WATER, WASTEWATER, AND STORM DRAINAGE FUNDS

CITY OF BRIGHTON

PERFORMANCE AUDIT
MARCH 2020

Two Hills
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March 13, 2020

Council Members of the City Brighton:

The attached report contains the results of our performance audit of the Water, Wastewater, and Storm Drainage Utility Funds.

We conducted the audit in accordance with Generally Accepted Government Auditing Standards. The report presents financial information on the Utility Funds along with our findings, conclusions, and recommendations, and the responses of the City.

Thank you for the opportunity to help you achieve your goal of improving services to the citizens of Brighton.

Sincerely,

Brian C. Hill, CPA, MBA, CFE

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Audit Overview

Background Information

City of Brighton

The City of Brighton (Brighton) is a self-governing home-rule city located in Adams and Weld Counties, comprising roughly 21 square miles. As one of the 97 home rule cities in Colorado, Brighton establishes and collects its own fees and local taxes, including sales, use and lodging taxes. As of July 1, 2018, The U.S. Bureau of the Census estimates that Brighton had a population of 41,254, an increase from the year 2000 census when the population was reported as 20,905. The rapidly growing population now comprises 12,244 households. Industrial space and, correspondingly, water and wastewater requirements, are expected to increase significantly. The current economic climate in Brighton is strong. The Brighton Economic Development Corporation reports an unemployment rate of 2.9 percent.

Brighton operates under the council-manager form of government. An elected city council serves as Brighton's primary legislative body, appointing a city manager to oversee municipal operations, prepare the budget required by Colorado law, and implement Council's policy and legislative initiatives. The Council is comprised of 9 elected officials from four wards, including the mayor. Brighton's City Manager is responsible for day-to-day operations and management of the City's staff of about 380 employees and budget of about $139 million.

Water, Wastewater, and Storm Drainage Funds

As part of its responsibilities, the City manages the Water, Wastewater, and Storm Drainage Funds (collectively, the Utilities). These funds are reported in the City's Comprehensive Annual Financial Report (CAFR) as Enterprise Funds. Such funds operate much like a

private business. They are self-supporting funds in which fees are charged to external users. For accounting purposes, the Water, Wastewater, and Storm Drainage utilities are considered to be major funds, and they are managed and presented separately in the City's financial statements.

Audit Scope and Methodology

The City contracted with Two Hills Accounting and Consulting, P.C. to conduct this performance audit. Because of Council's expressed interest in ensuring that the City has not been vulnerable to fraud, waste or abuse, our audit included forensic analyses. Audit work was performed from November 2019 through February 2020. We appreciate the cooperation of City management and its staff during the course of this audit and the support of City Council.

Our audit was conducted in accordance with generally accepted government auditing standards. The standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on the audit objectives. To accomplish our objectives, we applied best practices established by the American Institute of Certified Public Accountants (AICPA), Association of Certified Fraud Examiners (ACFE), and the Institute of Internal Auditors (IIA). These best practices provide credible criteria and guidance from leading professional organizations that define principles and theories of fraud risk, fraud risk management, and fraud prevention and detection activities. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. In summary, for the periods 2008 through June 2019 our objectives were to:

- Analyze the source of Utilities' funds revenue including operating or rate revenue and plant investment fees for the periods 2008 through June 2019. Confirm that the source of funds ties to financial statement balances reported in the Comprehensive Annual Financial Report.

- Analyze the use of funds, including operating expenses in comparison to the growth or expansion expenses for the periods 2008 through June 2019. Confirm that the source of funds ties to financial statement balances reported in the Comprehensive Annual Financial Report.
- Analyze the operating and capital budgets to determine if the uses of funds by year were authorized and expended in accordance with City Council's appropriations.
- Compare budgeted operating expenses to actual operating expenses and budgeted capital projects to the amount spent on capital projects by year.
- Perform additional substantive testing[1]: during our analysis, we identified certain areas whereby we recommended additional testing. This testing involved the request and review of additional invoices and other purchasing records to determine the nature of specific transactions.
- Present final reports and findings, if any, at a Council Study Session upon completion of audit work.

It should be noted that the audit was neither intended nor designed to provide a comprehensive evaluation of the current status of the City's internal controls over Water, Wastewater, and Storm Drainage expenditures and activities. However, when weaknesses in internal controls were identified during our audit work, we have included them in this audit report. We have also requested responses from management regarding internal control weaknesses identified and measures taken or planned to be taken to strengthen those controls.

In accordance with standards, we are reporting that, in our judgment, our test work and related conclusions are limited by the fact that the audit period covered expenditures and activities more than 10 years ago and, as a result, some staff and documentation were no longer available. In areas where evidence was limited, we performed alternative procedures to develop a reasonable basis for our findings and conclusions. Specific

[1] Additional substantive testing was a scope change from the initial contract.

limitations included the fact that many types of documents are only required to be retained for seven years under the applicable document retention policies. Whenever possible, we reviewed compensating documentation.

Risk Assessment

We began our audit with a risk assessment to identify areas where the City's Utilities' funds might be vulnerable to fraud, waste or abuse, which are defined as:

- Fraud: "A knowing misrepresentation of the truth or concealment of a material fact to induce another to act to his or her detriment." (Association of Certified Fraud Examiners)
- Waste: "using or expending resources carelessly, extravagantly, or to no purpose. Examples include making travel choices that are contrary to existing travel policies or are unnecessarily extravagant or expensive; making procurement or vendor selections that are contrary to existing policies or are unnecessarily extravagant or expensive." (Generally Accepted Government Auditing Standards - GAGAS)
- Abuse: "behavior that is deficient or improper when compared with behavior that a prudent person would consider reasonable and necessary business practice given the facts and circumstances, but excludes fraud and noncompliance with provisions of laws, regulations, contracts, and grant agreements. Abuse also includes misuse of authority or position for personal financial interests or those of an immediate or close family member or business associate." (GAGAS)

Our risk assessment included meeting with members of City Council, Finance and Utilities management and staff; an analysis of the CAFR's from 2008 through 2018; and a review of relevant City documents. As a team, we discussed operations and activities susceptible to fraud, waste and abuse and identified the most likely fraud schemes in the Water, Wastewater, and Storm Drainage Funds. Our discussions included consideration of incentives or pressures to commit fraud, the opportunity for fraud to occur, and

rationalizations or attitudes that could allow individuals to commit fraud. As such, we assessed internal controls designed to prevent or detect fraud; reviewed the oversight roles and responsibilities of management; and evaluated the likelihood of management overrides of internal controls. We also interviewed staff regarding strengths and weaknesses in internal controls in place during the audit period. Finally, to ensure a full understanding of all requirements governing the Utilities, we reviewed applicable State laws, local codes, and procurement requirements. Based on our risk assessment, we designed and performed procedures to provide reasonable assurance of detecting significant instances of illegal acts or violations of provisions of contracts or grant agreements.

