



# City of Chattanooga

INTERNAL AUDIT

City Hall

Chattanooga, Tennessee 37402

Stan Sewell  
Director

Ron Littlefield  
Mayor

January 21, 2011

Mayor and City Council  
City of Chattanooga  
Chattanooga, TN 37402

RE: Comcast of the South Franchise Fees, Audit #10-07

Dear Mayor Littlefield and City Council Members:

Attached is the Internal Audit Division's report on Comcast of the South Franchise Fees.

We thank the management and staff of both Comcast and the Finance Department for their cooperation and assistance during this audit.

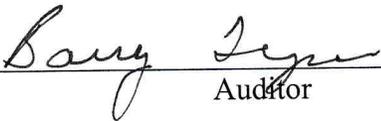
Sincerely,

Stan Sewell, CPA, CGFM  
Director of Internal Audit

cc: Dan Johnson, Chief of Staff  
Audit Committee Members  
Daisy Madison, Administrator Finance Department  
Russell Byrd, Comcast of the South

**FINANCE DEPARTMENT  
COMCAST OF THE SOUTH FRANCHISE FEES  
AUDIT 10-07  
DECEMBER 3, 2010**

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\_\_\_\_\_  
Auditor

  
\_\_\_\_\_  
Audit Director

**COMCAST OF THE SOUTH FRANCHISE FEES  
AUDIT 10-07**

**INTRODUCTION**

In May 1990 the City of Chattanooga (City) agreed to a non-exclusive contract with Comcast of the South (Comcast) to provide cable television service within the boundaries of the City (City Ordinance 11940). This contract was renewed in March 2007. In return for the privilege of providing cable television service within the City, Comcast agreed to pay five percent of certain gross revenues related to cable television, net of bad debt write-offs. The 2007 contract renewal specified payments were to be made no later than forty-five days after each quarter end, to be submitted with specific documents supporting the payment.

**STATISTICS**

Date	Quarterly Revenue*	Paid to City**
11/2007	\$ 8,241,552	\$412,078
02/2008	\$ 9,089,193	\$454,460
04/2008	\$ 9,224,791	\$461,240
08/2008	\$ 9,371,825	\$468,591
10/2008	\$ 9,334,906	\$466,745
02/2009	\$ 9,323,540	\$466,177
04/2009	\$ 9,638,969	\$481,948
07/2009	\$ 9,860,442	\$493,022
11/2009	\$ 9,554,501	\$477,725
02/2010	\$ 9,674,524	\$483,726
05/2010	\$ 9,735,622	\$486,781
08/2010	\$ 9,690,702	\$484,706

**\*Revenue reported by Comcast    \*\*Data from Collection Reports**

## **STATEMENT OF OBJECTIVES**

This audit was conducted in accordance with the Internal Audit Division's 2010 Audit Agenda. The objectives of this audit were to determine if:

1. Comcast is in compliance with the financial terms of the contract.
2. Comcast is using the proper revenue elements as a basis for calculation of franchise fees.
3. Comcast has accurately assigned addresses to be included in revenue calculations.
4. The City has procedures in place to properly oversee the Comcast contract.

## **STATEMENT OF SCOPE**

Based on the terms of the contract between the City and Comcast, the audit will cover the three-year period beginning October 1, 2007 and ending September 30, 2010.

## **STATEMENT OF METHODOLOGY**

We reviewed the contract between Comcast and the City for pertinent facts related to our audit. We met with personnel of Comcast to discuss expectations for the audit. We obtained records from Comcast and the City, performing tests to ensure proper revenue elements were being used to calculate franchise taxes paid to the City. We obtained records of addresses Comcast considered to be within the City and compared them to Hamilton County GIS records to determine if all proper addresses were included. We interviewed City Finance Department staff to determine if written policies and procedures were in place related to tracking compliance with contracts, and, if so, were being followed.

To achieve the audit's objectives, reliance was placed on computer-processed data contained in both the Comcast and City financial systems. The City's financial system was previously determined to be reliable and no additional work was necessary. Reliance on the Comcast system was based upon the 2009 audit report by Deloitte & Touche, which states in all material respects Comcast had internal control over financial reporting based on criteria established by COSO.

## **STATEMENT OF AUDITING STANDARDS**

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

## **AUDIT CONCLUSIONS**

Based upon the test work performed and the audit findings noted below, we conclude:

1. Comcast was principally in compliance with the financial terms of the contract.
2. Comcast revenue recognition was performed properly related to contract terms, with immaterial exceptions.
3. Comcast does not have all addresses related to annexations included in their calculations for franchise fee purposes.
4. The City does not have administrative procedures in place to properly determine if contract terms are met.

While the findings discussed below may not, individually or in the aggregate, significantly impair the operations of the Finance Department, they do present risks that can be more effectively controlled.

## **FRANCHISE FEES NOT PAID ON ALL ADDRESSES WITHIN THE CITY**

Comcast provided a file containing addresses used as a basis to determine addresses within the City. This information is used by Comcast to calculate franchise fees due the City. The City GIS department obtained a file of City addresses from the Hamilton County GIS department. The City GIS department compared the two files and found the Comcast file did not contain all current City addresses. These inadvertently missing addresses result in lower, incorrect franchise fee payments.

