



DATE: May 24, 2012

TO: Jorge Carrasco, Superintendent

FROM: Brian Brumfield, Interim CFO *DFB*

SUBJECT: SCL Actions to Address Cash Handling Weakness Identified in Baker Tilly Report

At our request Baker Tilly has conducted an assessment of our cash handling procedures within City Light (their report is attached).

This review did **not** focus on the typical payment of a customer electric account; which makes up approximately \$929 million in receipts per year and for which well established and well tested controls already exist. Those typical electric payments go through what is known as a “lockbox” – checks are sent by customers to a P.O. Box address that is then processed by a financial institution on City Lights behalf, where the deposit is made and information transmitted to City Light concerning what customer accounts to credit. The lockbox process provides well established controls to prevent theft or fraud, to verify the integrity of the receipt and to document the payment.

The focus of this review was to examine the handling of payments within City Light where checks may be received for a variety of services such as joint-use of poles, engineered service connection, conservation projects, etc. These types of receipts total approximately \$37 million per year, so they represent a relatively small portion of the total transactions SCL processes.

Baker Tilly identified several areas where we can improve our internal controls related to cash handling which I will briefly describe below along with the actions we are taking to address them and a timeline for completion.

Key Observations from Baker Tilly Report:

Check Handling:

The largest and most widespread control weakness found by Baker Tilly involves the way checks are handled at SCL. All mail is currently opened and sorted at SCL mailroom. Checks are separated from other mail; however, they are then (currently) delivered to as many as 15 different org units within SCL to whom they were addressed. The individual org

units then process the payments prior to preparing the deposit of the checks. This decentralization of checks throughout the organization increases the opportunity for checks to disappear or for fraud to occur.

SCL is addressing the problem as follows:

- We are currently implementing a manual process to have all checks currently received at the mailroom immediately handed over to a payment analyst to have all checks stamped, logged and deposits prepared. The supporting documents (without the actual check) will then be forwarded to the appropriate org units. This manual process will greatly reduce the risks identified under the current practice, and serve as a short term fix that can be implemented quickly. **(Expected to have in place by June 18)**
- SCL will establish lockbox processing for these checks, so that payments are sent to a P.O box as described above and checks are never handled within City Light. We have met with FAS to discuss this service and have further meetings scheduled to begin transitioning to this approach; beginning with the Escrow processing org unit, which currently receive the most payments, with others to follow shortly thereafter. It will take time to notify payees of the new addresses for mailing checks, but the manual process described above will be in place should checks continue to arrive. **(Escrow Org Unit expected complete by June 25, others by July 31)**

Unapplied Payments

When payments are received and we are unable to identify what the payment was for, or to what account to apply it, the checks are deposited but the funds are not credited to any customer account until the Account Control group can research the payment and determine where to apply it. Baker Tilly noted that there is a significant backlog of unapplied payments, and that the lag in applying payments can increase the likelihood of them being misapplied.

SCL Director of Customer Care (Kelly Enright) has committed to analyze the current process and devote additional resources to improving the process and working through the outstanding backlog of work. **(Expected work plan developed by June 30)**

Surplus Sales

SCL regularly sells off scrap metal resulting from its operations. Baker Tilly identified that the existing process where a single City Light employee works with the scrap dealer to weigh, price, and pay for the scrap metal results in a lack of proper supervision. With the same individual handling all aspects of the sale there is potential for inappropriate deals to be made. They recommend separating the responsibilities so that the role of weighing and

Jorge Carrasco, Superintendent
May 24, 2012
Page 3

negotiating is separately reviewed by another employee and well documented, and that payment is received separately through an established service center to avoid cash handling issues.

SCL is writing a new procedure to address the concerns and will institute training of the employees as soon as the procedures are set. **(Expected to be in place by July 31)**

Lighting Design Lab payments

SCL operated a training facility called the Lighting Design Lab, which educated people on energy conservation techniques. Some of the training offered there requires registration payments by those attending. Most pay ahead of time on-line, but occasionally checks are received. Baker Tilly identified that when checks are received for these classes they are made payable to Lighting Design Lab rather than Seattle City Light, which can make it easier for a check to be misappropriated and deposited incorrectly.

SCL has already taken steps to encourage more payments to be made ahead of time using the secure on-line payment method which is preferred. And in instances where checks are received, they are now only accepted made payable to Seattle City Light. **(Completed)**

Follow up:

In addition to making sure that the risk mitigation efforts described above are fully implemented as quickly as practicable, SCL will perform follow up testing 60-120 days after implementation to verify that the new processes are being adhered to and that training was adequate, and to revise processes where needed.

Historical Review:

Although we have no reason to believe, or evidence to suggest, that the current processes led to any fraud or theft; the controls as they existed have left that possibility open. Since these new control efforts only reduce the risk going forward, SCL will work in conjunction with the City Auditor and with its own available staff to do additional testing of past transactions to satisfy ourselves that no fraud has occurred prior to these control concerns being addressed.

BB:bb