Fund Financial Information

One of the primary objectives of our audit was to determine if the Utilities' financial reports were accurate and can be relied on for decision making purposes. To that end we were asked to evaluate reports on the sources and uses of the funds over the past 11 years. Specifically:

- Are revenues and expenditures accurately recorded and reported?
- Were funds used in accordance with budget authorizations?
- Are fund balances properly presented?
- Can management rely on information to make informed decisions about the future of the funds?

To achieve our objectives, we conducted substantive testing of account balances in accordance with the terms of our engagement agreement. Substantive tests are designed to determine whether financial information is accurate. We also conducted tests on the internal controls designed to ensure the accuracy of financial information.

During our test work, we identified opportunities for improving reporting and internal controls to ensure the integrity of recorded and reported information. In addition, we found that weaknesses in budget development and presentation made it difficult to ensure funds were expended in accordance with Council's authorizations. In the sections that follow, we present the testing we conducted and provide a report on each fund's financial results. Following the presentation of individual funds, we offer opportunities for improving the accounting and procurement systems and controls.

Test Work

Our engagement agreement required extensive substantive test work on all three funds, as well as testing of internal controls on accounting and procurement systems used to process transactions.

Sources of Funds

We analyzed the sources of funds to determine if revenue was properly recorded over the time period from 2011 through June of 2019. Sources include customer charges (rate revenue), plant investment fees (PIF revenue), and bond proceeds. Our work included confirming that revenue and bond proceeds had been accurately reported in the City's Comprehensive Annual Financial Report (CAFR). In summary, we:

- Met with Utilities' staff and the City's rate consultants to understand how rates had been developed and customer charges determined.
- Reconciled the revenue entries in the general ledger to the CAFR.
- Selected a judgmental sample of approximately 60 entries that were classified as "Charges for Services" to determine if the internal controls over the recording of customer billing were operating effectively. The sample included revenue entries from each time period and each fund.

- Compared the Capital Improvement Plan (CIP) in the rate model to the CIP provided by Utilities' staff and analyzed changes over time between the CIP's provided to rate consultants.
- Selected a random sample of approximately 300 plant investment fee invoices that included transactions from each year and each fund. Verified that the amounts were recorded in the correct period and posted to the correct fund.
- Tied the bond proceeds recorded in the general ledger to those reported in the CAFR.

Uses of Funds

We analyzed the uses of funds including expenditures for on-going operations, maintenance and capital improvements. In summary, we:

- Met with Utilities' staff to gain an understanding of the project scoping, vendor selection, project management, and vendor payment processes.
- Met with Finance staff to gain an understanding of procurement processes, the accounting systems, and the accounts payable processes.
- Reconciled the expense entries in the general ledger to the CAFR.
- Tested a random sample of approximately 300 operating expense transactions that included entries in each year and each fund to ensure that expenditures were reasonable, allowable, and recorded in the proper fund and category.
- Confirmed that expenditures had been properly categorized and reported in the CAFR.
- Tested a judgmental sample of approximately 40 vendors to ensure they had been properly entered into the procurement systems. For each vendor, we selected invoices to determine if the expenses were reasonable, allowable, and the required approvals had been completed.

- Analyzed operating and growth expenditures using various sources including the rate models, general ledger information, past allocations made by staff, and discussions with current staff.

Operating and Capital Budgets

Budgets play a key role in ensuring that funds are spent in the public's interest. We were asked to analyze budgets to determine if the use of funds by year had been authorized in accordance with City Council's appropriation. To that end, we:

- Created a list of capital projects based on information from the general ledger, plant investment fee spreadsheets provided by Utilities' staff, and the rate models provided by Stantec.
- Requested information summarizing project budgets and actual expenditures by year. Compared the totals in that schedule to the project totals in the annual CAFRs to ensure they agreed.
- Reviewed the City Council meeting minutes to understand the approval process and determine what information was presented.
- Interviewed Finance and Utilities' staff to gain an understanding of the process for developing Utility Fund budgets.
- Selected a judgmental sample of 20 projects representing all three funds. We:
    - Obtained and reviewed the project documentation to determine the scope and nature of the project.
    - Reviewed City Council budget resolutions, if required.
    - Verified that the amount recorded in the budget agreed with the City Council resolution.
    - Reviewed the transactions in the general ledger to determine the total cost and cost by vendor for each project.
    - Verified that appropriate approval and procurement processes had been performed for the project.

    - Compared the budgeted amount to the actual expenditures for the project.

- Selected a random sample of approximately 330 expense transactions from the selected 20 projects. Reviewed the invoices to determine if the expenditures were reasonable, allowable, and recorded in the proper fund, project, and category.

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Reports on Individual Utility Funds

Water Fund

The Water Treatment and Distribution System is operated and maintained by the City. It is supported solely by fees and consumption charges. The System is responsible for providing approximately one billion gallons of safe drinking water annually. Toward that end, the City operates a large water treatment plant that filters and processes water (for water pumped from the Beebe Draw and South Platte alluvia). Staff is responsible for maintaining the treatment and filtering plant, 12 municipal wells, three pump stations, seven park wells, and two diversion structures. Plant personnel must comply with all Federal and State drinking water standards as well as Environmental Protection Agency regulations. In addition, staff is tasked with maintaining equipment and conducting more than 800 water analyses a month. During the period under audit, the City's Utilities Department was responsible for billing citizens for water services.

Rates are an important issue to many citizens because they pay based on the amount of water they use. In 2019, the City commissioned a Comprehensive Rate and Fee Study to evaluate the water and wastewater rate structures. Based on results of the study, the City voted to decrease water usage and fixed charges by about eight percent beginning January 1, 2020. Over the years, the City has issued bonds for water system projects, including expanding system pipelines.

A table of the Sources and Uses of the Water Fund is included on the following page. The figures include selected totals from each year's CAFR. The 2008 through 2010 totals have not been included in the following chart because the funds were not reported separately in those years.

