APPENDIX 1

Review of The Management of the City’s Divisional Accounts Receivable

February 13, 2012

Auditor General’s Office

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Auditor General
City of Toronto
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EXECUTIVE SUMMARY

**Review of City Service related receivables included in 2011 Work Plan**

The Auditor General’s 2011 Work Plan included a review of the management and administration of City divisional accounts receivable. The objective of this review was to assess divisional practices for billing and collecting service related revenue owed the City for services provided to customers. Examples of divisional service related accounts receivable include recreational program registration fees, park facility rentals, rent for property administered by Facilities Management and street and road allowance fees collected by Transportation Services. The audit did not include the management of property tax and water billing receivables.

**Accounts receivable invoices totaling $1.6 billion issued in 2010**

In 2010, of the City’s $5.2 billion in general revenue, the City issued invoices of $1.6 billion. The $5.2 billion does not include property tax or water billings. The 2011 and 2010 year end accounts receivable balances excluding property tax and water billing were approximately $332 million and $344 million respectively.

The City’s accounts receivable balance is comprised of a number of different receivable types. In addition to accounts receivable where a customer is billed and payment is due within a specified number of days, the City accounts receivable balance includes long term loans, receivables related to agreements between the City and the City’s Agencies, Boards, Commissions and Corporations, receivables in the form of subsidies from other government organizations and receivables relating to parking tag fees and court services.

Table 1 is an analysis of accounts receivable at December 31, 2011 and December 31, 2010.
Table 1:

2011 and 2010 Accounts Receivable Balances at December 31

<table>
<thead>
<tr>
<th>Receivable Type</th>
<th>2011 $$$ (millions)</th>
<th>2010 $$$ (millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agencies Boards, Commissions &amp; Corporations</td>
<td>139.3</td>
<td>111.4</td>
</tr>
<tr>
<td>Long Term Loans</td>
<td>62.5</td>
<td>60.7</td>
</tr>
<tr>
<td>Parking Tags</td>
<td>43.6</td>
<td>43.0</td>
</tr>
<tr>
<td><strong>Service Related</strong></td>
<td><strong>51.4</strong></td>
<td><strong>39.6</strong></td>
</tr>
<tr>
<td>Other Municipalities</td>
<td>9.8</td>
<td>36.9</td>
</tr>
<tr>
<td>Court Services</td>
<td>33.7</td>
<td>33.7</td>
</tr>
<tr>
<td>Government Agencies – Federal</td>
<td>12.6</td>
<td>32.6</td>
</tr>
<tr>
<td>Government Agencies – Local</td>
<td>7.6</td>
<td>6.4</td>
</tr>
<tr>
<td>Customer Credit Balances</td>
<td>-3.6</td>
<td>-3.5</td>
</tr>
<tr>
<td>Government Agencies – Provincial</td>
<td>-24.2</td>
<td>-16.2</td>
</tr>
<tr>
<td><strong>Total Outstanding</strong></td>
<td><strong>$332.7</strong></td>
<td><strong>$344.6</strong></td>
</tr>
</tbody>
</table>

*Over $332 million in accounts receivables outstanding at the end of 2011*

This review focused on the management and administration of the $51.4 million in accounts receivable shown in the table as “Service Related.” Service related receivables are billings for City services such as recreation program registration fees and use of park facilities, rent due on City property and street and road allowance fees.

Table 2 provides a divisional breakdown of service related accounts receivable at December 31, 2011 and December 31, 2010.

*Review focused on approximately $51 million in service related receivables*
Table 2
Service Related Accounts Receivable
2010 and 2011 Year End Balances

