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April 12, 2011

Honorable Mayor and Members of the
Board of Aldermen
City of Portland
100 South Russell Street
Portland, TN 37148

Mayor and Members of the Board of Aldermen:

We have concluded our investigative audit of selected records of the City of Portland. The audit focused on the period January 1, 2008, through September 30, 2010. The investigative audit concentrated on expenditures related to improvements to the city's water system. As a result, the audit was primarily limited to an examination of selected disbursements. However, when warranted this scope was expanded.

Water System Rehabilitation Grant

In 2008 the Tennessee Department of Economic and Community Development awarded a \$414,607 grant to the City of Portland to rehabilitate the city's water system. The scope of the project included the replacement of service lines and water meters as well as plugging and abandoning old water lines.

Scope of services reduced but payment to contractor unchanged

The contract for the project was awarded to a construction contractor based on a competitive bid. The contract included the installation of 63 commercial meters at an installed price¹ of \$3,000 each. However, due to field conditions and other reasons, city officials did not require the contractor to install 21 of the commercial meters included in the original contract. That should have reduced the amount paid to the contractor, as well as the State of Tennessee's payment to the City of Portland under the grant, by \$63,000. However, we found that neither the payment to the contractor nor the city's claim for reimbursement from the state was reduced.

¹ Cost of the installation and the meter itself. The contractor purchased and provided the meters.

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Change in scope of services not documented in city's records and not properly reported to state

According to city officials and the contractor, the project required more work than had originally been anticipated. The city's maps depicting the locations of old water lines were inaccurate and incomplete; consequently and at the city's request, the contractor performed additional work² attempting to locate the old water lines. City officials acknowledged that the grant contract with the state did not have an expense category that allowed payment for this type of work. Although city officials requested and were granted two change orders to this grant by the state, the city did not request one to accommodate the additional work. To compensate the contractor for this additional work, the city paid him \$63,000 as if the 21 uninstalled meters had actually been installed under the contract. In addition, the contractor was allowed to keep the meters. The city's project documentation was completed to indicate the 21 meters were actually installed.

City paid contractor over \$40,000 with no justification

The contractor had documentation that appeared to support his assertion that he performed additional work. The city had no documentation that supported the extra work. We reviewed the documentation maintained by the contractor; however, it supported less than \$23,000 of extra work. We could not justify the payment of over \$40,000 to the contractor.

City used water meters without consent of the contractor and for nongrant use

All of the water meters purchased by the contractor for the grant project were stored on city property during and after the project. City utility personnel used seven of the meters for new taps and maintenance services that were not within the scope of the grant and without the knowledge or consent of the contractor. The city did not reimburse the contractor for these meters valued at over \$10,000.

Purchase of meters violated city's purchasing policy

Approximately 19 months after the completion of the project, the city purchased the remaining 14 meters from the contractor for \$20,887.72³ without obtaining bids and without obtaining board approval. The city charter and *Tennessee Code Annotated*, require that expenditures of \$5,000 or more be let out for bid. The city charter also requires council approval for purchases over \$5,000.

² This involved digging holes using a backhoe, operator, and up to two laborers.

³ This is the same price the contractor paid for the meters.

Other Issues

While performing the investigative audit, additional internal control and compliance deficiencies came to our attention:

1. The mayor authorized the former public works superintendent to charge a city credit card with over \$1,600 for airfare and other expenses related to a personal trip. In addition, another \$212 personal charge was placed on the former public works superintendent's city credit card. According to the former superintendent, the personal expense was inadvertently charged to the city card by a family member. The employee later reimbursed the city for all these costs. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 5, Chapter 18, Section 6, requires city officials to adopt a purchasing policy that would:

... designate individuals who are authorized to make purchases with municipal debit or credit cards. Clearly define the types of purchases permitted to be made using debit or credit cards. Such purchases must be approved in the same manner as any other purchase. If municipal officials authorize the use of credit and/or debit cards, the number of cards maintained should be kept to a minimum and should be properly accounted for. A record of the current holder(s)/user(s) should be maintained in the municipality's files. ***Personal charges should be strictly prohibited.*** [Emphasis added.]

2. The municipality's files did not include adequate supporting documentation for each disbursement related to the grant project. As previously noted, the city's project records indicated 63 rather than 42 meters had been installed. In addition, one change order on the project for over \$10,000 of additional work was not supported by adequate documentation. Based on the limited information in city files, we could not determine if the work was performed on the water system. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 5, Chapter 19, Section 6, states:

All disbursements, regardless of the accounting procedures, must be supported by invoices, cash tickets or other adequate supporting documentation.

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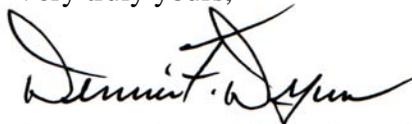
3. There was inadequate oversight over city inventories of materials. A contractor's employees had unlimited access to city inventory. In addition, the city stored materials belonging to a contractor on city property. Finally, we found that one meter valued at over \$1,400 was unaccounted for. The *Internal Control and Compliance Manual for Tennessee Municipalities*, Title 5, Chapter 23, Section 1, states:

Municipal officials should ... adopt policies and procedures that provide safeguards for inventories of materials and supplies. These policies and procedures should, at a minimum, include the following:... a requirement that all materials and supplies are stored in designated areas that are protected against unauthorized withdrawals and other losses....

4. In December 2009, the city spent \$1,875 for gift cards for city employees. However, the values of these gifts were not recognized as compensation on the employee's federal Form W-2. The Internal Revenue Service considers this type of gift by an employer to be a taxable fringe benefit.

The mayor and members of the board of aldermen should take immediate corrective action to resolve these issues. If you have any questions or need additional information, please contact me.

Very truly yours,



Dennis F. Dycus, CPA, CFE, Director
Division of Municipal Audit

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