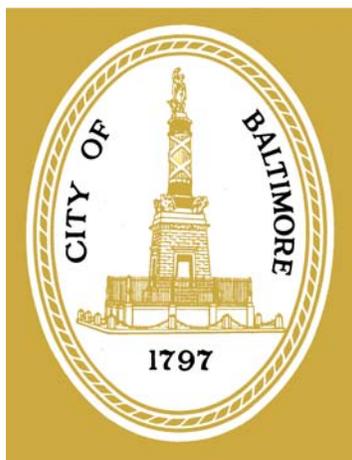


PERFORMANCE AUDIT REPORT

CITY OF BALTIMORE
MAYOR'S OFFICE OF TRANSPORTATION
DIVISION OF CONDUITS

REVENUES GENERATED THROUGH
THE RENTAL OF CONDUIT DUCT SPACE

JANUARY 2002



City of Baltimore
Department of Audits

CITY OF BALTIMORE

MARTIN O'MALLEY, Mayor



DEPARTMENT OF AUDITS

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January 9, 2002

Honorable Joan M. Pratt, Comptroller
And Other Members of the
Board of Estimates
City of Baltimore

We conducted an audit of the revenue generated through the rental of conduit duct space managed by the Mayor's Office of Transportation – Division of Conduits. We focused our review on the revenue generated during calendar year 2000, and on the revenue generated through the rental of duct space footage occupied at June 30, 2000.

The purpose of our audit was to determine whether adequate internal accounting and administrative control policies and procedures existed to ensure that the revenue amounts were properly determined and collected in accordance with applicable laws and regulations and that revenue was properly monitored and recorded.

As a result of our audit, we determined that there was a lack of clear definition of central responsibility over the City's conduit rental operation. The Mayor's Office of Transportation's Right-of-Way and Conduit Sections, the Department of Finance's Bureau of Accounting and Payroll Services, and the City's Law Department all contributed to the conduit operation. However, comprehensive knowledge of the conduit operation was not consolidated within any of these agencies.

For the six month period from July 1 through December 31, 2000, potential revenue of approximately \$2.2 million was not collected because of the lower rate charged to a major conduit user that was less than the \$.58 per foot charged to other conduit users.

We also noted other control weaknesses and recommend that the Mayor's Office of Transportation:

- Develop written policies and procedures that clearly define the Mayor's Office of Transportation's mission, objectives and operational responsibilities concerning the rental of the City's conduit space.

- Create an automated database to include all conduit users and other pertinent information such as the existence of leases, entry and exit dates, footage leased, rates, and billing information.
- Prepare written lease agreements for all conduit users and ensure that all pertinent information such as approved leases and applications of duct space are forwarded to the Bureau of Accounting and Payroll Services in a timely manner.
- Review its agreements with two major conduit users and address whether the conduit rental rates charged to them are equitable to the City and other users.
- Ensure the accuracy and timeliness of conduit billings, and periodically monitor conduit rental accounts receivable reports generated by the Bureau of Accounting and Payroll Services to ensure that conduit revenues are collected in a timely manner. To encourage timely vendor payments, monetary penalties should be assessed on delinquent accounts.

In July 2000, the Greater Baltimore Committee (GBC) issued a report to the Mayor indicating that conduit rental could potentially generate millions of dollars in additional revenue for the City. The realization of this revenue potential, however, is dependent on the implementation of our audit recommendations. In particular, the recommendation that the City determine whether the conduit rental rates charged to two major conduit users should be increased to achieve comparability with the rates charged to the other private companies is key to obtaining the level of revenue growth noted in the GBC report. At the new rate of \$.58 per foot, potential annual conduit rental revenue from one of the major conduit users would exceed the actual revenue by \$4.4 million for the conduit footage billed at June 30, 2000.

We appreciate the cooperation and assistance provided by the Mayor's Office of Transportation, the Department of Finance's Bureau of Accounting and Payroll Services and the Law Department while conducting this audit. Their cooperation was instrumental to the completion of this audit.

