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Audit Report

TEXAS GAS SERVICE FRANCHISE FEE

December 11, 2007

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Austin, Texas

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City of Austin

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Date: December 11, 2007
To: Mayor and Council
From: Stephen L. Morgan, City Auditor
Subject: Texas Gas Service Franchise Fee Audit

I am pleased to present this audit report on Texas Gas Service franchise fee revenues. The City of Austin grants a franchise agreement to Texas Gas Service (TGS) to operate a natural gas distribution system within the City. According to the agreement, TGS pays the City a gas franchise fee of five percent for every customer located within the corporate limits of the City of Austin. For this audit, we tested whether TGS is remitting this fee for all customers in Austin.

Based on our analysis we concluded that TGS remits a gas franchise fee to the City of Austin for the vast majority of customers located within Austin city limits. However, we identified a small number of miscoded records that resulted in incorrect payments of approximately \$11,000 and a net of approximately \$2,000 due the City.

We have issued one recommendation that addresses the need for the City to collaborate with TGS to correct the miscoded records identified during this audit and recover the additional fee due to the City associated with the miscoded records.

We appreciate the cooperation and assistance we received from staff in the Telecommunications and Regulatory Affairs division of Financial and Administrative Services Department and from Texas Gas Service during this audit.

Stephen L. Morgan, CIA, CGAP, CFE, CGFM
City Auditor



ACTION SUMMARY TEXAS GAS SERVICE FRANCHISE FEE



Recommendation Text	Management Concurrence	Proposed Implementation Date
01. In order to address current problems with TGS data and to ensure that the City receives all franchise fee revenue, TARA should work with TGS to ensure that existing errors in the TGS billing system are corrected and that TGS's records of City boundaries are accurate. Additionally, TARA should work with TGS to recover the additional fee due to the City for the 188 miscoded records.	Concur	January 2008

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BACKGROUND

The City of Austin grants a franchise agreement to Texas Gas Service (TGS) to operate a natural gas distribution system within the City. The streets, right-of-way, and public easements used by the gas companies within the boundaries of the City are valuable public properties acquired and maintained by the City. The City collects a five percent franchise fee on the company's total reported gross revenues each calendar quarter as rental payments for use of the public rights-of-way and to recover costs incurred by the City for regulating and administering the gas franchise agreement. The City's Office of Telecommunications and Regulatory Affairs (TARA) regulates and administers this franchise agreement. Gas customers are charged 5.376%, which includes the City's franchise fee plus a state tax imposed on the franchise fee.

In October 2006, the City renewed its gas franchise agreement with TGS for the next 20 years. Prior to the agreement renewal, TARA hired an outside consultant to determine whether TGS was complying with the terms of the agreement and to identify improvements to the agreement. The consultant reviewed gas franchise fee payments between 1997 and 2004 and determined that overall TGS complied with the terms of the agreement and found two monetary exceptions that resulted in TGS owing the City approximately \$50,000 due to:

1. A discrepancy between gross revenues reported to the City and actual gross revenues;
and
2. Several properties in annexed areas not being coded to the City in a timely manner.

TGS provides gas service to the majority of gas customers within the Austin city limits, serving over 200,000 customers. TGS gas franchise fee payments to the City average approximately \$5 million each year.

OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives

The purpose of this audit was to determine whether Texas Gas Service (TGS) remits a gas franchise fee to the City of Austin for all customers within Austin city limits.

The TGS agreement with the City was audited by an outside consultant in 2006. Our office, as part of an audit of gas franchise fees conducted in 2007, determined that the consultant work was reliable. However, the consultant study tested only areas annexed in 1997 and 1998, while this audit tested TGS customers located in and around Austin, regardless of the annexation date. Additionally, we selected this audit because previous work done by our office identified problems with regard to the reliability of data associated with the remittance of gas franchise fees and we wanted to provide assurance that all revenue from TGS was remitted to the City.

Scope

Given the previous work performed by an outside consultant on the TGS agreement, the scope of this audit was limited to the current gas franchise agreement between the City and TGS, which entered into effect in October 2006. Our scope included TGS billing records for all customers located in and around Austin, as of October 2007. Where problems were identified, our scope included gas franchise fee revenue paid to the City of Austin by TGS since the beginning of the current franchise agreement.

Methodology:

In order to perform this audit work, we used the various methods, including:

- Analyzing previous audit work related to gas franchise fee revenues;
- Obtaining and analyzing data from TGS billing system, including testing reliability of data;
- Using GIS to map TGS billing addresses to determine whether customers' records within the City of Austin are correctly codes as Austin customers.

This audit was conducted in accordance with generally accepted government auditing standards.

AUDIT RESULTS

TGS remits a gas franchise fee to the City of Austin for the vast majority of customers located within Austin city limits; however, we identified a small number of miscoded records that resulted in underpaying the City.

