	December 2005-September 2006
Larry Pennel	October 2005-November 2005
Ronald Ponds (3)	October 2005-September 2006
Debbie Shantz (4)	October 2005-September 2006
Don Thomson	October 2005-September 2006

(1) Geoffrey Butler was replaced by Mike Chiles in February 2007.
(2) Position remained vacant from April until September 2006.
(3) Ronald Ponds was replaced by David Jones in February 2007.

(4) Debbie Shantz was replaced by Todd Parnell in February 2007. Todd Parnell resigned in August 2007 and the position remains vacant.

The utility's other principal officials during the year ended September 30, 2006, are identified below. The compensation of these officials is established by the Board of Public Utilities.

Other Officials	Dates of Service During the Year Ended September 30, 2006		Compensation Paid for the Year Ended September 30, 2006
John Twitty, General Manager (2)	October 2005-September 2006	$	334,395
Associate General Managers :			
Andy Dalton, General Counsel (2)	October 2005-September 2006		211,019
Bill Burks, Chief Operating Officer (1),(2)	October 2005-January 2006		276,491
Scott Miller, Electric Supply (2)	October 2005-September 2006		194,251
Wade Stinson, Operations (2)	October 2005-September 2006		197,048
Karl Plumpe, Economic Development (2)	October 2005-September 2006		180,449
Jim Shuler, Chief Financial Officer	October 2005-September 2006		153,806
Robin House, Administration	October 2005-September 2006		150,814
Brenda Putman, Chief Internal Auditor	October 2005-September 2006		124,359
Directors:			
David Fraley, Environmental Affairs	October 2005-September 2006		127,568
Kyle McClure, Public Policy/ Government Relations	October 2005-September 2006		89,8778
Janet Hudson, Treasury	October 2005-September 2006		129,749
Jack Hadsall, Risk & Security Management	October 2005-September 2006		140,213
Ray Ross, Pricing	October 2005-September 2006		124,694
Max Ellis, Financial Technology	October 2005-September 2006		117,281
Cheryl Hamlin, Benchmarking/Utility Information	October 2005-September 2006		102,907
Mark Viguet, Marketing/ Communications	October 2005-September 2006		130,737
Melissa Turner, Human Resources	October 2005-September 2006		122,686
Amy Austin, Customer Services	October 2005-September 2006		115,879
Kathleen Fritts, Information Technology	October 2005-September 2006		144,974

Kenneth Reasoner, Operations Analysis	October 2005-September 2006	103,084
Mike Moore, Telecom	October 2005-September 2006	143,470
Todd Murren, SpringNet®	October 2005-September 2006	139,731
Gary Gibson, Distribution (2)	October 2005-September 2006	134,470
James Bingham, Management Services	October 2005-September 2006	160,434
Carol Cruise, Transit	October 2005-September 2006	116,220
Cara Shaefer, Energy Management/ Conservation	October 2005-September 2006	74,475
Bryan Feemster, Power Station	October 2005-September 2006	121,975

(1) Bill Burks retired, and CU separated his job duties and created two associate general manager positions which were filled by Scott Miller and Wade Stinson. This salary amount includes a payout of benefits at retirement for vacation and sick leave of $166,153.

(2) Includes a car allowance of $659.25 per month ($7,911 total) for October 2005 to September 2006.

Historical Operating Statistics of the City Utilities of Springfield are noted below:

		Year Ending September 30, 2006	2005
Sales			
Electric-thousand kilowatt hours		3,813,932	3,745,066
Natural Gas-dekatherms		11,760,255	11,974,091
Water-thousand gallons		10,031,354	9,992,904
Revenue Bus Passengers Carried		1,708,824	1,470,356
Number of Customers			
Electric		104,853	102,353
Natural Gas		81,610	80,489
Water		78,943	77,521
Residential Customer Data (average per customer)			
Electric:			
Annual Electric Bill	$	746.28	660.10
Kilowatt Hours Used		11,227	11,000
Revenue per Kilowatt Hour	$	.0665	.0600
Natural Gas:			
Annual Natural Gas Bill	$	826.47	694.96
Dekatherms Used		67	75
Revenue per Dekatherm	$	12.34	9.27

Water:			
Annual Water Bill	$	253.84	247.58
Thousand Gallons Used		72	72
Revenue per Thousand Gallons	$	3.53	3.44
Miscellaneous Statistics:			
Maximum Hourly Peak Demand (electric)-megawats		801	760
Maximum Day Purchase (natural gas)-dekatherms		102,221	106,518
Maximum Day Pumpage (water)-thousand gallons		51,570	51,791
Total Annual Pumpage (water)-thousand gallons		12,276	12,259
Electric Line-miles		1,951	1,924
Natural Gas Main-miles		1,280	1,266
Water Main-miles		1,154	1,143
Number of Fire Hydrants		7,526	7,413
Number of Streetlights		19,371	19,087