Respectfully submitted,

Yovonda D. Brooks, CPA
City Auditor

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Background Information

Historical

The Mayor's Office of Transportation (MOT) was established as a separate agency of the City of Baltimore (City) effective September 1, 2001. Until then, the Bureau of Transportation was one of four bureaus that comprised the Baltimore City Department of Public Works. During the period covered by this audit, the MOT was still a bureau in the Department of Public Works.

The MOT's Division of Conduits is responsible for developing, maintaining, and controlling approximately 5,000 miles of conduit ducts under the streets, lanes, and alleys of Baltimore City as authorized by Ordinance 107 of 1898 and Article 26 of the Baltimore City Code. The conduits carry wire and cable for high voltage electrical services, communications, traffic control devices, telephone and telegraph, and fire alarms. Roughly, one-half of the available duct space is occupied. Based on available information, the Baltimore Gas and Electric Company (BGE), Verizon (telephone company) and the City occupied approximately 91% of the total conduit space occupied at June 30, 2000. The remaining occupied conduit space was used by 43 private companies and organizations. Though a small percentage, this latter group is growing both in the number of users and in conduit footage occupied.

The rental of conduit space by the City originated at the end of the 19th Century. Initially, specific conduit rental rates were assessed and incorporated into the Baltimore City Code (Code) through agreements with the power and telephone companies. On July 1, 1967, the Code was amended regarding the establishment of conduit rental rates. Instead of indicating specific rate amounts, the amended Code stated, "The Board of Estimates is hereby authorized and empowered to determine and fix the annual amount to be charged for the use of the conduits...so as to charge or allocate to each user of the said conduits... its share of the actual cost to the City of owning, operating, and maintaining the same, in proportion to the amount of conduit space occupied by each said user." Conduit rental revenue was therefore restricted to the recovery of the City's conduit system costs. Annual calculations were made to determine the conduit rental rates.

The *Managing for Success* Report to the Mayor issued in July 2000 by the Greater Baltimore Committee and Presidents' Roundtable (GBC) recognized the limitations on revenue enhancement by the cost recovery method used to charge conduit users. The report recommended that the City consider lifting the restriction on charging rental fees that exceed the cost of maintaining the City's conduit system. According to the GBC report, the financial impact for additional revenue was estimated from \$3 million to \$25 million. In December 2000, a City ordinance was passed removing the cost recovery restriction from the City Code. The ordinance was amended to state, "The Board of Estimates may set and, from time to time, modify the annual charges imposed for the use of the conduits that are constructed under this article."

Operational

The Division of Conduits is responsible for determining the amount of conduit space occupied by the users and submitting the actual footage to the City's Department of Finance – Bureau of Accounting and Payroll Services (BAPS). BAPS is responsible for billing the users and

assessing late fees, if necessary. The Code requires that conduit rental billings be processed semi-annually in advance, in June for July through December, and in December for January through June. BAPS generates a report at the end of each month that lists unpaid billings.

Non-City users pay the City rent based on the amount of conduit footage occupied at the approved rental rate. Beginning July 1, 2000, the Board of Estimates increased the conduit fee rate from \$.209 per linear foot to \$.58 per linear foot, applicable to all non-City users except Verizon. The conduit revenue reported in the City's accounting records for calendar year 2000 was \$1,514,331 (excluding Verizon).

Despite removing the cost recovery section of the ordinance, the development of the \$.58 rate was still based on the City's conduit system costs. The total rental rate was determined by the City to be \$1.16 per foot of conduit space. However, in order to mitigate the financial impact on the users of increasing the rate more than five times the previous rate of \$.209, the City decided to phase in the new rate. Initially, fifty percent, or \$.58, of the calculated rate of \$1.16 was implemented as of July 1, 2000. The balance of the rate will be phased in when approved by the Board of Estimates.

Verizon's (originally the Chesapeake and Potomac Telephone Company) agreement with the City, which is a franchise, is subject to different rate regulations. Article 26, Subtitle 24 of the Baltimore City Code specifically relates to conduit use by the telephone company. The rates charged stem from a July 5, 1889 agreement and have remained the same since. Specifically, Verizon pays, annually, \$.30 per linear yard for the first 4 miles in aggregate length of conduit and \$.20 per linear yard for each successive mile or fraction thereof, not to be less than the annual sum of \$3,000. The telephone company is billed annually for the period May through April. Conduit revenue received in September 2000 from Verizon for the May 1999 through April 2000 period was \$117,468.