Our review of Texas Gas Service (TGS) billing records showed that TGS records accurately reflect customers located within the City of Austin. We noted some errors, including 188 customers located within Austin for which TGS is currently not paying the City and 12 customers located outside of Austin for which TGS is erroneously paying gas franchise fee to the City. However, miscoded records identified represent only 0.1% of the total records.

TGS has not paid the gas franchise fee to the City for 188 customers. According to the gas franchise agreement, TGS has to pay the City a gas franchise fee of five percent for every consumer (person or organization) located within the corporate limits of the City of Austin. Our review of TGS records showed that 188 customers located within Austin corporate boundaries were not attributed to Austin in TGS’s billing system. As a result, TGS did not remit the gas franchise fee to the City for these customers. From October 16, 2006 to present TGS should have remitted an additional \$6,700 to the City. This amount was calculated using TGS billing records that date back to the day the customer began gas service with TGS or October 16, 2006, the day the agreement was renewed (whichever occurred later). Exhibit 2 on the following page shows the location of the miscoded customers identified and how long TGS has not been remitting the gas franchise fee to Austin, based on the annexation year or the year the gas service started.

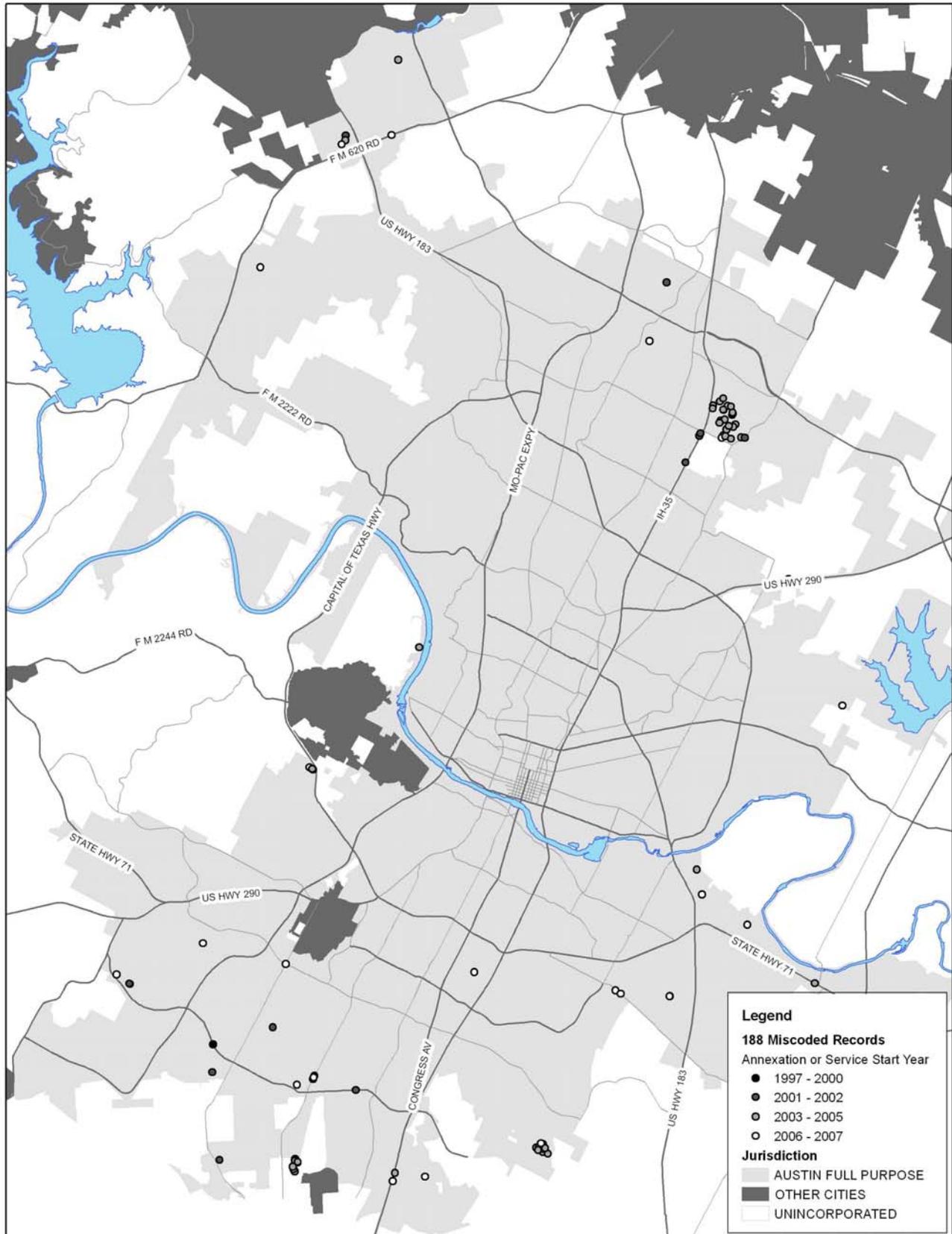
As shown in Exhibit 1 below, the majority (179) of the miscoded customers were coded in TGS billing system as being outside an incorporated area, and therefore were not charged a gas franchise fee. For the remaining nine customers TGS was paying the gas franchise fee to another jurisdiction.

