OFFICE OF THE CONTROLLER

CITY OF PHILADELPHIA PENNSYLVANIA

WATER DEPARTMENT

AUDITOR'S REPORT

FISCAL 2003 and 2004

Jonathan A. Saidel
City Controller

CITY OF PHILADELPHIA

OFFICE OF THE CONTROLLER
12th Floor, Municipal Services Bldg.
1401 John F. Kennedy Boulevard
Philadelphia, Pennsylvania 19102-1679
(215) 686-6680 FAX (215) 686-3832

JONATHAN A. SAIDEL
City Controller
ALBERT F. SCAPEROTTO
Deputy City Controller

December 7, 2005

Mr. Bernard Brunwasser, Commissioner
Philadelphia Water Department
ARAMARK Tower, 5th Floor
1101 Market Street
Philadelphia, PA 19107

We have examined the financial affairs and operations of the Water Department for the fiscal years 2003 and 2004 pursuant to the requirements of Section 6-400 (c) and (d) of the Philadelphia Home Rule Charter. A synopsis of the results of our work is provided in the executive summary to the report.

We have discussed our findings and recommendations with your staff during the course of our audit. Your written response, submitted in lieu of a formal exit conference, has been included as part of our report. Our recommendations have been numbered to facilitate tracking and follow-up in subsequent years. We believe that, if implemented by management, these recommendations will improve internal controls and the effectiveness and efficiency of the Water Department's operations.

We would like to express our thanks to you and your staff for the courtesy and cooperation displayed toward us during the conduct of our work.

Very truly yours,

JONATHAN A. SAIDEL
City Controller

cc: Honorable John F. Street, Mayor
Honorable Anna C. Verna, President
and Honorable Members of City Council
Members of the Mayor's Cabinet

Purpose

We examined the financial affairs of the Philadelphia Water Department (PWD) as part of our audit of the City of Philadelphia's basic financial statements, to determine whether management's internal controls over accountability of financial resources, safeguarding of assets, and compliance with certain laws and regulations were suitably designed and placed in operation.

Background

The PWD was established by the Philadelphia Home Rule Charter to operate and maintain the city's water supply, storm water and sewage systems and wastewater treatment plants. It also investigates and adopts methods for improving the water supply quality and fixes and regulates rates for supplying water and disposing of sewage. To carry out these responsibilities during fiscal year 2003, the PWD received operating and capital appropriations of $234.3 million and $288.0 million, respectively. For fiscal year 2004, the PWD received operating and capital appropriations of $251.3 million and $298.2 million, respectively. Not including amounts collected by the city's Water Revenue Bureau, revenues for fiscal years 2003 and 2004 were estimated to be approximately $54.1 and $62.0 million, respectively. At the end of fiscal years 2003 and 2004, exclusive of real property and infrastructure, the PWD reported that it held assets totaling $74.8 and $77.8 million, respectively.

Results In Brief

We found the following internal control conditions that detract from the ability of the PWD to adequately safeguard its assets and efficiently carry out its responsibilities.

Fairmount Water Works Interpretive Center

The Fairmount Water Works Interpretive Center (WWIC) has opened as an ecotourism center operated by the PWD. Because of its relative newness, documentation that would help define the WWIC's relationship with the Fairmount Park Commission which is responsible for the overall Water Works, steer its future, and establish policies and procedures over donation and fee collections have not been prepared. Also, opportunities exist to expand the marketing of the WWIC.

Petty Cash Controls

Our review disclosed a fund overage of approximately $500 that had existed for eight months. It was caused by the department requesting reimbursement for disbursements that were not made. We also noted inadequate separation of duties and other control weaknesses.

Status of Prior Year Findings

Action is still required to have annual evaluations prepared for all employees.

Recommendations

In order to formalize and define the WWIC's relationship with the Fairmount Park Commission, formally plan for its operation, and establish policies and procedures for collecting donations and fees, we recommend that the PWD:

- Prepare a written agreement with the Fairmount Park Commission covering the use of space occupied by the WWIC.
- Complete a strategic business plan that charts the course for the WWIC.
- Establish a policy regarding the solicitation and collection of donations and fees and prepare procedures for handling their receipt.

To help promote the WWIC, we recommend that PWD officials contact the Philadelphia Museum of Art in order to make its presence known to Museum visitors. Consideration should also be given to having the WWIC included in the city's Official Visitor's Guide.