<table>
<thead>
<tr>
<th>Service Description</th>
<th>2011 ($000)</th>
<th>2010 ($000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Children’s Services, Homes For The Aged &amp; Social Development</td>
<td>832</td>
<td>726</td>
</tr>
<tr>
<td>Parks Program Registration</td>
<td>2,287</td>
<td>2,859</td>
</tr>
<tr>
<td>Parks Other Services &amp; Programs</td>
<td>7,505</td>
<td>7,790</td>
</tr>
<tr>
<td>Emergency Medical Services</td>
<td>100</td>
<td>189</td>
</tr>
<tr>
<td>Public Health</td>
<td>74</td>
<td>67</td>
</tr>
<tr>
<td>Municipal Licensing &amp; Standards</td>
<td>4,226</td>
<td>4,098</td>
</tr>
<tr>
<td>Fire</td>
<td>2,287</td>
<td>2,810</td>
</tr>
<tr>
<td>Transportation</td>
<td>14,978</td>
<td>8,897</td>
</tr>
<tr>
<td>Solid Waste Management</td>
<td>5,368</td>
<td>3,936</td>
</tr>
<tr>
<td>Water Pollution</td>
<td>2,808</td>
<td>2,671</td>
</tr>
<tr>
<td>Water Services</td>
<td>872</td>
<td>1,044</td>
</tr>
<tr>
<td>Technical Services</td>
<td>926</td>
<td>547</td>
</tr>
<tr>
<td>Facilities &amp; Real Estate</td>
<td>8,477</td>
<td>2,901</td>
</tr>
<tr>
<td>Other Corporate Divisions</td>
<td>181</td>
<td>135</td>
</tr>
<tr>
<td>Accounting/Other Divisions</td>
<td>448</td>
<td>919</td>
</tr>
<tr>
<td><strong>TOTAL OUTSTANDING</strong></td>
<td><strong>$51,369</strong></td>
<td><strong>$39,589</strong></td>
</tr>
</tbody>
</table>

**Key Issues**

This report identifies five areas where the management and administration of divisional accounts receivable can be strengthened. The five areas are as follows:

1. **Improve Control and Oversight Over Accounts Receivable**

   There is currently no single point of authority to ensure a City-wide program exists to consistently manage accounts receivable. A single point of authority would assist in ensuring accounts receivable are managed consistently throughout the City.

   Many of the areas addressed in this report would be improved by aligning divisional procedures with existing City-wide policies and practices.

2. **Compliance With City Accounts Receivable Policies and Procedures Needs Improvement**

   The Accounting Services Division needs to monitor compliance with established policies and procedures at the divisional level.
Of the $51 million outstanding, $12.3 million has been outstanding for over one year.

(3) City and Divisional Financial Management Systems Do Not Provide Adequate Information to Monitor Collection Efforts

The City’s financial management system and divisional accounting systems do not provide adequate information to monitor accounts receivable collection activity. Customer collection rates and payment timeliness information are not collected and analyzed. Of the total service related accounts receivable of $51 million, approximately $12.3 million has been outstanding for over one year.

(4) Accounts Receivable Policies, Practices and Procedures Need to Be Strengthened

Managerial, supervisory and staff responsibilities are not clearly documented and followed. For example, there is little evidence of consistent management guidance, oversight and routine supervisory review over the accounts receivable collection activity.

(5) System Access Controls Should Be Strengthened

Periodic review of user access is not conducted

Periodic review of user access is required. Broad access privileges granted to accounts receivable system users increases the risk of unauthorized or fraudulent activity.

300 users have access to the accounts receivable module

Approximately 300 users have access to the City’s accounts receivable module. Included in the 300 users are nine individuals with the ability to create customer accounts, generate invoices, process payments and approve transactions.

Implementation of the eight recommendations in this report will result in improved accounts receivable collection efforts, operational efficiencies and internal controls.
AUDIT OBJECTIVES, SCOPE AND METHODOLOGY

The Auditor General’s 2011 Audit Work Plan included an audit of the management and administration of accounts receivable. The audit objective was to assess divisional practices for billing and collecting revenue owed the City.

Why we conducted the review

The audit was included in the work plan because of the significant value of accounts receivable in relation to the City’s general revenue. Accounts receivable is a City-wide function affecting many divisions and exposes the City to a certain level of financial risk.

Audit objectives

Specific audit objectives included:

- Determining the effectiveness of oversight provided by the Accounting Services Division
- Determining the adequacy of management and control of current and outstanding receivables
- Determining whether the management of City accounts receivable is in accordance with applicable legislation, City by-laws, policies, procedures and generally accepted industry practices.

Previous Auditor General reports on revenue control

The Auditor General has conducted a number of reviews over City revenue and receivables over the past number of years. These reviews were conducted as part of a series of continuous audits over City revenue streams. The reviews listed below are a sample of reports issued:

- Toronto Police Service, Parking Enforcement Review (2011)
- Parks, Forestry and Recreation Division - Concession Agreements Review (2011)
• Parks Forestry and Recreation Division – Controls over Ferry Services Revenue Need Strengthening (2010)

• Controls Over Parking Tags Needs Strengthening (2010)


• Fines and Income Review - Toronto Public Library (2006)
  http://www.toronto.ca/audit/2006/fines_income_review_final_may2006.pdf

• Review of the Administration of Leases on City-owned Property (2006)


• Cash Controls Follow-up Review - Toronto Zoo (2004)

**Audit Scope**

The audit reviewed outstanding accounts receivable as of December 31, 2011.
**Audit methodology**

Our audit methodology included the following:

- review of City Council minutes and reports;
- review of documents, management reports, policies, procedures and related records
- review of internal control reports by external consultants and internal audit staff
- interviews with City staff
- examination of documents and records
- evaluation of management controls and practices
- review of reports issued by other jurisdictions in North America
- other procedures deemed appropriate.