Water Fund: Sources and Uses of Funds

SOURCES OF FUNDS

REVENUES	2011 CAFR	2012 CAFR	2013 CAFR	2014 CAFR	2015 CAFR	2016 CAFR	2017 CAFR	2018 CAFR
Operating Revenues	$ 7,294,531	$ 10,359,736	$ 9,096,867	$ 9,216,577	$ 10,155,418	$ 11,775,537	$ 14,315,080	$ 14,401,750
Developer Contributions	4,512,757		509,454	98,044	1,003,419	402,275	2,615,500	359,333
Plant Investment Fees*	578,963	1,306,787	2,456,934	3,841,845	3,462,691	3,110,473	6,780,209	6,693,862
Miscellaneous**	157,792	285,175	179,522	451,137	793,444	330,912	271,072	1,493,024
Bond and COP Proceeds	-	-	-	-		22,482,344	-	-
Total Revenues	**12,544,043**	**11,951,698**	**12,242,777**	**13,607,603**	**15,414,972**	**38,101,541**	**23,981,861**	**22,947,969**

**Note: Plant Investment fees revenue includes the Plant Investment Fee, Tap Fees, and Permit Fees*
***Note: Miscellaneous includes Grants, Investment Income, and Transfers In*

USES OF FUNDS

Expenditures	2011 CAFR	2012 CAFR	2013 CAFR	2014 CAFR	2015 CAFR	2016 CAFR	2017 CAFR	2018 CAFR
Administration	772,417	589,804	180,381	224,904	317,221	360,599	556,933	510,552
Capital Outlay	2,019,496	9,854,971	-	-	-	-	-	-
Operations	4,776,641	5,685,358	-	-	-	-	-	-
Engineering & Distribution	-	-	625,589	598,659	724,867	678,645	837,630	1,060,800
Debt Service*	3,154,985	1,718,233	1,740,103	1,750,761	1,741,050	23,233,294	1,685,254	1,689,769
Utility Billing and Assistance**	-	-	242,975	267,956	267,740	347,163	401,232	377,374
Water Resources	-	-	1,315,318	1,416,740	983,313	1,036,948	1,344,621	4,766,043
Water Treatment Plant	-	-	3,748,509	3,855,975	4,131,379	4,961,910	5,228,942	2,186,344
Total Program Expenses	**10,723,539**	**17,848,366**	**7,852,875**	**8,114,995**	**8,165,570**	**30,618,559**	**10,054,612**	**10,590,882**
Total Project Expenses	-	-	735,693	2,573,764	3,173,931	5,131,297	8,075,550	16,898,996
Total Expenses	**10,723,539**	**17,848,366**	**8,588,568**	**10,688,759**	**11,339,501**	**35,749,856**	**18,130,162**	**27,489,878**

**Note: Debt Service includes Debt Service Principal and Interest, Interest Expense, Interest Paid, Principal, and Principal Long Term Debt*
***Note: Utility Billing and Assistance includes Utility Assistance Fund and Utility Billings*

Source: City of Brighton Comprehensive Annual Financial Reports for the fiscal years 2011 through 2018

Wastewater Fund

The City administers a sanitary sewer system that collects wastewater flows from residential taps, schools, businesses and industries. Used water and sewage is treated at the wastewater plant and returned to the environment. Plant operations include filtering; removal and testing of solids, organic matter and pollutants; and disinfection. Staff are responsible for compliance with laws and regulations. Like the Water Fund, the Wastewater Fund is a business-like enterprise supported by fees and charges.

We have included a table with selected financial information from the CAFR's on the following page.

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Wastewater Fund: Sources and Uses of Funds

SOURCES OF FUNDS

REVENUES	2011 CAFR	2012 CAFR	2013 CAFR	2014 CAFR	2015 CAFR	2016 CAFR	2017 CAFR	2018 CAFR
Charges for Services	-	-	4,839,238	5,689,919	4,993,351	6,843,216	7,435,416	7,960,153
Bond and COP Proceeds	-	-	-	-	-	6,481,978	-	-
Developer Contributions	1,734,790	-	173,926	14,767	551,085	140,675	1,692,936	182,530
Investments*	95,597	113,378	65,153	41,187	77,624	141,700	115,183	264,164
Miscellaneous**	606,421	509,186	156,467	21,662	26,476	5,167	28,845	31,953
Plant Investment Fees	44,591	65,078	2,108,808	711,920	794,844	2,274,402	1,579,850	1,382,505
Sewer Connection Fees	-	-	-	-	2,430,440	-	-	-
Utility Sales and Reimbursements	3,835,602	4,925,556	439,030	186,485	-	-	-	-
Total Revenues	**6,317,001**	**5,613,198**	**7,782,622**	**6,665,940**	**8,873,820**	**15,887,138**	**10,852,230**	**9,821,305**
-	-	-	-	-	-	-	-	-

*Note: Investments includes Investment Earnings and Investment Income
**Note: Miscellaneous includes Grants, Miscellaneous Revenue, and Transfers In

USES OF FUNDS

Expenditures	2011 CAFR	2012 CAFR	2013 CAFR	2014 CAFR	2015 CAFR	2016 CAFR	2017 CAFR	2018 CAFR
2009 Bond Refunding	-	-	-	-	-	-	-	-
Administration	1,344,004	495,521	155,236	201,576	246,913	-	484,372	441,868
Capital Outlay	1,228,216	151,395	-	-	-	-	-	-
Debt Principal and Interest*	401,950	727,707	716,488	728,693	712,496	6,710,466	459,883	460,849
Engineering	-	-	116,095	137,363	189,166	180,408	252,062	340,289
Miscellaneous**	-	1,820,190	-	-	-	2,149,839	-	-
Operations	1,279,812	2,112,486	-	-	-	-	-	-
Utility Billing	-	-	240,602	270,578	263,252	338,372	404,719	363,462
Waste Water Collections	-	-	393,156	376,348	530,337	592,658	686,496	674,819
Waste Water Treatment Plant	-	-	1,758,891	1,788,314	1,795,270	1,944,462	2,049,623	2,554,217
Total Program Expenses	**4,253,982**	**5,307,299**	**3,380,468**	**3,502,872**	**3,737,434**	**11,916,205**	**4,337,155**	**4,835,504**
Total Project Expenses	-	-	96,355	187,497	258,193	3,348,298	2,644,267	2,986,640
Total Expenses	**4,253,982**	**5,307,299**	**3,476,823**	**3,690,369**	**3,995,627**	**15,264,503**	**6,981,422**	**7,822,144**

*Note: Debt and Principal includes Debt Principal and Interest, Interest Expense and Fees, and Principal
**Note: Miscellaneous includes Budget Reserve, Transfers Out, and Purchase of Metro Taps

Source: City of Brighton Comprehensive Annual Financial Reports for the fiscal years 2011 through 2018

Storm Drainage Fund

Similar to the Water and Wastewater Funds, the City's Storm Drainage System is operated and maintained as a self-supporting Enterprise Fund. The Fund collects storm drainage charges from the City's water utility account base. The independent third-party rate studies also included an analysis for the Storm Drainage Fund.

We have included a table with selected financial information from the CAFR's on the following page.

