



Friedman Recycling Contract Follow-Up Audit A2014-03 Report

Issued by the
Internal Audit Office
March 17, 2014

**City of El Paso
Internal Audit Office
Friedman Recycling Contract Follow-Up Audit A2014-03**

EXECUTIVE SUMMARY

The Internal Audit Office conducted a Follow-Up Audit of the Friedman Recycling Contract Audit Report dated August 31, 2011. The original Audit Report contained five findings. Upon completion of the audit fieldwork, we have determined the status of the recommendation for each audit finding as outlined in the table below:

Finding No.	Description of Findings	Status
1	In Sections 2.1.1.1.1a. and 3.12.2 of the Amendment, payment terms were calculated using 12 years. This contradicts the Amendment effective date and termination date, which is 11 years.	Implemented
2	Friedman Recycling Co. has not provided the City of El Paso a Performance Bond.	Implemented
3	Environmental Services has not been providing for the disposal of the first 1,000 tons of contaminants/residuals at the Clint Landfill to Friedman Recycling Co. free of charge since 2007.	Implemented
4	As part of the negotiations to the Amendment, the City applied \$709,902.00 in credit for equipment purchases made by Friedman towards Friedman's "consideration" owed to the City. The Single Stream Curbside Recycling Contract is "silent" as to who retains ownership of the equipment at end of contract. In addition, there is no verbiage in the Contract that addresses the disposal/clean-up costs associated with the equipment in the event the contract goes full term and does not terminate early.	Implemented
5	Environmental Services has not implemented a process to request and review the annual report identifying Friedman's public recycling educational/outreach program expenditures that is to be provided by Friedman Recycling Co.	Implemented

For a detailed explanation of the findings and current observations please refer to the appropriate finding contained in the body of this Audit Report.

BACKGROUND

The City of El Paso awarded Contract No. 2006-015, *Single Stream Curbside Recycling Collection and Processing Services for Environmental Services Department*, to Friedman Recycling Co. on February 14, 2006.

An “Addendum” to the City of El Paso, Invitation for Bids, *Single Stream Curbside Recycling Collection and Processing Services* was executed effective June 26, 2006 between the City of El Paso and Friedman Recycling of El Paso, LP. The Addendum revised the period of performance from April 22, 2007 through April 21, 2022 (fifteen years), and clarified the terms and conditions of the original bid solicitation, amendments to solicitation, and the successful bid.

A “First Amendment to Addendum” was developed in order to modify the revenue sharing language, accept new considerations, and expand the residential curbside recycling program by including additional recyclables. The said Amendment (Version 5) was initially presented to City Council on February 22, 2011. The Amendment proposed to replace a pending payment of \$2,426,740.00 with considerations implemented or to be implemented by Friedman Recycling of El Paso, LP; the amendment was postponed for further review. On April 12, 2011, City Council was presented with Version 6 of the Amendment proposing considerations for a payment due of \$2,499,332.12. City Council requested additional options. Two additional options were presented by Environmental Services in lieu of the considerations provided in the Amendment. City Council passed “Option 3” which was the most conservative option of the three. City Council agreed to \$1,026,412.44 in considerations with a cash payment of \$1,472,919.68 for a total of \$2,499,332.12.

AUDIT OBJECTIVES

The audit objective was to ensure that corrective action was taken by management to address the recommendations detailed in the original Audit Report dated August 31, 2011.

AUDIT SCOPE

The audit period covered the operations of Fiscal Year 2013 – 2014.

AUDIT METHODOLOGY

To achieve our audit objectives we:

- Conducted interviews with Environmental Services Department management and staff,
- Verified that the income received by Environmental Services is consistent with contract terms and revised payment schedule,
- Verified that Environmental Services resumed providing credit for the disposal of the first 1,000 tons of contaminants/residuals to Friedman Recycling Co. per contract year.
- Reviewed policies and procedures in place by Environmental Services to review and monitor Recycling Program income streams and third party contributions,
- Obtained and reviewed Performance Bonds provided by Friedman Recycling Co.
- Verified that Environmental Services established an agreement with Friedman Recycling Co. regarding the ownership and liability of equipment.