**Compliance with generally accepted government auditing standards**

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence that provides a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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**BACKGROUND**

**City has decentralized billing and collection**

Due to the broad range of services provided by the City, many divisions manage and administer their respective accounts receivable. Multiple independent management information systems such as the CLASS registration system used by the Parks, Forestry and Recreation Division and the Street Allowance Renewal System used by the Transportation Division are used to process customer billings. The SAP Financial System consolidates accounts receivable on a City-wide basis.
City spends $4 million annually on accounts receivable activity

In 2010, the City issued approximately 139,000 accounts receivable invoices. Staff resources dedicated to City accounts receivable are approximately 48 full time equivalent positions at an annual cost of over $4 million.

Legal Services Division pursues accounts receivable when necessary

In some situations, the Legal Services Division assists in pursuing outstanding accounts receivable by initiating legal action where appropriate, or settling legal action where warranted. Legal Services also assists in collection proceedings to enforce judgements where necessary and recommend write-off of amounts deemed uncollectible.

Two collection agencies used

Where traditional collection methods fail the City maintains contracts with two collection agencies. There is no cost to the City unless the collection agency is successful in its efforts. Collection agencies receive 25 per cent of the amount collected.

The City provides each collection agency six months to pursue an account. If collection efforts are unsuccessful after six months the account is transferred to the other collection agency for a further six month period before being transferred back to the City where in most cases the receivables are written off.

Bad debts and write-offs

City by-laws specify that the Treasurer is authorized to write-off outstanding amounts owing to the City up to $50,000. Table 3 provides accounts receivable write-off activity from 2006 to 2010.

Table 3:

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount of Debt Write-Off ($000s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>$1,100</td>
</tr>
<tr>
<td>2007</td>
<td>2,400</td>
</tr>
<tr>
<td>2008</td>
<td>1,100</td>
</tr>
<tr>
<td>2009</td>
<td>684</td>
</tr>
<tr>
<td>2010</td>
<td>257</td>
</tr>
<tr>
<td>5 year total</td>
<td>$5,541</td>
</tr>
</tbody>
</table>
AUDIT RESULTS

CONTROL AND ACCOUNTABILITY

Oversight of the City’s Accounts Receivable Function

No single point of authority to manage accounts receivable

There is no single point of authority to ensure the City-wide accounts receivable function operates effectively, efficiently and within a framework that ensures consistent practice and control. Opportunities exist to improve efficiencies and cost-effectiveness in administering City accounts receivable. These opportunities include the need to:

- improve the integration of collection activities between the Accounting Services Division and other divisions involved in the billing and collection of accounts receivable
- ensure that all collection policies and procedures throughout the City are applied in a consistent manner and followed by divisions
- maximize the use of the City’s SAP financial system to provide management information and reduce reliance on stand-alone reports such as Excel spreadsheets
- develop and implement performance measures.

Consistent practices and standards should be followed by City divisions and Accounting Services

City divisions and the Accounting Services Division should follow the same basic practices and standards. Exceptions to these standards should follow a generally accepted review and approval process. Steps should be taken to ensure accounts receivable managed by all divisions are consistent with one City-wide accounts receivable framework.

Finally, as part of the ongoing shared services review, opportunities should be explored with all Agencies, Boards, Commissions and Corporations with a view to consolidating where appropriate, policies, procedures and collection activities.
Recommendation:

1. City Council request the City Manager to review the current management of all City-wide receivables. Such a process should be a part of the ongoing shared service review. The review should include an evaluation of centralizing the collection efforts of all outstanding receivables.

Accounts Receivable Policies and Procedures

Policies and procedures established in 2006

In 2006, City Council approved accounts receivable policies and procedures. These policies and procedures prescribe steps and processes to be followed by City divisions when extending customer credit and for following up on the collection of outstanding amounts owed the City.

Since these policies and procedures are now over six years old, they should be reviewed and updated where appropriate.