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Storm Drainage Fund: Sources and Uses of Funds

SOURCES OF FUNDS								
REVENUES	**2011 CAFR**	**2012 CAFR**	**2013 CAFR**	**2014 CAFR**	**2015 CAFR**	**2016 CAFR**	**2017 CAFR**	**2018 CAFR**
Charges for Services	-	-	843,707	595,276	507,109	612,554	732,814	816,388
Developer Contributions	4,556,353	-	404,264	8,557	293,539	259,592	1,642,583	338,643
Investment Income*	8,341	2,972	98	9,630	20,342	48,238	44,790	71,539
Miscellaneous**	-	1,800,867	9,535	335	225	152	65,396	28,722
Plant Investment Fees	-	-	-	-	426,454	891,907	844,796	982,141
Utility Sales	228,636	420,236	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
Total Revenues	4,793,330	2,224,075	1,257,604	613,798	1,247,669	1,812,443	3,330,379	2,237,433
-	-	-	-	-	-	-	-	-

*Note: Investment Income includes Earnings on Investments
**Note: Miscellaneous includes Grant Revenue, Miscellaneous, and Transfer In

USES OF FUNDS								
Expenses	**2011 CAFR**	**2012 CAFR**	**2013 CAFR**	**2014 CAFR**	**2015 CAFR**	**2016 CAFR**	**2017 CAFR**	**2018 CAFR**
Administration	-	3,542	18,749	29,398	47,187	69,621	126,937	110,413
Capital Outlay	-	1,840,679	-	-	-	-	-	-
Operations	209,817	145,206	182,426	146,051	88,934	170,476	623,213	660,978
Total Program Expenses	209,817	1,989,427	201,175	175,449	136,121	240,097	750,150	771,391
Total Project Expenses	-	-	214,016	7,386	72,203	97,554	1,196,180	2,148,520
Total Expenses	209,817	1,989,427	415,191	182,835	208,324	337,651	1,946,330	2,919,911

Source: City of Brighton Comprehensive Annual Financial Reports for the fiscal years 2011 through 2018

Audit Findings and Conclusions

Development of Annual Budgets Needs Improvement

The City's annual budget is the most important control over ensuring that funds are spent wisely and in furtherance of the public's interests. The budget process involves gathering stakeholder needs and priorities; presenting planned revenues and expenditures to City Council; authorizing spending; and recording spending limits in the accounting system to encumber funds. Funds that are allocated for specific projects are committed within the accounting system so that those funds are not spent on other items.

Because of the importance of the budget, the City's Municipal Code includes specific requirements for budget development and presentation. Section 3-4-20 of the Municipal Code states that:

> "All offices, departments, boards, commissions and other spending agencies of the City shall, on or before the first day of September of each year, prepare and submit to the City Manager estimates of their **expenditure requirements and their estimated revenues for the ensuing budget year**. The estimates of expenditures shall be classified so as to set forth the data by funds, character and objects of expenditure. The budget shall be segregated as to offices, departments, boards, commissions and other spending agencies. The revenue estimates shall be classified as to funds and sources of income."

We found that Water, Wastewater, and Storm Drainage budgets had not always been developed and presented to City Council in accordance with the Municipal Code. Specifically, Utilities' budgets were not restricted to requests for appropriations of the "ensuing year's" expenditures. Budgets included requests for authorizations of funding for multi-year planned projects. A complete listing of all projects and their actual and budgeted expenses will be provided under separate cover.

The water treatment plant had the largest budget-to-actual variance for both 2015 and 2016. We found that although construction for a water treatment plant was not scheduled to begin in 2015, the 2015 budget appropriation for the Water Fund included $18 million for a that project. The inclusion of the $18 million was thought by staff to demonstrate the City's intention to meet state and federal clean water requirements. We note, however, that the CIPs for 2015 through 2019 listed the water treatment plant as an "Unfunded Project." Specifically, the CIPs included costs for water distribution projects and water treatment projects, but they did not include the cost for the new water treatment plant. Additionally, planning for the water treatment plant project had not been completed, and the Utilities' staff was still evaluating solutions to meet the water quality requirements and the City's growing capacity needs. Tables that include the budget and actual expenditures by project for 2015 and 2016 are included on the following page.

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Water Fund: Budget to Actual Expenses Fiscal Year 2015

Project Number	Project	Total Revised Budget	YTD Expense
91480	Non Potable System	6,000	-
92011	Annual Utilities Rate Study		
93101	Non-Potable Diversion Flow Attenuation		
93102	South Platte Reservoir Upgrades	584,074	94,956
93104	South Platte Well Rep & Maintenance	197,399	
93105	Beebe Draw Well Rep & Maintenance	140,000	61,709
93106	Remote Site Rep & Maintenance	50,000	17,138
93107	Storage Tank Structural Repair	147,000	15
93108	Water Treatment Plant Construction	18,364,647	46,080
93109	Greensand Scaffolding Engineering	80,000	2,275
93110	Water Treatment Rep & Maintenance	68,000	52,625
93111	Roof Green Sand and RO Plant	203,500	187,929
93113	Distribution Infrastructure	169,075	22,147
93114	Water Master Plan	100,000	99,911
93115	Distribution Emergency Repair and Maint	100,000	-
93116	Distribution Line Replacement	1,227,999	-
93119	Alluvial Aquifer Exploration	10,000	-
93120	Mag Meter Install for Wells	55,000	-
93121	Water Treatment Emer Repair and Maint	100,000	41,701
93122	Ken Mitchell Cell 1 Upgrades	1,500,000	1,318,392
94041	Well 11 Design, Construction, Permitting	809,800	54,852
94060	Water Tanks	10,000	-
97800	Water Acquisition		
98410	Beebe Aquifer Monitoring Project	105,614	41,813
98420	148TH Ave Augmentation	546,540	497,770
98540	Metro Pumping IGA Project	180,000	171,624
98602	Water Meter Replacements & Upgrades	350,000	151,050
98900	Ken Mitchell Project	10,000	-
99010	Innoprise ERP Software (Water)	80,650	-
99930	Ken Mitchell 2015 Flood Damage	1,716,000	70
EPC	EPC Projects		
	Total Water Projects	**26,911,298**	**2,862,057**

Source: Project Expenses vs Actual data provided by the City of Brighton.

Because the total amounts budgeted in a given year exceeded actual spending needs by a large margin, staff carried over, or "re-budgeted", remaining authorized amounts for some projects. As an example, the 2016 unspent budget was rolled directly into the 2017 budget for 18 of the 36 Water Fund projects. Nine of the projects that were rolled from 2016 to 2017 had no need for budget authorization in 2017 and were subsequently dropped from the 2018 budget. Re-budgeted amounts contributed to the large variances between the annual budget and actual expenditures. Some of the rollover problems appear to be attributable to the lack of communication among various departments.