Audit Scope, Objectives and Methodology

We conducted an audit of the revenue generated through the rental of conduit duct space managed by the MOT – Division of Conduits. Our review focused on the revenue generated during calendar year 2000, and on the revenue generated through the rental of duct space footage occupied at June 30, 2000. Our audit was conducted in accordance with generally accepted *Government Auditing Standards* related to performance audits, issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

The objectives of our audit were to determine whether adequate internal accounting and administrative control policies and procedures existed to ensure that the revenue amounts were properly determined and collected in accordance with applicable laws and regulations, and that revenue was properly monitored and recorded.

To accomplish our objectives, we obtained an understanding of the functions and activities performed by the MOT related to the revenue generated through the rental of conduit duct space, including an understanding of applicable policies and procedures. As part of our audit, we spoke with various MOT personnel as well as officials from the Law Department and the Department of Finance's Bureau of Collections. We also obtained an understanding of the procedures performed by the BAPS related to conduit billings and reviewed the Baltimore City Code sections related to conduits. We performed tests of transactions and other information to determine the accuracy of footage and billing amounts, timeliness of collections, whether leases were executed, and that deposits were properly recorded.

Our audit findings and recommendations are detailed in the Findings and Recommendations section of this report. The response from the Mayor's Office of Transportation is included as an appendix to this report.

Findings and Recommendations

Accounting and Administrative Control Environment

Conclusion

The MOT did not establish written policies and procedures that defined the Division of Conduits' objectives and operational responsibilities related to the rental of conduit space. The Division of Conduits was unable to provide a complete list of conduit users. The MOT could not provide us with leases for all of the conduit users. Conduit users were not billed in advance as required by the Baltimore City Code. A significant number of billings were not paid timely and the MOT did not utilize the provisions of the Baltimore City Code regarding the collection of delinquent billings. Billing rates for two major conduit users were not consistent with other conduit users.

Finding #1

The Mayor's Office of Transportation did not have written policies and procedures that defined the Division of Conduits' objectives and operational responsibilities regarding rental of conduit space.

Analysis

The MOT did not have written policies and procedures that defined the Division of Conduits' objectives and operational responsibilities regarding the rental of conduit space. The City's Administrative Manual requires that every organization should provide reasonable assurance that it adopts certain standards and follows adequate written policies and procedures. The Right-of-Way Section conducted the initial contact with prospective users of the conduit space and subsequently executed the lease agreements between the City and the users. The Division of Conduits determined the footage that the user occupied and forwarded that information to the Right-of-Way Section and the BAPS. The BAPS billed the users based on the effective rate and footage provided by the Division of Conduits.

As a result of the lack of written policies and procedures, the City entities (Right-of-Way Section, Division of Conduits, BAPS) participating in the conduit revenue operation did not have a clear understanding of their responsibility or that of the other participants. Monitoring by the MOT to determine whether users were properly billed and whether rental payments were made to the City was not performed. Excessive reliance on the BAPS and the information it maintains has resulted in limited management of the program by the MOT. Overall responsibility for the efficient and effective operation of the City's conduit rental program has not been established.

Recommendation

We recommend that the MOT establish written policies and procedures that identify its specific operational responsibilities for conduit rental functions, including monitoring of user billings and collections. Overall conduit program responsibility should be established within the MOT.

Finding #2**The Mayor's Office of Transportation did not maintain an automated database of conduit rentals.****Analysis**

The Mayor's Office of Transportation did not maintain a database of conduit rentals that includes data on user names, status of leases, changes in space occupied and billable footage, rental rates applied, rental periods and status of billings and payments. The MOT was unable to provide a complete, accurate listing of conduit users and the space occupied. We compiled a listing from information obtained from the Right-of-Way Section, the Division of Conduits and the Bureau of Accounting and Payroll Services. It's vital that footage totals and adjustments be tracked continuously in order to provide the information necessary for the City to properly bill the users, budget revenues, determine the amount of conduit space used and available, and monitor the status of conduit user accounts.