Non-compliance with Council approved policies and procedures

Our review identified non-compliance with a number of checks and balances provided for in the accounts receivable policies and procedures. For example:

- A number of required reports and listings are not submitted quarterly for review by the Accounting Services Division
- Regular customer account reviews are not undertaken
- Payment plan reports are not prepared quarterly for review by senior management
- Credit check protocols are not always followed
- Record retention requirements are not followed.

Staff should be directed to comply with established accounts receivable policies and procedures.

Recommendation:

2. City Council direct the Treasurer to review and update accounts receivable policies and procedures where appropriate. A directive should also be issued to all staff responsible for the collection of receivables that all such policies and procedures should be complied with.
### Need for More Effective Use of the City’s SAP Financial System

<table>
<thead>
<tr>
<th><strong>Opportunities to better utilize SAP in monitoring collection efforts</strong></th>
<th>Opportunities to more fully utilize the SAP financial system to monitor the effectiveness of City collection efforts and improving operational efficiency should be reviewed.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The City’s SAP financial system produces an Aged Receivables Report. This report is used by management to measure collection activity. The report provides details for each customer account including how long the amount has been outstanding.</strong></td>
<td>The City is not consistently utilizing further reporting features in the SAP financial system that have the capacity to assist management in measuring and monitoring accounts receivable activity.</td>
</tr>
<tr>
<td><strong>Over 40 per cent of accounts on the aged accounts report are loans outstanding</strong></td>
<td>Over 40 per cent of Accounting Services Division customer accounts on the aged report were for loans outstanding. Loans are generally more long term in nature and as such are usually recorded separately from accounts receivable.</td>
</tr>
<tr>
<td><strong>The SAP financial system classifies the length of time a particular amount has been outstanding based on the billing date or for loans, the loan origination date. The Aged Receivables Report shows these long term loans as overdue when in fact payments may have been made in accordance with the loan repayment schedule.</strong></td>
<td>This misleading information reduces the usefulness of the report. Without manual intervention an accurate accounts receivable outstanding amount is not reflected on the Aged Receivables Report.</td>
</tr>
<tr>
<td><strong>City participates in OMBI to measure against other municipalities</strong></td>
<td>Each year the City participates in the Ontario Municipal Benchmarking Initiative (OMBI). This initiative provides a forum for comparing operational results with other municipalities and requires the compilation of selected City data related to accounts receivable.</td>
</tr>
</tbody>
</table>
Although the required data is available in the financial system the process requires several extraction routines and manipulation. Some examples of information provided to OMBI include:

- Per cent of all revenues billed
- Per cent of billed revenue written off
- Cost to process and collect one invoice
- Average collection period for one invoice
- Per cent of billings over 90 days

**Performance measures should be used to routinely measure internal performance**

Performance measures such as those provided to OMBI can be useful to management in measuring divisional performance against internal benchmarks. This internal practice is currently not taking place on a routine basis.

Management should review how data from the SAP financial system can be used more effectively to manage and monitor accounts receivable collection results on a regular basis while minimizing manual intervention.

**Recommendation:**

3. City Council request the Treasurer to review current SAP management reports pertaining to the management of receivables. The reports should contain relevant and current information and include performance management information.

**Improve Documentation on Accounts Receivable Follow Up Activity**

Various levels of staff are involved in administering accounts receivable. Typically, in best practice circumstances, staff perform daily follow up activity on accounts receivable. Supervisors review staff activity and account status and management oversees activities by providing direction and required authorizations.
Management reporting process of long outstanding amounts needs to be formalized

There are no criteria prescribing conditions and circumstances required to escalate an account to a higher level for management review and direction. A formal reporting methodology is also not in place providing management with information regarding accounts with long outstanding amounts and where no recent activity has occurred. Consequently, customer accounts are not always administered in a timely manner.

There are a number of customer accounts where amounts have been outstanding since prior to 2009. In some instances we were unable to determine if recent follow up activity has occurred as follow up actions are not always documented.

Evidence of recent follow up activity was not available for seven accounts with a total outstanding amount of approximately $1.2 million.

Regular review of accounts receivable needed

Routine management review and oversight of accounts receivable is required in order to maximize collection opportunities. Management review of collection activities should be timely, diligent and documented.

Recommendation:

4. City Council request the Treasurer to implement an accounts receivable process that provides for timely management review of collection activity and disposition of accounts receivable. Such process to include appropriate documentation and approval requirements.