Water Fund: Budget to Actual Expenses Fiscal Year 2016

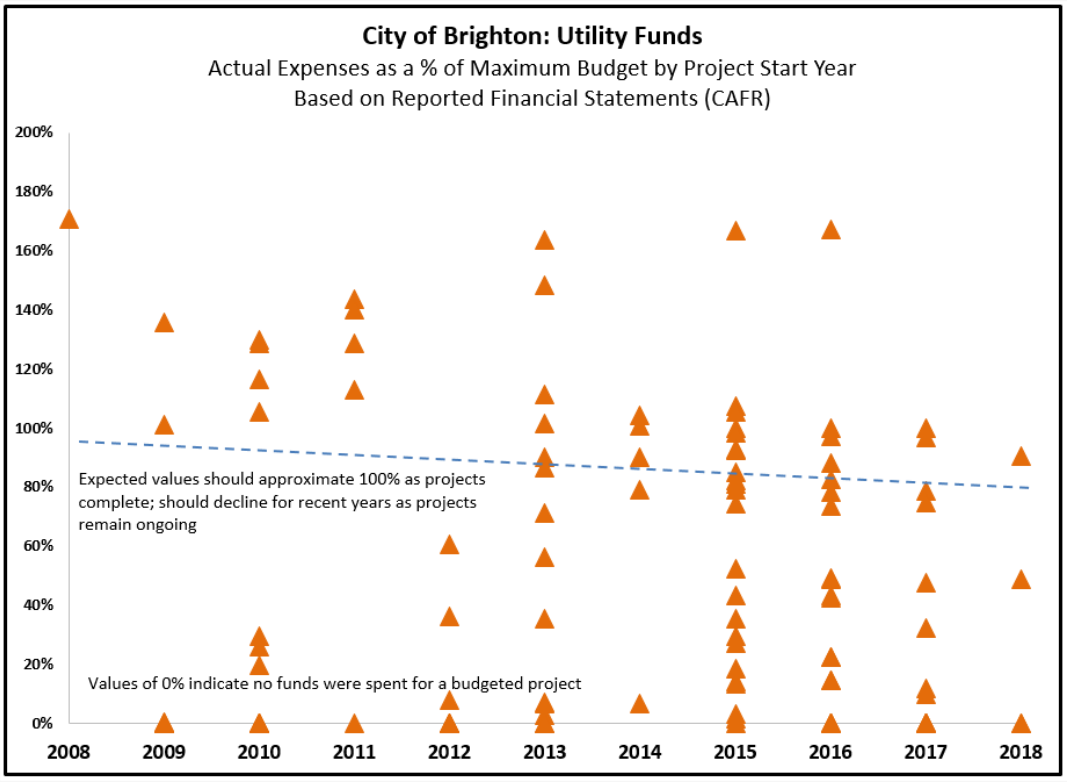
Project Number	Project	Total Revised Budget	Actual Expense
92011	Annual Utilities Rate Study	22,500	1,492
93101	Non-Potable Diversion Flow Attenuation	6,000	-
93102	South Platte Reservoir Upgrades	5,185,954	2,372,974
93104	South Platte Well Rep & Maintenance	289,399	25,812
93105	Beebe Draw Well Rep & Maintenance	78,291	-
93106	Remote Site Rep & Maintenance	130,214	1,473
93107	Storage Tank Structural Repair	658,985	64,977
93108	Water Treatment Plant Construction	18,325,747	69,298
93109	Greensand Scaffolding Engineering	405,000	52,197
93110	Water Treatment Rep & Maintenance	253,375	60,484
93111	Roof Green Sand and RO Plant	15,571	-
93113	Distribution Infrastructure	151,728	47,905
93114	Water Master Plan	169,660	138,382
93115	Distribution Emergency Repair and Maint	100,000	-
93116	Distribution Line Replacement	1,227,999	140,780
93119	Alluvial Aquifer Exploration	30,000	7,357
93120	Mag Meter Install for Wells	55,000	40,913
93121	Water Treatment Emer Repair and Maint	58,299	
93122	Ken Mitchell Cell 1 Upgrades	214,146	221,767
93137	Green Sand Plant Air Gap Project	140,000	31
93138	GPS Unit Purchase	15,000	13,247
93139	Beebe Draw Well Field Capacity Upgrades	1,700,000	-
93140	Asset Management Software	15,000	
94041	Well 11 Design, Construction, Permitting	754,948	-
94060	Water Tanks	10,000	-
98410	Beebe Aquifer Monitoring Project	63,800	-
98420	148TH Ave Augmentation	128,962	(1,108)
98602	Water Meter Replacements & Upgrades	198,950	46,259
98701	Water Meter Upgrades (AMR)	913,000	-
98702	Distribution Infrastructure Upgrades	160,000	40,080
98703	Distribution Line Purchase and Install	1,000,000	-
98704	Utilities Shop Repairs	8,750	-
98708	Supplemental Water CL17 Installation	85,000	-
98709	Utilities Heavy Duty Equipment	227,000	164,990
98900	Ken Mitchell Project	10,000	
99010	Innoprise ERP Software (Water)	80,650	-
99930	Ken Mitchell 2015 Flood Damage	1,715,930	1,196,252
EPC	EPC Projects	828,228	425,735
	Total Water Projects	**35,433,086**	**5,131,297**

Source: Project Expenses vs Actual data provided by the City of Brighton.

The Brighton Municipal Code, as well as codes in other state and local governments, requires that budgets be restricted to the "ensuing" fiscal year to ensure that spending is limited to the amount authorized. Out-year funding for long-term projects can be disclosed, designated or restricted in the CIP and the financial statements.

In addition to significant budget to actual variances, we also found the total costs by project had high variances from the estimated cost. The chart below shows the variance for each project's estimated cost to the total actual expenses. The vertical axis shows the percent the total actual expenditures from 2009 to 2018 for a given project varied from the maximum budgeted expenditures for that project. We used the maximum budgeted expenditures because that was the most representative figure for the projected total cost of the project. The horizontal axis shows the first year that the project had either a budgeted amount or actual expenditures. For the years 2013 through 2018, the actual versus authorized variances were as much as almost 100 percent on several projects.

All Funds: Project Expected Cost vs Actual Costs



Source: Two Hills Accounting's summary of the City's 2011 to 2018 general ledger and CAFR.

While our test work did not identify unreasonable or unallowable expenditures, we note that a budget that authorizes spending well above amounts needed to fund capital projects, operations and maintenance expenses provides the opportunity for wrongdoing.

Any concern about authorizing too little to meet the Utilities' needs can be addressed through the formal budget amendment process. The process increases transparency and enhances budgetary controls.

> "In amending the budget, the City Council may add or increase programs or amounts and may delete or decrease programs or amounts except those expenditures required by law, for debt service or for estimated cash deficit. Such amendments shall not increase the total expenditures for the overall budget as presented at the public hearing. If such amendment does increase the total expenditures, then another public hearing shall be held prior to adoption of the budget." [Brighton Municipal Code Section 3-4-40b]

Recommendation:

We recommend:

- Strengthening existing practices for budget development and project review.
- Providing both on the job and classroom training on budgets for those with budget development or approval responsibility.
- Ensuring communication among staff involved in budget development.
- Apportioning expenditures on a year-to-year basis to allow for effective comparison of annual expenditures to budgeted amounts for long-term project budgets.