To reduce the chance of petty cash errors or irregularities occurring and not being discovered in a timely manner, we recommend that overages be resolved quickly, reimbursements only be requested when disbursements are made, and that adequate separation of duties be maintained.

To provide employees with feedback regarding their job performance, as well as to comply with Civil Service Regulations, the department should take action to see that supervisors fulfill their responsibility of completing annual evaluations.

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BACKGROUND

Powers and Duties

The Philadelphia Home Rule Charter established the Philadelphia Water Department (PWD) which is one of the operating departments under the direction of the Managing Director. The department's responsibilities include:

- Operating and maintaining the city's water supply and stormwater system. This includes constructing, maintaining, repairing and improving the city's water supply facilities.
- Operating and maintaining the city's sewage system and wastewater treatment plants.
- Investigating and adopting methods for improving the quality of the water supply.
- Fixing and regulating rates and charges for supplying water and sewage disposal services.

Management

At the close of fiscal 2003 and fiscal 2004, the Water Commissioner directed a staff of about 2,100 and 2,000 employees, respectively, most of whom were appointed through civil service procedures. For budgetary purposes, the PWD's operations are divided into six divisions.

Financial Resources

Management has responsibility for establishing and maintaining controls to safeguard the financial resources for which it is accountable. Safeguarding controls are designed to (1) prevent or timely detect unauthorized acquisition, use, or disposition of assets, (2) ensure the reliability of financial reporting and (3) to comply with applicable laws and regulations. During fiscal years 2003 and 2004, management of the PWD was accountable for the following appropriations, revenues and assets (exclusive of real property and infrastructure):

	2003	2004
Appropriations:		
Water Operating Fund	$234,306,232	$251,255,374
Water Capital Fund	287,959,000	298,156,000
Revenues:		
Non-Tax Revenue	$ 31,085,000	$ 38,590,000
From Other Governments	8,400,000	7,700,000
From Other Funds	14,567,000	15,695,000
Assets (Year End Balances):		
Petty Cash	$ 60,000	$ 60,000
Accounts Receivable	1,267,600	1,636,614
Materials & Supply Inventory	12,930,465	13,338,350
Personal Property	60,568,749	62,809,852

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Philadelphia, Pennsylvania 19102-1679
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JONATHAN A. SAIDEL
City Controller
ALBERT F. SCAPEROTTO
Deputy City Controller

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL

We annually audit the basic financial statements of the City of Philadelphia, Pennsylvania as of and for its June 30 fiscal year end and issue a report thereon. Those statements include financial transactions of various city departments and agencies. We conduct our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the basic financial statements are free of material misstatement, we perform centralized and departmental tests of the City of Philadelphia's compliance with certain laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. 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 consideration of the Water Department's compliance with certain laws, regulations and contracts was limited to tests of certain assets, revenues, and appropriation activity during fiscal years 2003 and 2004. Grant compliance was tested and reported on as part of our single audit in accordance with Office of Management and Budget Circular A-133. Our departmental tests disclosed no instances of noncompliance by the Water Department that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we consider the internal control over financial reporting for the City of Philadelphia's centralized system, as well as for those systems in place at each department or agency, in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on the internal control over financial reporting.

Our consideration of the Water Department's internal control over financial reporting was limited to determining if its control components for certain assets, revenues, and appropriation activity were suitably designed and placed in operation during fiscal years 2003 and 2004, and would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the Water Department's internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

We noted no matters involving the Water Department's internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the Water Department's internal control over financial reporting, which are described in the accompanying findings and recommendations section of the report.

This report is intended solely for the information and use of the management of the City of Philadelphia, the Water Department, and City Council and is not intended to be and should not be used by anyone other than these specified parties.

October 31, 2005

Albert F. Scaperotto

ALBERT F. SCAPEROTTO, CPA
Deputy City Controller

FAIRMOUNT WATER WORKS INTERPRETIVE CENTER

The Fairmount Water Works Interpretive Center (WWIC) is an ecotourism center operated by the Philadelphia Water Department (PWD). It is located on the east bank of the Schuylkill River within the Fairmount Water Works complex. The Water Works complex is an 1815 National Historic Landmark and a National Historic Civil and Mechanical Engineering Landmark, owned by the City of Philadelphia and administered by the Fairmount Park Commission, that has been beautifully restored in recent years. It was considered an architectural and engineering marvel from the day it opened, supplying water to City residents until the early 1900's. The WWIC, which opened on October 29, 2003 at a cost of over $5 million, is used by the PWD to advance its public and watershed education programs, while also informing the public of the role that the Water Works and the PWD have played in the development of the city and region.