Customer Accounts With Nominal Amounts

Number of customer accounts with nominal balances

An aged analysis report produced by the SAP Financial System is used to monitor customer account receivable balances. According to the aged analysis report there are a number of accounts where a nominal amount has been outstanding for over two years.

Accounts receivable aged report contains numerous accounts less than $500

At the end of 2011, the aged report contained over 3,600 customer accounts of which 148 of the total number of customer accounts had an outstanding amount or credit balance of less than $500. There has been no activity over the last two and a half years for these accounts.
Removing inactive and nominal balance accounts where collection efforts have been exhausted will provide an aged report that provides more meaningful information for management.

**Recommendation:**

5. City Council request the Treasurer to periodically review inactive customer accounts with small balances where collection efforts have been exhausted and such accounts be written off in accordance with City bylaws.

### MONITORING COLLECTION ACTIVITY

**Lack of Supervisory Review and Documentation**

**Little evidence of supervisory review**

Routine supervisory review provides assurance that staff are taking appropriate and timely steps to collect receivables, reduce receivable write-offs and minimizing accounts with long outstanding balances. Routine supervisory review of accounts receivable is not taking place. On occasions when supervisory review occurs it is not effective.

**Number of old items with no current collection activity**

Accounts receivable status reports prepared by staff include old items which should have been written off by now or at a minimum include an explanation of why the account remains outstanding. For example, the “Sundry” and “Miscellaneous” customer accounts have a number of items totalling $471,000 and $814,900 respectively that have been outstanding for more than 150 days. There is no evidence of supervisory review or action taken on these items.

More effective supervisory review and documentation will ensure collection activity is conducted in a timely manner.

**Recommendation:**

6. City Council request the Treasurer to clarify and document the roles and responsibilities of supervisory staff and accounts receivable staff to ensure due diligence in collection activities. Staff roles and responsibilities should include collection activity, supervisory review and documentation requirements.
**Monitoring of Accounts Involving Legal Action**

<table>
<thead>
<tr>
<th>140 customer accounts totaling $8.6 million with Legal Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>At the time of our review, 140 customer accounts totaling $8.6 million in outstanding receivables were with the Legal Services Division. Of the total 140 accounts with Legal Services, 44 were transferred to the Legal Services Division in 2009 or prior.</td>
</tr>
</tbody>
</table>

**Difficulties in determining account status**

A number of reports are used to monitor the status of accounts with Legal Services. However, determining the account status from these reports is difficult. For example:

- the account status does not include an “as of date” making it difficult to impossible to determine at what point in time status is being reported
- the report includes items for which Legal Services had closed the file
- the report includes items previously closed in the SAP financial system
- multiple lists exist with inconsistent data rather than one single master list resulting in confusion regarding information accuracy
- the data is not always complete.

**Reports do not include planned actions**

In addition, reports do not include expected dates for planned actions. In many instances, reports do not indicate planned or current activity.

**Current reports provide limited value**

Other than providing limited history on customer accounts, reports generated provide limited value.

**Recommendation:**

7. **City Council request the Treasurer to assess the feasibility of using the City SAP Financial System to the fullest extent in tracking actions taken on customer accounts sent to Legal Services and collection agencies.**
SYSTEM ACCESS CONTROLS SHOULD BE STRENGTHENED

Separation of Duties

*Periodic reviews of user access not conducted*

Separation of duties is an important control in reducing the risk of unauthorized transactions.

Approximately 300 users have access to the City’s accounts receivable module. Included in the 300 users with access are nine individuals with the ability to create customer accounts, generate invoices, process payments and approve transactions.

Broad access privileges granted to accounts receivable module users increases the risk of unauthorized or fraudulent activity. Limited access should be granted to employees requiring current access as a part of their regular duties.

*Periodic Review of User Access*

In addition, once users are granted access to the SAP accounts receivable module they have access for an indefinite period of time. Periodic review of user access to the accounts receivable module is not conducted.

Generally accepted industry practices recommend periodic review of user access to information systems. Periodic review of user access reduces the risk of unauthorized activity by ensuring only individuals requiring access to the accounts receivable system can gain access.

**Recommendation:**

8. City Council request the Treasurer take steps to ensure the proper separation of duties by limiting access to users of the SAP accounts receivable functions. In addition, user access should be reviewed periodically to ensure only those with a current and regular need are authorized to use the system.
CONCLUSION

This report presents the results of our review of City policies and practices to ensure controls over City Divisional accounts receivable are adequate.

Implementing the eight recommendations included in this report will strengthen controls, improve efficiency and accountability, and should result in increased revenues and potential cost savings.