Recommendation

We recommend that the MOT account for all conduit users and footage occupied through the creation and maintenance of a comprehensive automated database. We recommend that the database include pertinent information such as user names, status of leases, footage occupied, changes in space occupied and billable footage, rental rates and periods, and the status of billings and payments.

Finding #3**Payments for conduit rental billings were not collected timely. Monetary penalties were not assessed on late vendor payments.****Analysis**

Payments for conduit rental billings were not collected timely. Additionally, the Mayor's Office of Transportation did not utilize the provisions of the Baltimore City Code to enhance collection efforts for delinquent conduit users. Conduit rental payments were not made to the City within 30 days of billing dates. We reviewed thirty-five (35) billings for 18 conduit users for the period from July 1 through December 31, 2000. Payments for only two of the 35 billings were received within the specified 30 days. Four (4) of the payments were received more than 100 days after the billing dates, and eight (8) billings had not been paid as of April 30, 2001.

Article 26, Subtitle 23-5(c) of the Baltimore City Code specifies that "charges shall be billed semi-annually, in advance as of the 1st days of January and July in each and every year, and such bills shall be paid within 30 days after the date thereof." Furthermore, Section 7 of the conduit lease agreement states that, "In the event of failure by the Lessee to pay the rentals within the thirty (30) days specified, the Department of Public Works shall remove all cables and wires in the conduits belonging to said Lessee, without notice, at the Lessee's expense, and require the payment of rentals in arrears by said Lessee before its cables and wires may be replaced."

Monetary penalties or interest fees were not assessed for late payments on billings for conduit space rental. We believe that penalties assessed on late vendor payments will encourage vendors

to make conduit rental payments timely. Before the assessment of penalties for delinquent conduit users can be made, however, the conduit leases should be amended to include a provision indicating the criteria for the imposition of the penalties. The lease provision should include either a monthly interest or flat fee charge assessed against any outstanding balance.

Recommendation

We recommend that the MOT periodically monitor lease billings to ensure that conduit revenues are collected in a timely manner. We also recommend that the MOT enforce the provisions of the Baltimore City Code and lease agreements regarding collection of conduit rentals within 30 days of billing dates. Conduit leases should be amended to include provisions for the assessment of monetary penalties on lease payments which are made beyond the 30 day grace period. We also recommend that the City develop a policy to address the time period allowed before the City will remove the cabling of delinquent users from the conduit system.

Finding #4

The Mayor's Office of Transportation did not have written lease agreements for all conduit users.

Analysis

The Mayor's Office of Transportation did not have written lease agreements for all conduit users. In accordance with Article 26, Subtitle 23-4 of the Baltimore City Code, the MOT is authorized and empowered to adopt and promulgate rules, regulations, and conditions pertaining to or governing the use of conduits. The current conduit rental program requires a written lease agreement between the City and each user. We selected 18 of the 43 conduit users to determine whether proper leases were executed. The MOT was not able to provide us with lease agreements for 12 of the 18 users tested.

Recommendation

We recommend that the MOT prepare written lease agreements for all current and future conduit users to ensure that the lessees are informed of the terms, conditions and specifications required by the City and that the City's interests are protected. The approved leases should be forwarded to the Bureau of Accounting and Payroll Services in a timely manner.

Compliance with the Baltimore City Code

Finding #5

Conduit users were not billed in advance as required by the Baltimore City Code for the period covering July 1 through December 31, 2000.

Analysis

Conduit users were not billed in advance as required by Article 26, Subtitle 23-5(c) of the Baltimore City Code for the period covering July 1 through December 31, 2000. The billing rate for July 1 through December 31, 2000 was increased by the City from \$.209 to \$.58 per foot of conduit space. However, this rate change was not approved until December 2000. The BAPS was aware that a rate change was forthcoming and decided to postpone billing for this period until the rate was approved. Rate approval did not occur timely, and BAPS billed the conduit users in November 2000 at the old rate of \$.209. Supplemental billings were sent out to all the conduit users several weeks later for the difference between the two rates.

