



21-06

INTERNAL AUDIT REPORT

Damage Recovery Billing Process

FEBRUARY 2022

City of Sioux Falls Internal Audit Department
Carnegie Town Hall | 235 West 10th Street
Sioux Falls, SD 57117-7402
siouxfalls.org/council/internal-audit

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Introduction

The Damage Recovery Billing Process Audit was included as a carry-over assurance audit on the 2020 Annual Audit Plan. The purpose of the audit was to review the billing process for damage done to City property for effectiveness and efficiency. Controls are intended to provide reasonable assurance, but cannot guarantee, that fraud & errors will not occur. The audit focuses on substantiation of actual costs and labor for damage claims; procedures for invoicing damage billing claims; coordination/efficiency between City departments related to invoice processing, cost recovery, collections, small claims court and write-offs and controls to prevent fraud, waste and abuse as outlined in the City Billing for Damages to City Property Policy. This audit will not include an in depth review of the collections process, small claims process or fleet related damage claims.

Background

The City of Sioux Falls, as a self-insured entity, seeks reimbursement for property damage losses from third parties (the individual who caused the damage or the individual's insurance company). Recovery of losses (expenditures to repair/replace, including materials and labor) directly impacts City revenue and expense budgets. The pursuit of recovery against third parties responsible for damaging City assets is a decentralized process, not specifically part of the City's self-insurance program under Risk Management. The Finance Department is responsible for the Billing for Damages to City Property Policy as well as the write-off process for outstanding damage billing invoices deemed uncollectible. The City Attorney's Office is responsible for pursuing damage billing claims in small claims court when appropriate.

Departments incur the expense to repair/replace damaged property/assets. Actual invoiced amounts for recovery of damage to City property for 2020 and 2021 is noted in the following table.

Figure 1. Property Damage Billing Invoice Totals

Department	2020 Actual	2021 Actual
Traffic and Streets Lights	\$79,955	\$102,798
Fleet	\$135,653	\$104,454
Streets Maintenance	\$1,500	\$5,506
Parks	\$698	\$4,516
Grand Total	\$217,806	\$217,274

*Hydrant repair invoices were excluded from totals due to the inclusion of non-damaged billing invoices.

Any recovery of funds is recorded as revenue to code 384000 – Damage Recovery Payments. Actual revenue received for recovery of damages to City property for 2020 and 2021 can be seen in the table below.

Figure 2. Damage Revenue Totals

Department	2020 Actual	2021 Actual
Fleet	\$61,741	\$96,523.71
Traffic and Street Lights	\$76,954	\$115,234
Power and Distribution	-	\$17,171
Fire Operations	\$12,424	-
Streets Maintenance	-	\$5,506
Parks	\$698	\$14,427
Public Parking	\$4,785	\$22
Engineering	\$2,774	-
Grand Total	\$159,376	\$248,884

*Hydrant Repair invoices were excluded from totals due to the inclusion of non-damaged billing invoices.

Property damage recovery claims are typically the result of a vehicle accident resulting in damage to a street light, stop sign, fire hydrant, electric box, electric pole, etc. It is important to consider South Dakota Codified Law § 15-2-13 regarding statute of limitations for damage recovery. Any suit for recovery of damages not filed within 6 years may be barred by SDCL § 15-2-13 and as such the efficiency of the claims process is critical to recovering damages.

The damage recovery billing process generally begins with a vehicle accident. For all accidents, a police report is completed with details of the incident. The department responsible for the damaged property is notified via several methods: Metro Communications, SeeClickFix or Risk Management. Metro Communications will notify the department of damages via a phone call, whereas SeeClickFix and Risk Management send email notifications. For the specific case of Risk Management notifications, the Risk Manager will forward the police report to the staff member responsible for invoicing damage claims at the department level. At that point, the department repairs the damages incurred. VueWorks has been implemented to various degrees throughout Public Works, where the majority of damage billing claims occur. For the departments that utilize VueWorks, a work order is created in the system to track the actual labor, materials and equipment used to conduct the repair. Details are also entered in the work order in VueWorks related to the accident and any supporting documentation such as photos, notes and the police report are attached.

If the department does not utilize VueWorks, supporting documentation, including invoices, police reports and notes, are typically scanned into Munis and attached to the corresponding damage billing invoice. There was one department who maintained paper copies of the supporting documentation, including work order information rather than scanning or notating in Munis.