The cost to restore the Water Works was shared by the city and a number of other sources, including state agencies and private organizations. Grants and contributions for the restoration have been funneled through the Fund for the Water Works, a 501(c)(3) nonprofit organization. The PWD has utilized this fund to also handle funds raised for the WWIC. Contributions for future Water Works renovation projects are also made to this fund.

Currently, admittance to the WWIC is free. It attracts school groups, other groups, tourists and residents of the region. It averages about 26,000 visitors yearly and provides a series of educational programs. Comments we received from groups visiting the WWIC have been unanimously favorable regarding the restoration efforts and the historic and environmental exhibits it houses.

As part of our 2003-04 audit of the PWD, we performed a very limited review of WWIC operations. Based on that review, we offer the following comments and observations.

Written Policies Needed on Interdepartmental Relationship

There is currently no written agreement between the PWD and the Fairmount Park Commission outlining the rights and responsibilities of both parties concerning the use of space occupied by the WWIC. Currently, the PWD operates the WWIC based on a series of verbal agreements with the Fairmount Park Commission that were established over the years as the project was envisioned and came to fruition. We understand that these verbal agreements address such issues as the handling of costs for security and maintenance of the facility. While these unwritten agreements have apparently sufficed so far, it is in the best interest of the parties involved to put current practices in writing. We therefore recommend that the Water Department execute a written agreement with the Fairmount Park Commission regarding the current operations of the WWIC and its anticipated future expansion [12803.01].

Current Strategic Business Plan Not Yet Completed

A current strategic business plan, in the works for a number of years, has not yet been completed. This plan should chart the course for the WWIC for a number of years, and cover such topics as operations, development, marketing, and fundraising. We were informed during our audit that it was scheduled to be completed by June 30, 2005. As of October 31, 2005, it was

still in progress. We urge the department to complete the business plan as soon as possible as it will provide guidance and help set the direction for future WWIC activities [12803.02].

Written Policies Needed on Donations and Facility Use

The Water Department accepts and may at times solicit donations from groups that tour the WWIC and occasionally use it as a venue for meetings and other events. However, the Water Department has no written policies or procedures covering the solicitation or acceptance of such donations and the handling of donations once accepted. The donations, when discussed in advance, are usually agreed upon by the group using the facility and the PWD's General Manager of Public Affairs. Donations are deposited to the Fund for the Water Works or, if the event involves after-hours use of the facility, collections are deposited into a city account.

Questions that need to be addressed in a written policy include:

- Is the solicitation of donations from groups visiting the facility during normal business hours acceptable? If so, in what situations will donations be "solicited" as opposed to merely accepted if offered voluntarily? If solicited, what are appropriate amounts considering that the facility is officially "free" to the general public?

- Considering that after-hours use of the facility involves extra costs, who can use the facility after hours? Can it be used for private parties not related to fund-raising for the WWIC?

- When the facility is used for after-hours functions, is it acceptable to require the group to pay a fee to cover the cost of staff overtime and other expenses? In cases where fees are required, how are these amounts to be calculated (e.g. flat fee per hour, fee per person, etc.)?

- In which situations should monies collected be forwarded to the City as opposed to the FFWW? What controls will be in place regarding these collections?

We believe the lack of a written policy can invite inconsistent application of unwritten policies, and in a worst case, favoritism of certain groups over others. This could lead to a lessening of support for the WWIC.

We recommend that the department decide on and put into writing policies covering donations and fees [12803.03]. The consistent application of clearly defined policies on these matters can only serve to benefit the WWIC into the future.

Increased Visitor Opportunities Exist

Although the WWIC is located just steps away from the world-renowned Philadelphia Museum of Art, the potential synergy of this situation is not being fully realized. There is no prominent attempt at the city-owned Museum of Art to encourage visitors to consider a visit to the WWIC. The Museum of Art's 700,000 annual visitors represent an opportunity to increase

visitorship. We therefore recommend that the PWD discuss with Museum of Art management the possibility of promoting the WWIC [12803.04].

We also noted that the WWIC is not promoted at all in the current edition (Fall/Winter 2005-06) of the Official Visitor's Guide to the City of Philadelphia. It is not mentioned in the detailed descriptions of City visitor attractions, or covered in the write-up on the insert page covering Fairmount Park attractions. This guide, provided free in most City hotel rooms, is probably the main source of information used by tourists in planning their day-to-day activities. We urge the department to look into this form of promotion for the WWIC [12803.05].