Recommendation

We recommend that the Bureau of Accounting and Payroll Services continue to bill semi-annually in accordance with the Baltimore City Code. Billings should be prepared in advance based on approved rates in effect at January 1 and July 1. If necessary, supplemental billings should be issued for any retroactive, approved rate changes.

Equity in Billing Rates

Finding #6

Billing rates charged by the City for the period of July 1 through December 31, 2000 to two major conduit users were not consistent with those of other conduit users.

Analysis

Billing rates charged by the City for the period of July 1 through December 31, 2000 to two major conduit users were not consistent with those of other conduit users. Excluding these two users, the previous rental rate was \$.209 per foot for the period January 1 through June 30, 2000. Effective July 1, 2000, the rental rate was increased to \$.58 per foot.

Although the City billed conduit users at the new rate of \$.58 per foot, one conduit user did not pay its rental of conduit space at that rate. Instead, it paid rent based on its own calculated rate. For the period July 1 through December 31, 2000, this resulted in a reduction in revenue to the City of \$2,223,732. This conduit user has not paid its conduit rental at the new rate of \$.58 per

foot. Instead, it has negotiated a separate rate with the City effective January 1, 2001. This rate is less than half of the \$.58 rate applicable to the other conduit system users and was never presented to the Board of Estimates for approval. Moreover, even before this rate increase, for years, this user paid less than other conduit users. Conduit rental rates were determined using one method for this user and another for the other users, which resulted in lower rental rates for this user. The Baltimore City Code does not provide for special treatment concerning billing rates for any user except for Verizon.

Verizon's conduit rental rate has not changed since it was first established in a contractual agreement with the City dated July 5, 1889. In short, the agreement states that, annually, the phone company pays \$.30 per yard for the first 4 miles of conduit space and \$.20 per yard for each succeeding mile or fraction thereof, not to be less than the annual sum of \$3,000. At July 1, 2000, Verizon occupied 584,743 yards of conduit space which, in accordance with the agreement, was an estimated annual rental charge of \$117,652. For most of its conduit space, Verizon's rate was about one-tenth the rate charged to other conduit users. Verizon is a franchise holder which accounts for the lower rental rates. Nevertheless, the City should review its agreement with Verizon to determine whether its rate is still equitable more than 110 years after it was established.

Considering the City's desire to develop the rental of conduit space as a revenue source, it must address the rental rates assessed these two major users.

Recommendation

We recommend that the City review its agreements with these two major conduit users and the appropriate sections of the City Code and determine whether these rates are equitable to the City and other conduit users. As required by the City Code, the Board of Estimates should approve rental rates for all conduit users.

APPENDIX I

THE MAYOR'S OFFICE OF TRANSPORTATION'S RESPONSE

TO THE

PERFORMANCE AUDIT OF THE

REVENUES GENERATED THROUGH THE

RENTAL OF CONDUIT DUCT SPACE

FROM	NAME & TITLE	Alfred H. Foxx, Director	CITY of BALTIMORE MEMO 
	AGENCY NAME & ADDRESS	Office of Transportation Room 527, Benton Building	
	SUBJECT	CONDUIT AUDIT	

TO:

Yovonda D. Brooks, CPA
 City Auditor
 Room 321, City Hall

DATE:

December 18, 2001

This memorandum is in response to the Draft Audit Report concerning the administration of the City's conduit system. We recognized the need for this type of comprehensive audit and were pleased to be of assistance with its' preparation. While we agree with all of the findings and recommendations outlined in that report, we must say that the rental of conduit space is not presently "managed" solely by the Office of Transportation. As stated in the audit, we are just one of several agencies that currently play a role in the administration of the conduit system.

Our replies to each of the specific findings and recommendations are as follows:

Finding #1

The Mayor's Office of Transportation did not have written policies and procedures that defined the Division of Conduits' objectives and operational responsibilities regarding rental of conduit space

Recommendation

We recommend that the MOT establish written policies and procedures that identify its specific operational responsibilities for conduit rental functions, including monitoring of user billings and collections. Overall conduit program responsibility should be established within the MOT.