Once the repair work has been completed and all supporting documentation is gathered, the department staff responsible should generate an invoice based on actual labor, materials and equipment. In order to bill the responsible party, a customer number is requested from Finance. The department level staff then create the invoice in Munis and Finance posts the invoice. If the State's Attorney Office is involved, a copy of the invoice is emailed for restitution purposes. The State's Attorney Office is also updated as payments are made.

Statements are automatically generated by Munis and mailed by the department at 30, 60 and 90 days as applicable. Additionally, the department level staff are responsible for contacting the insurance company if payment has not been made after the first notice is mailed. Detailed notes regarding insurance company correspondence, any discussions with the responsible party and payment plans are made in the special conditions/notes section with the invoice in Munis. The department level staff are also responsible for tracking outstanding invoice status. Risk Management is contacted if the insurance company attempts to negotiate or dispute an invoice. At final notice, the City Attorney's Office is contacted to determine if the invoice will be pursued in small claims. Determinations are made on an individual invoice basis whether to pursue in small claims court or send to collections. Small claims invoices are tracked in a master spreadsheet accessible to the department and Finance. AAA Collections is utilized by the City Finance Department for collections typically below \$300. When action is taken related to small claims or collections, notes are updated for the invoice in Munis. Payments for damage billing invoices are made to the Finance PO box. If a payment is mailed to an individual department, Finance is notified and send the check for deposit with notes detailed in Munis. Outstanding damage billing invoices are written off under several circumstances. The specifics of the write-off process were outside the scope of this audit; however, an overview of the process as it relates to damage billing was provided. Once there is some kind of collections activity, the invoice is removed from the current receivables. Additionally, if the amount ordered for restitution is less than the invoiced amount, the payment is applied to the original invoice and the balance is written off. If a payment is received for an invoice with a shortage of up to 5%, it is accepted for settlement of the invoice with the remainder of the invoice written off. Finally, a bad debt write-off list is prepared quarterly for invoices deemed uncollectible. Write-off and collections activity related to an invoice are documented in Munis notes.

Objective

To assess the effectiveness and efficiency of the damage recovery billing process to ensure the City is recovering labor and material costs to repair damages to City assets.

Scope

The audit scope included a review of the current damage recovery billing process, damage recovery invoices, supporting documentation including repair work and labor expenses and policies and procedures as they are currently in place. The detailed testing of transactions covered the twelve-month period of January 1, 2020 through December 31, 2020.

Methodology

To complete this audit, we performed the following steps:

- Obtained an understanding of the Billing for Damages to City Property Policy, City Billing, Cash Receipts and Collections Policy and South Dakota Codified Laws § 15-2-13 regarding statute of limitations for damage recovery.
- Interviewed Risk Management regarding their role in the damage recovery billing process and City Attorney's Office staff handling small claims processing for outstanding damage billing invoices.
- Conducted site visits with department staff responsible for creating/processing damage billing invoices to observe the process and software utilized.
- Reviewed other municipal damage billing policies and procedures.
- Reviewed a sample of damage billing invoices to determine if all actual costs were invoiced, if sufficient documentation was maintained to support the invoices, if statements were generated according to City Policy, if insurance company and City Attorney's Office were contacted at appropriate times and if all required write-off documentation was included when applicable.
- Performed an analytic review of number of invoices billed, paid, written off and with an outstanding balance.
- Performed an analytic review of the timeline between incident, invoice date, payment date and write-off date for the sampled invoices.

Efficiency of Damage Recovery Billing Process

Over the two-year period of calendar year 2020 and 2021, approximately 386 invoices were billed related to damages to City property (excluding invoices for hydrant repair). Of those 386 invoices, 271 were paid as of March 3, 2022. A cost recovery ratio of 65% was calculated by dividing the total payments received by the total invoices billed. Additionally, the percentage of invoices outstanding was calculated at 22% by taking the total outstanding balance as of March 3, 2022 and dividing it by the total amount of invoices billed. Calculating these ratios can provide a measurable benchmark to monitor the efficiency of the damage recovery billing process over time.

The table below provides a summary of property damage claims invoices in 2020 and 2021.