We found responsibility related to notification of annexations is not required in the franchise fee contract. The latest annexation for which Comcast made adjustments was in 2005. Comcast took no measures to discover annexation information, nor did the City notify Comcast of annexations taking place after 2005.

## **RECOMMENDATION 1**

We recommend Comcast implement measures to track annexations by the City. We further recommend the City Finance department implement procedures to adequately inform Comcast of annexation activity. The Internal Audit Division will open a special project and work with Comcast to correct the current discrepancies, calculate delinquent fees and associated interest owed the City by Comcast.

## **AUDITEE RESPONSE**

Comcast agreed to implement measures to more closely track City annexations.

The City Finance department will establish procedures to ensure timely reporting of annexations for franchise agreements.

## **DOCUMENTATION NOT INCLUDED IN FRANCHISE FEE PAYMENTS**

The contract between Comcast and the City states supporting documents submitted with franchise fee payments will include a statement of total gross sales and a schedule broken down by major revenue categories. The schedule by major revenue categories was not attached as backup with any payment of franchise fees during the audit period. The exclusion of this document prevents the City from determining if payments are based on all revenues specified in the contract and prevents duplication of the fee calculation.

## **RECOMMENDATION 2**

We recommend Comcast include all required documentation with fee payments going forward as specified in the contract.

## **AUDITEE RESPONSE**

Comcast concurs with the finding and will attach required documentation with future payments of franchise fees.

## **CONTROL PROCEDURES NEEDED FOR CONTRACT ADMINISTRATION**

Related to the Comcast franchise fee contract, we determined no City department or employee has been assigned responsibility for: Ensuring payment is remitted, proper documentation is included with the payments, proper reviews are performed to ensure the payment is correct, and payment is submitted within forty-five days of quarter end, per the contract.

## **RECOMMENDATION 3**

We recommend responsibility for each City contract be assigned to a specific group or position within the Finance Department to ensure compliance with contract terms. We also recommend an electronic tickler list be created listing all City contracts of

this nature, along with specific contract terms related to requirements for payment (e.g. due date, documentation). The employee who reviews a contract payment should sign off on the tracking spreadsheet after completing the review to ensure compliance with contract terms. Also, we recommend one individual be responsible for updating the list of contracts and terms as needed to keep it current. We further recommend this process be detailed in writing, distributed to necessary staff, and available on the City's Intra-Net.

#### **AUDITEE RESPONSE**

The Accounting division will be given responsibility to monitor receipt and franchise fee contract compliance. Monitoring procedures will be developed and documented.

#### **FRANCHISE FEES SHOULD BE MAILED TO TREASURER'S OFFICE**

Franchise fee payments and documentation are currently mailed to the Mayor's office. The package is then forwarded to the office of the City Finance Officer, and sent from there to Accounting to be processed and transferred to the Treasurer's office. Stamps notating receipt date and time are used inconsistently, excepting the Treasurer's office.

#### **RECOMMENDATION 4**

We recommend Comcast be notified to send checks directly to the City Finance Officer. The check should be received, the stub date stamped and a collection report prepared by the accounting division within three days of receipt in compliance with T.C.A. 6-56-111.

#### **AUDITEE RESPONSE**

We concur with the above recommendation. Finance will notify Comcast and implement the suggested changes.

#### **CITY ACCOUNTS RECEIVABLE UNRECONCILED**

A Comcast quarterly franchise fee payment (8/2010) of \$484,705.76 (revenue) was incorrectly credited to accounts receivable. The posting error was discovered more than two months later when Internal Audit searched for the payment related to this audit. We found accounts receivable are not reconciled regularly. We further found budget variance analysis of revenue accounts was not performed thoroughly during the early portion of the fiscal year.

### **RECOMMENDATION 5**

We recommend the City Finance Department reconcile accounts receivable on a scheduled, timely basis.

### **AUDITEE RESPONSE**

To facilitate transitioning to Oracle, a temporary procedure was put in place whereby FY10 revenues received during the first quarter of FY11 were recorded as collections against a receivable account. These accounts were reviewed by Accounting for proper reclassification and reporting in accordance with GASB 33 for year-end audit purposes. The procedure will be revised to ensure proper reporting and monitoring of all receivable and revenues on a timely basis.

### **AUDITOR COMMENT**

Entries posted to an incorrect account occur in the course of regular business, and are to be expected. An erroneously posted Comcast payment resulted in a general review of the accounts receivable reconciliation process. We discovered accounts receivable are not being reconciled regularly. Results of unreconciled receivables can include: amounts owed the City not being aged, or follow up measures not being timely performed. A basic tenet of accounting requires asset and liability balances to be reconciled to the detailed records at regular intervals, with discrepancies researched and appropriate corrections made promptly. Also, it is important for accounts to show the correct balance at all times, not only year-end.

### **RECOMMENDATION 6**

We recommend the City Finance Department perform analysis of revenue accounts versus budgeted amounts in a regularly scheduled, timely manner. Significant variances should be traced to the root cause, and corrections made as necessary.

### **AUDITEE RESPONSE**

The Finance Department reviews revenue collections monthly looking at actual collections, collections compared to budget and estimated collections for the full fiscal year; this includes research and corrections as an integral part of the process. A more detailed review of year end adjusted revenues during the accrual period will be performed in the future.