Management Response:

City staff agree. Process changes to follow these best practice recommendations were implemented beginning in July 2019 with the development of the 2020 budget.

- In June and July 2019, Finance staff met with department directors to discuss current year projections for operating and capital spending in comparison to Council's amended budget, and Department Directors submitted their 2020 recommended spending plan for their department.
- In August 2019, the City Manager and Finance staff met with Department Directors, Division Managers, Engineers and Project Managers to vet the recommended 5 year CIP plan for capital project funds and review operating and personnel requests.
- In early September 2019, Finance staff met with the City Manager to finalize recommendations for the 2020 budget and 5-year CIP plan to present to City Council.
- At the all-day study session on September 9, 2019, Finance staff presented the City Manager's 2020 proposed budget and 5-year CIP recommendation to City Council.
- During the months of October and November 2019, Finance staff incorporated feedback from the Mayor, City Council and the City Manager to refine and prepare the final budget for 2020, and met with Department Directors to cull the capital project spending down to apportion expenditures for the coming year with a "shovel ready" mindset, ensuring project spending requested of City Council for 2020 could be accomplished in 2020. Additionally, capital project costs were presented in the 2020 Budget Book on a year by year basis to help City Council and residents understand the total estimated cost of a project, time to complete, and anticipated spending by year. Following is an example of a project as presented in the 2020 Budget Book:

South Storage- Storm Drainage Improvements		**Project #:** 502035
Project Duration: 2020-2021	**2019 Carryover:**	-
Total Cost: $850,000	**2020:**	$50,000
Funding Source(s): Water User Fees	**2021:**	$800,000
Description: Fix erosion problem at the south tank site.	**2022:**	-
	2023:	-
	2024:	-

- On December 3rd, 2019, at a public hearing, Finance staff presented the budget for Council's formal consideration and Council approved the 2020 Budget resolution as presented with a unanimous 8-0 vote.
- In January 2020, Finance staff conducted several trainings for staff at all levels of the budget process. Finance launched a new capital budgeting and tracking process and hosted training sessions with project leads, admins, and directors on budget and procurement requirements as well as introduced online resources and tutorials for reference throughout the year.
- In February 2020, a similar roll-out was conducted for the new grant process. Grant leads, directors, and admins were present at these trainings which introduced the new grant budgeting, tracking, and procurement process. A grant portal was also created including resources and tutorials that can be used throughout the year. The Budget and Procurement teams are also scheduled to provide training on procurement and tracking of spending in the Emergency Operations Center on March 25th, 2020.

Recording and Reporting Systems Need to be Improved

As part of this engagement, we were asked to evaluate reports on operating versus growth revenues and expenditures. Such reporting is important in rate setting and budget development. We found that information provided to decision makers on operating versus growth revenues and expenditures has been inconsistent and unreliable. Neither we nor staff have been able to generate consistent and reliable reports, because the City's systems do not uniformly contain information on specific projects and subtasks. In addition, the basis for significant estimates has been neither documented nor publicly disclosed. For example, we were not able to obtain a comprehensive description of each project along with the impact that the project would have on existing operations and the increased capacity to the system.

Using judgement and estimates, staff have generated ad hoc reports allocating operating and growth revenues and expenditures, but the reports have not all been consistently prepared and maintained. Documentation to prepare reports has to be compiled from a variety of sources, including estimates, rate studies, the general ledger, and ad hoc memos and documentation.

Rate consultants need to have consistent and reliable information, particularly on large projects. During the rate study process, City staff provide a current asset listing, the historical capital contributions from developers, and the capital improvement plan for at least the next 10 years to the rate consultants. Additional information for the rate study includes the current operations and maintenance costs, the estimated operating and PIF balances, and the projected population growth. Based on the information provided by staff, consultants determine the appropriate charges for services and plant investment fees for the upcoming year.

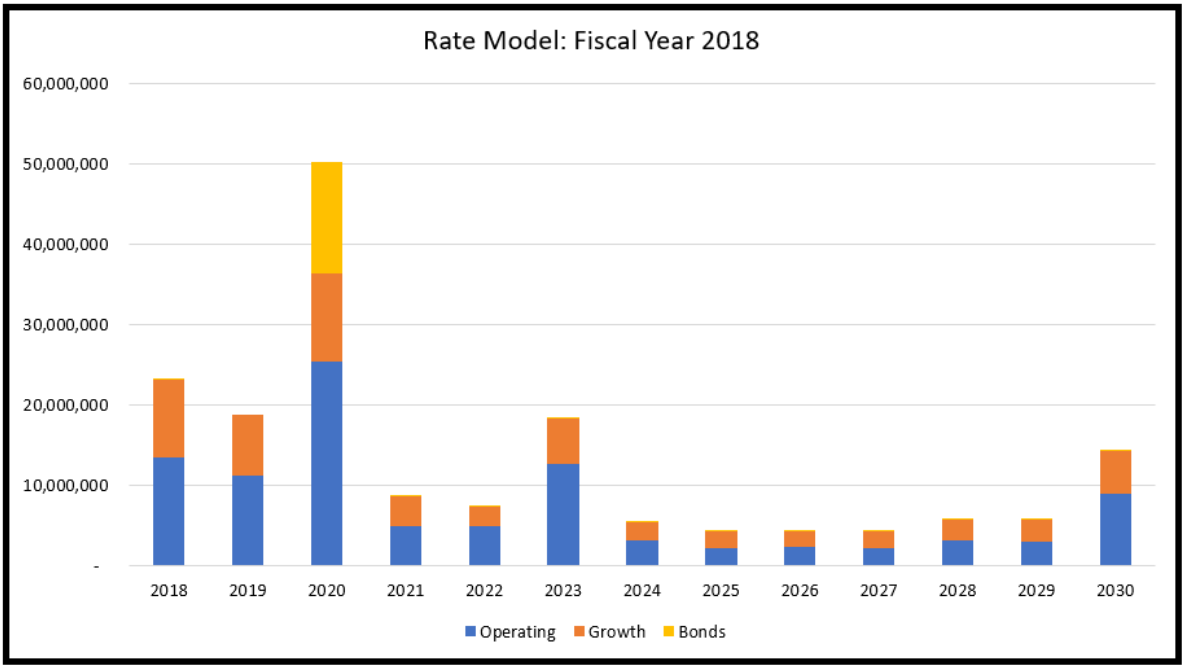
The CIP includes the projects that will be completed over the coming 10 to 30 years, the projected cost of each project by year, and the allocation between growth and operations for each project. The allocation between growth and operations is based on whether the project will increase the capacity of the system (growth) or maintain/improve the current

system (operations). The CIP is a living document that is updated based on the latest needs of the City. For example, if the engineering team discovers that a main component of the City's water system is close to failure, the CIP should be updated to include the associated costs.