Figure 3. Summary of Property Damage Claims

	# of Invoices	Amount
Invoices Billed January 1, 2020 through December 31, 2021	386	\$1,049,220
Invoices Paid	271	\$(678,599)
Write offs to Collections, Bad Debts and Settlements	22	\$(136,639)
Invoices with a balance outstanding as of March 3, 2022	115	\$233,982
Cost Recovery Ratio		65%
Percentage of Invoices Outstanding		22%

*Source: Analysis performed by Internal Audit on data provided by Finance Department staff.

*Hydrant Repair invoices were excluded from these totals since they include non-damage billing invoices.

*Cost Recovery Ratio = Payments Received/Invoices Billed

*Percentage of Invoices Outstanding = Outstanding Balance as of March 3, 2022/Invoices Billed

To determine the efficiency of the damage billing process, the timeline between different steps of the process was analyzed, including the incident date, invoice date, payment date and write-off date if applicable. A statistical sample of 25 damage claims paid or written off during the audit scope of January 1, 2020 through December 31, 2020 was selected. For this sample, damage claims were invoiced on average approximately one month after the incident date, or 32.11 days. There was one outlier in the sample in which 294 days passed between the incident date and invoice date. With this single outlier removed, the average number of days between incident date and invoice date is only 17.56 days. The average number of days between invoice date and payment date was 24.77 days. This would be considered an efficient standard as most payments were received prior to the first statement even being generated. For the invoices written-off in the sample, an average of 699.50 days passed between invoice date and write-off date. See table below for a summary of the average days calculated in the sample.

Figure 4. Average Days for Invoicing

Average # of days between incident date and invoice date	32.1
Average # of days between invoice date and payment date	24.8
Average # of days between invoice date and write-off date	699.5
Average # of days between incident date and invoice date (outlier removed)	17.6

*Source: Statistical sample of 25 damage invoice claims paid or written-off between January 1, 2020 and December 31, 2020.

Overall, the average initial invoicing timeframe and average payment dates were found to be efficient at 32.11 days and 24.77 days respectively. However, the average number of days between invoice date and write-off date was 699.50 days, nearly two years. A detailed analysis of the write-off process is outside the scope of this audit; however, the probability of collection decreases significantly after the first six months. A standardized procedure for write-offs to minimize that timeframe would be beneficial, understanding that claims pursued in court take additional time to settle than those processed by the collection agency.

See Opportunity 1.

Damage to City Property Policy Implementation

In addition to the statistical sample of 25 damage claims analyzed for efficiency, the same sample of invoices was evaluated for compliance with the Damages to City Property Policy. Detailed testing was conducted on the sample to verify:

- supporting documentation for all actual costs,
- documentation to support the determination of the responsible party,
- documentation of payments,
- generation of statements,
- documentation of insurance company communication,
- collections or small claims activity and
- write-off documentation if applicable.

There were seven instances in which a work order number was not included on the invoice or in the attachments in Munis. Additional research was conducted to locate work order numbers or invoices and all actual costs could be substantiated. It is now practice for the work order number to be included with the Munis documentation on the invoice or attachments. There were two instances from older invoices which had been written off that work order numbers could not be located; however, invoices were located and all costs were substantiated.

Prior to the implementation of VueWorks, Public Works departments utilized Munis for work orders. Most departments have since transitioned to include all the necessary documentation in VueWorks with appropriate notes to correspond in Munis.

Overall, proper documentation was included to substantiate expenses, verify work orders and police reports, document correspondence with the City Attorney's Office and insurance agencies and verify write-off documentation when applicable in the sample tested.

The following audit findings were noted:

Finding 1:

Materials invoiced with an overhead charge in one City department

Damage billing claims are being invoiced with a 15% overhead on materials billed in addition to the actual costs incurred in one City department, not in compliance with the Billing for Damages to City Property Policy. It was determined through preliminary survey in the form of an in-person observation and interview that the Water Department damage claims are invoiced by adding 15% upcharge to the actual materials total to cover overhead costs in addition to the actuals from the VueWorks work order. The Billing for Damages to City Property Policy states that "Actual costs and invoices will be obtained. Department or Finance invoices the full amount of damages to the person responsible..." The staff responsible for damage claim invoicing is not aware of the requirement to bill only for actuals outlined in the City Policy. The department handles only a minimal amount of damage invoice claims annually, primarily related to water hydrant repair. In 2020, \$15,668 was billed for hydrant repair and in 2021 the total was \$26,273. It should be noted the total billed amounts for hydrant repair include both repairs for damages to city property and also regular repairs unrelated to accidents or damage. The consequence of invoicing for more than the actual costs incurred creates a potentially inequitable standard. It is best practice to implement the City policy requirements consistently across all departments. **See Recommendations 1 and 2.**