PETTY CASH CONTROLS

Our review of the department's $60,000 combined petty cash fund, which is split among 10 separate locations, revealed a number of control weaknesses along with two cash overages above $10. These included:

- An overage of $542 in the Administration account. This overage existed for eight months, and was apparently caused by the department requesting reimbursement for disbursements that were not made. We had commented on this same problem in our 2001 report. Overages and delays in resolving them increase the risk of misappropriation.

- An overage of $89 in the Information Systems and Technology account.

- The preparer of the Administration account bank and fund reconciliations is also the reviewer of these reconciliations. This increases the risk of errors or irregularities not being discovered in a timely fashion.

- Bank reconciliations for two of ten accounts were not dated. The fund reconciliations for the Operations and Facilities Management divisions were not signed. These control weaknesses result in an inadequate audit trail should errors or irregularities be discovered.

We recommend that:

- Petty cash custodians only request reimbursement for disbursements that were made [12803.06].

- Overages or shortages be resolved in a timely manner [12803.07].

- The duties of preparer and reviewer for the Administration account be separated [12803.08].

- The importance of signing and dating bank and fund reconciliations be emphasized to employees involved with the petty cash account [12803.09].

STATUS OF PRIOR YEAR FINDINGS

As part of our current year review, we followed up on conditions brought to management's attention in the prior year report. We will continue to pursue these conditions and report on them until management takes corrective action or until changes occur, making our recommendations obsolete.

Unnecessary Encumbrances

We previously reported that Water Department procedures for reviewing and closing out unnecessary encumbrances were ineffective and recommended that greater care be exercised in identifying unnecessary commitments [12801.04]. Our current year testing showed that there were no significant unnecessary purchase commitments; we therefore consider this finding resolved.

Vehicles Assigned To Employees With Take Home Privileges

We have commented in prior audits on weaknesses in the process followed to provide vehicles with take home privileges to employees. We cited violations of Administrative Board Rule No. 34 concerning justification records, and urged compliance with City policies [12801.01]. This rule has subsequently been superceded by new City policies on this matter.

As part of the Citywide Fleet Reduction Project, the Water Department reduced its fleet and cut back on take home privileges. An official in the Fleet Management department informed us that city departments are no longer required to submit authorization forms for vehicle use. They are only required to maintain a list of users who have take home privileges. Based on these facts, we will consider this matter resolved.

Employees' Performance Evaluations

We have previously reported that employee performance evaluations were not always being prepared as required by Civil Service Regulations. We recommended that the department designate someone to oversee this area [12801.05]. We were informed this year that although no one was assigned this duty, supervisory personnel did attend training which emphasized the importance of timely evaluations. Nevertheless, for 6 of 23 employees tested, there were no current evaluations on file. Action is still required to address this shortcoming.

CITY OF PHILADELPHIA

WATER DEPARTMENT
ARAMARK Tower
1101 Market Street
Philadelphia, PA 19107-2994

BERNARD BRUNWASSER
Water Commissioner

December 7, 2005

Hon. Jonathan A. Saidel
City Controller
Municipal Services Bldg. 12th Fl
1401 J.F.K. Boulevard
Philadelphia, Pa. 19107

Dear Mr. Saidel:

Thank you for providing the Water Department with this opportunity to comment on the findings and recommendations contained in the "Philadelphia Water Department Auditor's Report Fiscal 2003 and 2004" as prepared by your office. As in recent years, we sincerely appreciate the thorough efforts and professionalism of your staff. Given the source and nature of the report and its findings, I do not see a need for an exit conference.

The following are our responses to your specific findings and recommendations:

Page 4 Fairmount Water Works Interpretive Center (WWIC)

Written Policies Needed on Interdepartmental Relationship.

Although, at present, no formal lease exists for the WWIC, the center is housed within a complex that is owned and controlled by the Fairmount Park Commission. The center, along with the adjacent restaurant, plaza and other facilities were renovated by the Park Commission and the City without direct involvement by the Water Department. The Department was involved in the construction of certain interior renovations within the WWIC.