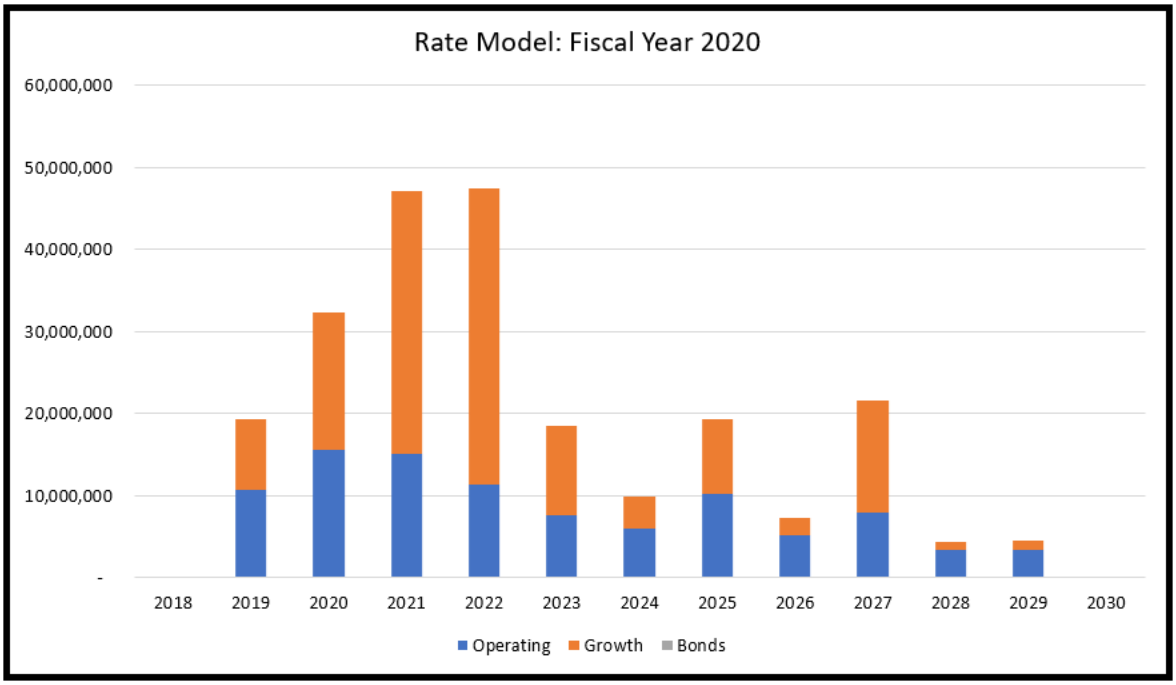
While the CIP is a living document and needs to be changed based on the latest information, large changes to the CIP can result in significant changes to consumer rates. We found that the rate models for the 2018 and 2020 fiscal years had large differences in the proposed projects, the cost of those projects, and the allocation between growth and existing operations. The charts on the following pages show the costs included in the two models; demonstrate significant differences in the costs by year; and illustrate the allocation between growth and operations. The differences are most likely caused by changes to multiple projects' scopes, varying estimates, and additional data provided by staff.

The charts on the following pages illustrate the total capital improvement plan costs by year included in the 2018 and 2020 rate models. The costs are separated by operating and growth based on the allocation percentage specified in the capital improvement plan.

Capital Improvement Plan Costs Included in Selected Rate Models



Source: Two Hills' summary of CIP data provided by Brighton staff to Willdan for the FY 2018 rate model.



Source: Two Hills' summary of CIP data provided by Brighton staff to Stantec for the FY 2020 rate model.

The following table summarizes the total capital costs allocated to operations and growth for the 10-year period from 2019 to 2028 in the two rate models. The operating costs grow by approximately 16 percent, and the costs for the expansion of City infrastructure grew by approximately 180 percent.

CAPITAL IMPROVEMENT PLAN COSTS SUBMITTED FOR RATE MODEL			
Allocation	**2018 Rate Model 10 Year Total 2019 to 2028**	**2020 Rate Model 10 Year Total 2019 to 2028**	**% Change**
Operating *	79,955,199	93,000,393	16.32%
Growth *	47,889,481	134,340,829	180.52%
Total	**127,844,680**	**227,341,222**	
* The operating and growth allocations include capital costs to be paid by the issuance of bonds. Per the rate study, the total bonds issuance was projected to be $13.9 million. 53.8% of the bonds were allocated to operating and 46.2% were allocated to growth.			

Source: Two Hills' summary of CIP data provided by Brighton staff to Stantec for the FY 2020 rate model.

The largest costs included in the CIP relate to the Greensand Water Treatment Plant (Project Code 93018). The table below shows the total costs allocated to existing operations and growth for the Greensand Water Treatment Plant for the two rate models:

Classification	FY 2018 Rate Model	FY 2020 Rate Model
Operating	16,340,920	8,560,000
Growth	7,549,080	63,640,000
Total	**23,890,000**	**72,200,000**

The Fiscal Year 2020 model includes $30 million for a water softening project to be completed in 2021 and 2022 that was allocated 100% toward growth. The result was an increase in the PIF fee from $11,040 to $13,346 (21%) and no change to consumer rates. Based on our review of the presentation of the project in the fall of 2019 to City Council, it appeared that the softener project would impact both existing water consumers and new water consumers.

Through our interviews, we found that the City was required to improve their plant's filtration system to meet Colorado Department of Health and Environment (CDPHE) requirements. Beginning in 2013, the City's Utilities division began developing solutions to

improve the filtration to meet the updated regulations. Due to changing regulatory requirements, City priorities, and staff turnover, the solutions to both upgrade the existing facility and increase capacity changed over time. While some change in the allocation between growth and existing operations is understandable, we did not find sufficient justification for the allocation between growth and existing operations for the water treatment plant.

Because of the changes in both the cost and the allocation between growth and operations, there were substantial increases to the plant investment fees. We want to emphasize that because of the dynamic nature of utilities projects, in which the engineering team may not know the full extent of the project until the construction team has broken ground, there can be a need to adjust growth and operating data as more information becomes available. However, in the interests of transparency, we believe that staff should document the basis of estimations used and the reasons for any changes in estimation methodologies.

Recommendations:

We recommend that a user group comprised of Utilities and Finance staff evaluate the current allocation methodologies to determine where improvements can be made. In addition, we recommend:

- A review of policies and procedures regarding the capital improvement plan, in particular related to the assignment of growth and allocation percentages.
- City Council approval of capital improvement plan cost changes in excess of 10%.
- City Council approval of the allocation between growth and existing operations for projects that account for over 10% of the capital improvement plan for the following 10 years.