We conducted this performance audit in accordance with Generally Accepted Government Auditing Standards. Those 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 our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

This audit was also conducted in conformance with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors.

**SIGNIFICANT FINDINGS, RECOMMENDATIONS,
AND MANAGEMENT’S RESPONSES**

The definition of a significant finding is one that has a material effect on the City of El Paso’s financial statements, identifies an internal control breakdown, a violation of a City procedure, or a violation of a law and/or regulation, which the City is required to follow. Any finding not meeting these criteria will be classified as an “Other Finding”.

Finding: 1

Amendment Calculations

In two sections of the Amendment, payment terms were calculated using 12 years (144 months) instead of 11 years (132 months):

- Section 2.1.1.1.1a. states, “Contractor shall provide a minimum amount of ONE THOUSAND DOLLARS and NO/100 (1,000.00) per year for the remaining twelve years of the Contract term for an Environmental Summit.”
- Section 3.12.2 states, “The Pending amount of \$1,472,919.68 due to the City from Contractor...will be repaid over the remaining twelve years of the Agreement, to commence upon execution of this Amendment, with a monthly payment of \$10,228.60.”

As a result of this miscalculation, \$122,743.20 will still be due at the conclusion of the Single Stream Curbside Recycling Contract. See calculation below:

	Formula used in Amendment to calculate monthly payment amount	Actual payments that will be made from the effective date of the Amendment (April 27, 2011) to the expiration date of the Contract (April 21, 2022)	Payment amount that will be remaining at the conclusion of the Contract
Number of years	12	11	1
Number of years/months	144	132	12
Monthly Payment Amount	\$ 10,228.60	\$ 10,228.60	\$ 10,228.60
Total Payment Amount	\$ 1,472,918.40	\$ 1,350,175.20	\$ 122,743.20

* Note total payment amounts may be off a few cents due to rounding.

Recommendation:

Environmental Services should ensure that Friedman Recycling Co.’s pending amount due is paid in full by the conclusion of the *Single-Stream Curbside Recycling Processing Services Contract*.

**City of El Paso
Internal Audit Office
Friedman Recycling Contract Follow-Up Audit A2014-03**

Management's Response

In an effort to eliminate any pending amount due the City of El Paso at contract end, Friedman Recycling Co. has agreed to forego annual credits for the 1,000 tons of residuals each year until the amount is paid in full. The payment schedule is as follows:

Pending amount at contract termination:	\$122,743.20	Remaining Balance
Credit for landfill fees due 3/31/09	\$26,000.00	\$96,743.20
Credit for landfill fees due 3/31/10	\$26,000.00	\$70,743.20
Credit for landfill fees due 3/31/11	\$26,000.00	\$44,743.20
Credit for landfill fees due 3/31/12	\$26,000.00	\$18,743.20
Credit for landfill fees due 3/31/13	\$18,743.20	\$-0-

If gate fees remain constant at \$26.00 per ton, the department will credit Friedman Recycling \$7,256.80 on 3/31/13 and the full 1,000 ton gate rate each year thereafter. The monthly remittance amounts stated in the contract will remain unchanged.

Responsible Party

Deborah Strom, Department Administrative Manager

Implementation Date

Contractor agreed to these terms on 10/5/2011. Pending amount due at contract end will be extinguished by 3/31/2013.

City of El Paso
Internal Audit Office
Friedman Recycling Contract Follow-Up Audit A2014-03

Current Observation

- Friedman Recycling has adhered to the Revised payment schedule outlined in the Amendment.
- During the course of the Follow-Up Audit, Environmental Services with the assistance of the Internal Audit Office conducted a reconciliation of the “catch-up” payments received from Friedman Recycling.

As of January 30, 2014, Friedman Recycling made a total of 34 payments totaling \$347,832.40 toward their pending amount due. 98 monthly payments of \$10,228.60 are still pending, with the last payment due in March 2022.

In order to ensure that Friedman Recycling Co.’s pending amount due is paid in full by the conclusion of the *Single-Stream Curbside Recycling Processing Services Contract*; Environmental Services needs to take a proactive approach to the monitoring of Friedman Recycling Contract payments.