When the center was opened, a number of meetings occurred between the staff of Fairmount Park and the staff of the Water Department to discuss and delineate the areas of responsibility for maintenance and operations of the complex. Agreements were made with respect to such areas as security, custodial services and repairs and maintenance both within the WWIC and in the entire complex. Many of these agreements are outlined in letters, memos and e-mails between the related parties. Unfortunately, these may not have been provided to the auditors.

Since the entire complex is owned and controlled by the City, we do not believe a formal agreement is required or necessary. However, that is not to say that such an agreement would not be helpful in outlining and memorializing the agreements in place. We will contact Fairmount Park and see if they would be willing to do so.

"AN EQUAL OPPORTUNITY EMPLOYER"

Hon. Jonathan A. Saidel
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Current Strategic Business Plan Not Yet Completed

We agree that there is a need to revisit and revise the original business plan for the WWIC. The existing plan was prepared prior to the opening of the center and called for staffing the center almost exclusively by volunteers, which proved to be impractical. Much has been learned in the several years of operation that could be incorporated into a new plan. In fact, the department has been working on development of a new business plan which, unfortunately, was not ready in time to make available to the auditors. We would expect that a revised plan will be completed within the next year. However, we should note that we consider the operation and maintenance of the WWIC to be evolving as the facility matures and additional planned improvements are completed. We are hoping that, with the opening of a restaurant at the site, utilization of the complex will increase substantially and provide for additional opportunities for cost sharing and operational changes.

Written Policies Needed on Donations and Facility Use

We agree that there may be a need for written policies regarding donations and facility use. Although the department considered the implementation of a charge for admission for this facility at its inception, it was decided that the collection of a required fee would discourage attendance at the site and pose additional internal control problems related to the collection , deposit and accounting for these fees. It was believed that this would detract from the intent of the department to maximize its outreach to as many individuals as possible regarding the costs, benefits and alternatives of the treatment of water, wastewater and stormwater.

In response to an employee suggestion, the department has been examining the costs, benefits and complications of adding a "donation box" at the WWIC, where members of the public could contribute voluntary sums for either the operations of the WWIC or for additional improvements. Although, the department does have an existing policy with respect to some of the questions raised in the report such policies have not been codified into an agreement or put into writing. The policy covers the suggested donation for visitation by school groups. The policy also covers the use of the facility by groups after hours and the reimbursement for avoidable out of pocket costs incurred as a result of such an event. We have also had discussions with both the Law Department and the Fund for the Water Works on the collection and deposit of these donations into their account. We will attempt to formalize each of these policies and procedures into a single document within the next year.

Increased Visitor Opportunities Exist

We agree with the report that there are certainly additional opportunities for increased attendance at the WWIC. We have tried various methods to increase the attendance at the site including outreach to the media and schools and to various professional and/or environmental groups. We have also been working with the Art Museum, Fairmount Park, the Mayor's Press Office and the Office of the City Representative to identify additional ways we can identify and take advantage of increased visitor opportunities.

Page 6 Petty Cash Controls

We agree with the report and will attempt to improve our controls, oversight and compliance with procedures in this area. In a rare instance a petty cash check was issued and not cashed. After a time, the check was returned unused. The funds were repaid to the Water Fund.

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In an effort to promote better management of the Petty Cash Fund, the supervisor has been handling the bank and fund reconciliation of the Petty Cash. The Department intends to change the procedure. In the future the custodian will process all requests. The supervisor will provide the reconciliations. The manager will review the work for accuracy.

The custodian of the Administration Petty Cash Fund maintains a schedule of received reconciliations to ensure the timely processing of the reconciliations. When it is not received timely, a request is made for the reconciliation. To date, this procedure has been very successful in achieving the timely processing of the reconciliations. The review of the reconciliations will include the verification of the signature of the preparer and the date the reconciliation was prepared.

Page 7 Employees' Performance Evaluations

We agree that employee performance evaluations should be issued each year. This finding is somewhat mitigated by the fact that many ratings are pass or fail only and the prior year's evaluation stays in effect if there is none in the current period. Nonetheless, I will again direct our General Manager of Human Resources to assign someone on his staff to follow up with PWD personnel who have not completed filling out their employee's evaluations.

This concludes out comments. We would appreciate their inclusion in the final report. We do not believe an exit conference is necessary.

Thank you for your attention in this matter.

Very truly yours;

Bernard Brunwasser
Water Commissioner

cc: Anthony Radwanski, Deputy City Controller
Fredrick Wise, Audit Administrator
Eli Massar, Assistant to the Department of Finance
Loree Jones, Chief of Staff Managing Director's Office