Finding 2:

Estimated labor rates utilized for invoicing in one City Department

In one City department, damage billing claims are currently invoiced utilizing an estimated \$25 hourly rate for all labor rather than the standard actual costs outlined in the City Billing for Damages to City Property Policy. It was determined through preliminary survey in the form of email correspondence, that Parking Department related damage claims are invoiced using a flat \$25 estimated hourly rate for all damage claims. The Billing for Damages to City Property Policy states that "Actual costs and invoices will be obtained. Department or Finance invoices the full amount of damages to the person responsible..." Staff responsible for damage claim invoicing are not creating invoices according to the City Policy in place because they are unaware of the requirements of the Policy. It should be noted that the Parking Department handles a very limited amount of damage billing claims each year. Between 2020 and 2021, only \$4,807 was received in revenue for the Parking Department related to damage recovery billing.

The consequence of invoicing for a flat estimated labor hourly rate is the potential that the City will not recover the full amount of labor required to repair damage. Additionally, there is a slight risk that individuals who damage City property and are invoiced using this method could pay more than the actual cost to repair the damage if an individual with a lower rate was utilized to perform the repair. This also creates inconsistency across the City when different standards for labor rates are applied to the same type of damage recovery billing invoices. **See Recommendations 1 and 2.**

Procedural Internal Controls

Because damage recovery claims are typically the result of an accident or incident, each one presents a unique situation for the individual processing the claim. There are multiple different avenues a department can be notified of the damage and also several different software available at the department level to handle work orders or asset documentation. Currently, no formal administrative procedures exist that are tailored to the software each department has available. The current City policy is too vague to allow for consistent implementation without the addition of detailed, formal administrative procedures to support the City policy.

Finding 3:

Billing for damages to City property claims procedures not formally documented

The Finance Department provided a copy of the Billing for Damages to City Property Policy, updated in 2021. This policy provides a general overview of the requirements each department must follow for processing damage recovery claims. However, no formal administrative procedures to guide the specific details of damage recovery processing exist at the department level. Such procedures are integral to ensuring consistency and accuracy in the claims process, especially since damage recovery is managed through a decentralized structure.

It was found, upon conducting process overviews and interviews with each department processing damage recovery claims, that formal administrative procedures have not been documented for processing damage claims at the department level. Formal workflows are documented for traffic signs, signals, street lights and small claims process, but that level of detail is not provided to every department that processes damage claims. Water Department's supporting documentation is only stored in paper form rather than scanned or noted with the invoice in Munis as is the standard in other departments. Additionally, neither the overarching City policy nor a department policy outlines what proper storage should entail. Currently, there is also variability regarding sending invoices to collections.

The current practice is to pursue in small claims court regardless of dollar amount for Public Works invoices; however, other departments typically send to collections when the amount is less than \$300. A consistent standard procedure for departments to follow is lacking. Staff processing damage claim invoices are attempting to follow the instructions they have been provided; however, there is inconsistent implementation of the Billing for Damages to City Property Policy due to lack of training on the expectations and lack of detailed, formal procedures specific to the departments. The design, implementation and monitoring of formalized and documented specific control-related policies and procedures is an essential element of any comprehensive internal control structure. Inconsistent storage of supporting documentation, inconsistent labor rates applied to invoices in one department (noted in Finding 1), overhead charges for material costs in one department (noted in Finding 2) and inconsistent workflows for collections or small claims processing were due to the absence of a consistent, standard procedure at the department level in line with the overall City policy. **See Recommendations 1, 2 and 3.**

Recommendations and Management Response

1 We recommend each department responsible for processing damage recovery claims establish a formalized Administrative Procedure for Property Damage Recovery claims specific to the software utilized. This procedure should detail record keeping requirements, establish a point of contact with each department, and detail roles and responsibilities for implementing the requirements of the Billing for Damages to City Property. We also recommend Finance play an active role in the development of these procedures to ensure they align with the Billing for Damages to City Property Policy and maintain oversight responsibility for ensuring the procedures are created and implemented.