Reply

We fully agree with this recommendation. We anticipate that it will take approximately six months to secure the necessary personnel and to develop the written policies and procedures as outlined above and referred to in the audit analysis. This will also provide the opportunity to gain any needed administrative or legislative approvals.

Finding #2

The Mayor's Office of Transportation did not maintain an automated database of conduit rentals.

Recommendation

We recommend that the MOT account for all conduit users and footage occupied through the creation and maintenance of a comprehensive automated database. We recommend that the database include pertinent information such as user names, status of leases, footage occupied, changes in space occupied and billable footage, rental rates and periods, and the status of billings and payments.

Reply

We agree with the need for an automated database that includes all of the information outlined in the recommendation. We will ask that the MOIT assist us with identifying or developing a computer program that will accomplish this. We also understand that as a result of this audit the Department of Audits compiled a list of occupants of the conduit system and that is now probably the most comprehensive listing. We would appreciate a copy of that listing. We will begin to do this now with the expectation that it should be in use within three months as this will facilitate the implementation of the other recommendations in this report.

Finding #3

Payments for conduit rental billings were not collected timely. Monetary penalties were not assessed on late vendor payments.

Recommendation

We recommend that the MOT periodically monitor lease billings to ensure that conduit revenues are collected in a timely manner. We also recommend that the MOT enforce the provisions of the Baltimore City Code and lease agreements regarding collection of conduit rentals within 30 days of billing dates. Conduit leases should be amended to include provisions for the assessment of monetary penalties and lease payments which are made beyond the 30-day grace period. We also recommend that the City develop a policy to address the time period allowed before the City will remove the cabling of delinquent users from the conduit system.

Reply

While we agree with this recommendation and each of its provisions, we wish to make it clear that we expect the Bureau of Accounting and Payroll Services in the Department of Finance to continue to bill the conduit users based on the information provided by us as well as, collect the appropriate fees or penalties for late payment that may be developed.

Finding #4

The Mayor's Office of Transportation did not have written lease agreements for all conduit users.

Recommendation

We recommend that the MOT prepare written lease agreements for all current and future conduit users to ensure that the lessees are informed of the terms, conditions and specifications required by the City and that the City's interests are protected.

Reply

Clearly, we must have a current written lease agreement with each conduit user. We will require the assistance of the City Law Department for the review of any existing leases as well as, the development and review of any new leases that must be prepared. This would include the review for legal sufficiency as well as, the inclusion of any new provisions such as penalties for non payment or untimely payment. We will require this assistance, until a suitable person can be hired to do this in the Transportation Office.

Finding #5

Conduit users were not billed in advance as required by the Baltimore City Code for the period covering July 1 through December 31, 2000.

Recommendation

We recommend that the Bureau of Accounting and Payroll Services continue to bill semi-annually in accordance with the Baltimore City Code. Billings should be prepared in advance based on approved rates in effect at January 1 and July 1. If necessary, supplemental billings should be issued for any retroactive, approved rate changes.

Reply

We concur with this recommendation.

Finding #6

Billing rates charged by the City for the period of July 1 through December 31, 2000 to two major conduit users were not consistent with those of other conduit users.

Yovonda D. Brooks, CPA
December 18, 2001
Page 4

Recommendation

We recommend that the City review its agreements with these two major conduit users and the appropriate sections of the City Code and determine whether these rates are equitable to the City and other conduit users. As required by the City Code, the Board of Estimates should approve rental rates for all conduit users.

Reply

We agree that the City must review its agreements with the two major conduit users and will locate and review, along with the Law Department those agreements to assure that all of the agreements are consistent and comply with all applicable City Codes.

If you have any questions concerning this reply, please contact me at 396-6802 or Mr. Anthony P. Wallnofer, Jr., Acting Chief of the Transportation Maintenance Division, at 396-1686.

Respectfully,

ALFRED H. FOX
DIRECTOR

AHF/APW:lb

Cc: Mr. Anthony P. Wallnofer, Jr.