**EXHIBIT 1
Jurisdiction Allocation for 188 Miscoded Records in City of Austin**

Current Allocation	Correct Allocation	Count
Austin unincorporated area	City of Austin	175
Cedar Park unincorporated area	City of Austin	3
Dripping Springs unincorporated area	City of Austin	1
City of Cedar Park	City of Austin	4
City of Westlake Hills	City of Austin	4
City of Sunset Valley	City of Austin	1
Total		188

SOURCE: OCA analysis of TGS billing records, November 2007.

EXHIBIT 2
Location of 188 Miscoded Records



SOURCE: OCA analysis of TGS billing records, November 2007.

Additionally, our work identified 12 customers located outside of Austin’s full purpose jurisdiction for which TGS has erroneously paid the gas franchise fee to the City of Austin. In addition to the 188 customers noted above, our work identified 12 customers located outside the City of Austin for which TGS has erroneously remitted gas franchise fee revenues to Austin, resulting in an overpayment to the City of approximately \$4,700.

As shown in Exhibit 3 below, the majority (11) of these customers should be coded as being outside an incorporated area, and therefore should not be charged a gas franchise fee, while for the remaining customer TGS should remit the gas franchise fee to the City of Sunset Valley.

EXHIBIT 3
Jurisdiction Allocation for 12 Miscoded Records outside the City of Austin

Current Allocation	Correct Allocation	Count
City of Austin	Austin unincorporated area	8
City of Austin	Cedar Park unincorporated area	3
City of Austin	City of Sunset Valley	1
Total		12

SOURCE: OCA analysis of TGS billing records, November 2007.

Miscoded records represent a small fraction of records reviewed. As described above, analysis performed on over 224,000 TGS billing records for customers located in and around Austin identified coding errors for only 200 records (188 customers located within Austin for which TGS is currently not paying the City and 12 customers located outside Austin for which TGS is erroneously paying the gas franchise fee to the City). Miscoded records represented only 0.1% of the total records. The limited number of errors seems to be due to strong controls implemented by TGS in their data entry process. Specifically, in 2004 TGS has upgraded to a new system with built-in controls, such as rules and validation tables, which validate the jurisdiction, and its corresponding rate, against the zip code. Additionally, TGS has assigned the responsibility to set-up new addresses in the system to only one person, increasing consistency and data integrity.

Recommendations

01. In order to address current problems with TGS data and to ensure that the City receives all franchise fee revenue, TARA should work with TGS to ensure that existing errors in the TGS billing system are corrected and that TGS’s records of City boundaries are accurate. Additionally, TARA should work with TGS to recover the additional fee due to the City for the 188 miscoded records.

MANAGEMENT RESPONSE: Concur

TARA will verify that TGS has corrected errors in their billing system and records of City boundaries and recover franchise fee revenues for miscoded records

APPENDIX A
MANAGEMENT RESPONSE



TO: Stephen L. Morgan, City Auditor
FROM: Leslie Browder, CPA, Chief Financial Officer
DATE: December 4, 2007
SUBJECT: Management Response to Texas Gas Service Franchise Fee Audit

Thank you for the opportunity to provide management's response to the audit report recommendation. We concur with the one (1) recommendation provided below. Rondella Hawkins, Manager of the Office of Telecommunications & Regulatory Affairs, has the primary responsibility to ensure action is taken and that the recommendation is implemented.

01. In order to address current problems with TGS's data and to ensure that the City receives all franchise fee revenue, TARA should work with TGS to ensure that existing errors in the TGS billing system are corrected and that TGS's records of City boundaries are accurate. Additionally, TARA should work with TGS to recover the additional fee due to the City for the 188 miscoded records.

The Office of Telecommunications & Regulatory Affairs plans to implement this recommendation in the month following adoption of the report by the Audit and Finance Committee, but in any event, no later than January 31, 2008.



Leslie Browder, CPA, Chief Financial Officer

12-4-2007
Date

ACTION PLAN
Texas Gas Service Franchise Fee Audit

Rec #	RECOMMENDATION TEXT	Concurrence	Proposed Strategies for Implementation	Status of Strategies	Responsible Person/ Phone Number	Proposed Implementation Date
01	02. In order to address current problems with TGS data and to ensure that the City receives all franchise fee revenue, TARA should work with TGS to ensure that existing errors in the TGS billing system are corrected and that TGS's records of City boundaries are accurate. Additionally, TARA should work with TGS to recover the additional fee due to the City for the 188 miscoded records.	Management concurs with recommendation.	The Office of Telecommunications & Regulatory Affairs will verify that TGS has corrected errors in their billing system and records of City boundaries and recover franchise fee revenues for miscoded records.	<ul style="list-style-type: none"> • Planned 	Rondella Hawkins, Manager, Office of Telecommunications & Regulatory Affairs	Within one month after adoption of report by the Audit and Finance Committee and no later than January 31, 2008.