Management's Response: The City is currently implementing VueWorks asset management software across several Public Works departments. We agree this software can be used to help account for costs associated with damaged property. Finance and Public Works will coordinate to develop standardized procedures for all damage property claims that meet the requirements of the Billing for Damages to City Property policy by the end of the second quarter.

Management Representative Responding: Dean Borchardt, Business Operations Manager

Date of expected implementation: 6/30/2022

2 We recommend Finance establish a monitoring program to ensure department procedures are in place and appropriately implement the Billing for Damages to City Property Policy. This should include periodic checks on damage recovery invoices, collections and write-offs.

Management's Response: Finance will work closely with the departments to ensure the policy and procedure for damage recovery is reviewed and followed. We will continue to review and evaluate on an annual basis.

Management Representative Responding: Janelle Zerr, Finance Manager

Date of expected implementation: On-going

3 We recommend all department procedures for damage billing require supporting documentation be stored electronically in the software available to the department. We also recommend the procedures require that the work order number be noted somewhere with the invoice in Munis to ensure supporting documentation can be located and substantiated.

Management's Response: All damage billing supporting documentation was available for all claims. We agree for convenience that these documents should be stored electronically and we will include that requirement in the administrative procedures. For the departments that are using the work order system, we will require in procedure the work order number be noted on the Munis invoice.

Management Representative Responding: Dean Borchardt, Business Operations Manager

Date of expected implementation: Implemented moving forward.

Opportunities for Improvement

1 We recommend a formalized procedure to aid the departments in decision-making, including exactly when a write-off should be initiated, including dollar amount thresholds, timing and under what circumstances it is appropriate, considering that collections agency invoices and invoices pursued in small claims court have different specific circumstances.

Management's Response: Finance will develop a formalized procedure to clarify when and how write offs should be initiated. This procedure will identify the most common situations where write-offs occur and recognize the fact that each claim can have unique circumstances that warrant individual decision making. We will have this procedure in place by the end of the second quarter.

Management Representative Responding: Janelle Zerr, Finance Manager

Date of expected implementation: 6/30/2022

2 We recommend utilizing VueWorks work order management capabilities as they are implemented in each department by integrating the work order management processes into the damage recovery billing processes for maximum efficiency.

Management's Response: The City is currently implementing VueWorks asset management software across several Public Works departments. We agree this software can be used to help account for costs associated with damaged property. Finance and Public Works will coordinate to develop standardized procedures for all damage property claims that meet the requirements of the Billing for Damages to City Property policy by the end of the second quarter.

Management Representative Responding: Dean Borchardt, Business Operations Manager

Date of expected implementation: 6/30/2022

Conclusion

Based upon our review of the Damage Recovery Billing process, it was determined that the invoicing process is currently conducted efficiently and effectively. Particular areas of success include the efficiency of generating the initial invoice, cost recovery ratio, percentage of invoices outstanding and accuracy of claims processed utilizing VueWorks work order management. It appears there are also opportunities to strengthen controls and improve the overall process to ensure the accurate and timely collection of funds due to the City. We found:

- Inconsistent implementation of the Billing for Damages to City Property Policy
 - One department utilizing an overheard charge not outlined in Policy
 - One department invoicing for labor at an average rate rather than actual cost incurred per City Policy
- Lack of department level procedures to strengthen internal controls

The above recommendations will provide additional assurance to mitigate the risks related to damage billing. No evidence of fraud, waste or abuse was detected. We would like to thank Risk Management, the City Attorney's Office, Public Works and Finance for their assistance provided during this audit.

Authorization

The Sioux Falls City Council approved this audit by resolution and it was included as an assurance audit in the 2020 Annual Audit Plan. The Internal Audit Division operates under the authority of Sections 32.010 through 32.025 of the Sioux Falls Code of Ordinances.

Audit Standards

This audit was conducted in accordance with the *International Standards for the Professional Practice of Internal Auditing* issued by the Institute of Internal Auditors.

Statement of Independence

Internal Audit is administratively and operationally independent of the programs and departments it audits, both in appearance and in fact. The Internal Audit Manager is accountable to an Audit Committee appointed by the City Council per Section 32.022 of the Code of Ordinances of Sioux Falls, SD.

Distribution of Report

This report is intended for the information and use of the Mayor and City Council, management, and others within the City of Sioux Falls. However, the report is a matter of public record and its distribution is not limited.

Performed By

Emily Newell
Internal Auditor