Management Response:

City staff agree, it is important for City Council (policy makers and the rate setting body) to consider and approve allocations between growth and existing operations for projects that account for over 10% of the capital improvement plan, and it is important to engage the

rate consultant and do a financial check-in on the 10 year capital improvement plan if costs change more than 10%.

- City staff will continue the practice of presenting all capital improvement plan cost changes, regardless of cost difference, at the fall budget forum and budget hearing.
- At the fall 2020 budget forum (work study session with City Council to review the City Manager's 2021 budget recommendation), staff will present and take Council's direction on the allocation between growth and existing operations for projects that account for over 10% of the 10 year capital improvement plan in the utility funds.
- Moving forward, staff will recommend City Council engage a rate consultant to review the current and planned future rates and plant investment fees when there is a change of 10% or more in the 10-year capital improvement plan.

Controls Over the Procurement System Need Improvement

Controls over the City's procurement system are essential to prevent fraud, waste and abuse. Key controls include separation of duties, limited access to automated systems, periodic internal audits, and approval authority. The American Institute of Certified Public Accountants (AICPA) says that:

> "Effective internal controls reduce the risk of asset loss and helps ensure that plan information is complete and accurate, financial statements are reliable, and the plan's operations are conducted in accordance with the provisions of applicable laws and regulations."

The City has millions of dollars flowing through its procurement systems. It cannot risk the financial and reputational risk of losses caused by insufficient controls.

As noted earlier in this report, we were not engaged to conduct a comprehensive audit of internal controls. However, during the course of our test work, we identified areas where improvements in the procurement system are needed. Specifically, we found that access to the master vendor list is not sufficiently limited and unique vendor numbers are not consistently and appropriately used.

Because of ineffective controls limiting access to and modification of the master vendor list, we found that individual vendors were included multiple times with different identification numbers in the accounting system. The lack of a single unique identifier for each vendor leads to confusion: when faced with four vendor records, all of which contain the same name and address, it can be difficult for the staff member to determine the appropriate vendor. It can also lead to duplicate payments, where the same invoice is erroneously paid multiple times. Lack of controls over the master list provides an opportunity for fraud, waste, or abuse, including the addition of ghost vendors that allow for phony payments.

We performed analytical procedures to identify potential duplicate payments and/or transactions with vendors at suspicious addresses. Based on our analytical analysis, we reviewed the underlying transactions for approximately 40 vendors. We did not identify suspicious activity or duplicate payments in our sample. We also retrieved documentation

and performed additional analytical procedures where we identified overlap between addresses. We did not identify transactions that we believe represent phony payments or ghost vendors.

In addition to single vendors existing multiple times, we identified situations where payments to many different vendors flowed through a "one-time vendor" code. Because the system has allowed this single vendor to process different vendors, the approval of several vendors currently in the system has not occurred. We reviewed documentation related to these transactions and did not identify any that were erroneously paid. However, we believe that the lack of unique identifiers increases the risk of fraud, waste, or abuse.

An up-to-date master vendor list containing unique identifiers for each vendor is important to ensure the proper payment of invoices and the subsequent tracking of vendor payments. For example, with a structurally sound vendor list, reports can be run to determine if a vendor has been paid in excess of certain procurement thresholds over the course of a year. The vendor file is the central repository of contact and payment information for all contractors and entities providing goods and services to the City. The accounting system should contain unique identifying numbers for vendors, enabling tracking and review of payments, regardless of which department requested goods or services. Effective tracking of vendors and vendor invoices is important to ensure that an invoice for multiple services does not get paid twice when received by different departments.

We believe that the lack of adequate controls over procurement systems was caused by insufficient automated controls over adding vendors to the master file and changing the information in the file; inadequate policies and procedures regarding adding and changing vendors; lack of sufficient periodic internal audits over procurement; and insufficient on the job and classroom training.

Recommendations:

We recommend:

- Evaluating policies and procedures to ensure adequate controls over the master vendor list.
- Conducting sufficient internal audits of compliance with policies and procedures, including sample testing of transactions to ensure the accuracy and integrity of payment systems.
- Increasing on the job and classroom training.
- Developing automated access controls to the City's master vendor list and eliminating the use of "one-time vendor" codes for multiple transactions.
- Performing a comprehensive review of the City's vendor list, including designating as "inactive" all duplicative vendor names and numbers.

Management Response:

City staff agree and began implementation of these recommendations in July 2019.

- City Management recognized the need to expand and improve the skill level in the Finance Department. Maria Ostrom joined the City in late May 2019 as a financial consultant to oversee several projects and professional development of staff. Ms. Ostrom is a CPA with a Master's degree in Accounting and over twenty years of municipal finance experience in the Denver metro area. Acting City Manager Marv Falconburg appointed Ms. Ostrom to the position of Director of Finance in September 2019. Over the past few months, Brighton has successfully recruited eight experienced Finance staff including a new accounting manager, budget manager, and tax supervisor.
- In July 2019, the process began to evaluate all finance policies and procedures to ensure adequate controls over the master vendor list as well as the system of internal controls.

- In September 2019, Finance staff completed cash drawer counts and petty cash reviews for all locations within the City.
- As of October 2019, view access to vendor tax ID numbers was limited to Finance staff only.
- In October 2019, the City began implementation of a new purchasing card system which will significantly limit the need to use the one-time vendor classification. Moving forward, the one-time vendor classification will be used for building permit and utility billing refunds. The City expects to convert all departments by the end of May 2020. During the implementation phase for each department, Finance staff review the purchasing card utilization over the past year and adjust the card user's daily and monthly limit based on need and usage.
- In November 2019, Finance staff began auditing IT equipment and software and developed a financial planning tool for lifecycle replacement.
- In November 2019, Finance staff began auditing fleet throughout the City and will make recommendations to the City Manager on reductions and changes based on utilization, maintenance and fuels costs and overall requirements and fit for the activity.
- As of December 2019, access to change or add a vendor was restricted to Procurement staff through log-in security in the general ledger system. Also in December 2019, 3,071 vendors were made inactive and the City obtained a current W-9 from every active vendor to ensure accurate information is on file.
- In January 2020, Finance staff began an FTE audit to evaluate optimal staffing and efficient cost-effective use of taxpayer resources. Staff will make recommendations to the City Manager and Department Directors for possible changes prior to the start of the 2021 budget process.
- Beginning April 2020, Finance staff will conduct annual p-card audits to ensure users are following purchasing card policies.

- Beginning June 2020, Finance staff will conduct annual physical capital asset audits of movable equipment and machinery. Capital assets will be selected by systematic sample of in-use assets. The sample will be designed so that each in-use moveable asset is physically observed at least once every three years.