

## INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements of the City of Lubbock (COL) as of and for the year ended September 30, 2012, 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 and U.S. Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Nonprofit Organizations*, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified.

Because of the limits of internal control, errors, fraud, illegal acts or instances of noncompliance may occur and not be detected. Two or more people may also circumvent controls, or management may override the system.

A deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements of the Company's financial statements on a timely basis. A deficiency in design exists when a control necessary to meet a control objective is missing or an existing control is not properly designed so that, even if the control operates as designed, a control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.

A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented or detected and corrected on a timely basis.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

We observed the following matters that we consider to be deficiencies.

While performing internal control procedures over the procurement procedures at Lubbock Power and Light (LP&L) we noted that certain invoices lacked documentation of approval by the person that was responsible for receiving the service or goods. Based on our discussions with personnel and other procedures, it appears that invoices are being properly reviewed, but this approval is not consistently documented. In some cases, administrative staff signed off as

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approving the invoice. We recommend that approval of invoices be limited to a select group of employees and that signatures be required on any invoice by the individual responsible for receiving or accepting the goods or services before the invoice is paid.

We noted that certain invoices lacked sufficient documentation detailing the scope of work that had been performed. Although contracts and purchase orders contain the scope of services procured, we recommend that a policy be implemented requiring all vendors to provide a detail of work performed including labor charges, equipment rental, parts, etc. This will provide transparency and allow for a more effective review of the invoice.

We noted that several procurement files lacked documentation on how the winning bid or proposal was selected. Individual employees are often responsible for evaluating the bids and making a recommendation of which company should be used. We recommend that a committee of at least three employees from LP&L review each proposal and that adequate documentation be included in the bid file showing how the committee chose the winning bid or proposal. This would allow for more transparency in the procurement process and force staff to discuss ideas before a large investment is committed.

We noted that the purchasing manager at LP&L reports to the Director of Transmission and Distribution (Director of T&D). Purchases are made by managers that report to the Director of T&D. The Director of T&D's managers are responsible for purchasing a significant amount of goods and services at LP&L. We recommend that the purchasing manager report to an administrative position instead of the Director of T&D.

#### **OTHER MATTERS**

Although not considered material weaknesses, significant deficiencies or deficiencies in internal control over financial reporting, we observed the following matters and offer these comments and suggestions with respect to matters which came to our attention during the course of the audit of the financial statements. Our audit procedures are designed primarily to enable us to form an opinion on the financial statements and, therefore, may not bring to light all weaknesses in policies and procedures that may exist. However, these matters are offered as constructive suggestions for the consideration of management as part of the ongoing process of modifying and improving financial and administrative practices and procedures. We can discuss these matters further at your convenience and may provide implementation assistance for changes or improvements if you require.

The COL performs many functions for the benefit of Lubbock Power and Light. One of those functions is preparation and signing of checks and the processing of ACH transactions for the payment of LP&L invoices. We recommend that LP&L consider designating a finance or executive level manager to approve large invoices before they are sent to the COL for processing. This would give the COL greater assurance prior to payment.

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LP&L's policy is dated October 14, 1999, which is prior to the current LP&L charter. The procurement system at LP&L is very complex and an updated procurement policy is needed. We recommend that various scenarios be documented in the policy to provide guidance on what constitutes an emergency and when it is appropriate to use job order contracts and master service agreements for procuring goods or services.

There is a lot of conflict as to who is responsible for certain duties between the City and LP&L. We recommend that a formal service agreement be put into effect for the benefit of both parties.

This communication is intended solely for the information and use of management, the audit committee, the city council, and others within the City and federal and state awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

March 27, 2013