Status

Implemented

Finding: 2

Performance Bond

The Single Stream Curbside Recycling Collection and Processing Services Solicitation No. 2006-015 Section C.I. Performance Bond states:

*“The Offeror, if awarded a Contract, shall provide a Performance Bond or irrevocable, direct pay Letter of Credit to be approved by the City conditioned upon the true and faithful performance of the Contract in an amount of \$2 million in the first year of the Contract. **The amount for each succeeding year shall be inflated by the Consumer Price Index**, and the Performance Bond or Letter of Credit shall be renewed by the Contractor and maintained throughout the term of Contract. After the Contractor successfully completes the Contract to the City’s satisfaction, the City will release the performance bond or letter of credit.”*

Friedman Recycling Co. has not provided the City of El Paso a Performance Bond or irrevocable, direct pay Letter of Credit.

Recommendation:

The Environmental Services Department needs to ensure that Friedman Recycling Co. provides a Performance Bond in accordance with Solicitation No. 2006-015 *Single Stream Curbside Recycling Collection and Processing Services*.

Management's Response

Environmental Services has secured a commitment from the contractor, Friedman Recycling Co., to secure a performance bond. A copy will be delivered to the City of El Paso's Purchasing and Environmental Services departments. It is anticipated that such bond will be available within 90 days.

Responsible Party

Deborah Strom, Department Administrative Manager

Implementation Date

January 9, 2012

Current Observation

- Friedman Recycling submitted a \$2 million Performance Bond for 2012 and a Continuation Certificate for 2013. The annual Performance Bond was not being inflated by the Consumer Price Index (CPI) as required by the *Single Stream Curbside Recycling Collection and Processing Services* Solicitation No. 2006-015 Section C.I. Performance Bond.
- Environmental Services calculated the 2014 Performance Bond to include the CPI inflation with compounding since 2007 when the compounding should have begun. Environmental Services presented the revised Performance Bond amount of \$ 2,252,356.00 to Friedman Recycling. The 2013 Performance Bond Continuation Certificate expired on February 9, 2014.
- On March 7, 2014 Friedman Recycling provided Environmental Services with their 2014 Performance Bond Continuation Certificate in the amount of \$2,255,978.53.

In order to ensure that Friedman Recycling Co. provides a Performance Bond in accordance with the *Single-Stream Curbside Recycling Processing Services* Contract; Environmental Services needs to take a proactive approach to the monitoring of the annual Performance Bond amounts.

Status

Implemented

Finding: 3

Landfill Fees

According to Section C.I. of Solicitation No. 2006-015, “*The City will provide or pay for the disposal of the first 1,000 tons of contaminants/residuals during each year of the Contract at the disposal site of the City’s choosing.*”

Environmental Services has not been providing for the disposal of the first 1,000 tons of contaminants/residuals at the Clint Landfill free of charge to Friedman Recycling Co. since 2007. In calculating Friedman Recycling Co.’s total amount due for Amendment Section 1.01, Environmental Services did not factor that a total of \$78,000 in landfill fees should have been waived for 2008, 2009, and 2010.

Recommendation:

Going forward from the effective date of the Amendment, Environmental Services should ensure that it provides a credit for the disposal of the first 1,000 tons of contaminants/residuals to Friedman Recycling Co. per contract year.

Management’s Response

Credit for 1,000 tons (\$26,000) was issued in the first contract year when the Friedman Recycling Co. was compliant with the contract and was paying for landfill services provided. When Friedman Recycling Co. defaulted and failed to remit landfill fees, the department did not issue credit. Due to the contract calculations resulting in a pending unpaid balance at contract end, and in agreement with the contractor, the department has applied the credits at year two, 3/31/09, year 3, 3/31/10 and year 4, 3/31/11, to offset the pending amount due at contract termination. The department will also be applying the 2011, 2012 and a portion of the 2013 credits against the outstanding pending balance referenced in Finding 1. When the pending unpaid balance is extinguished the department will resume full credit of the 1,000 tons per year at the applicable gate rate.

Responsible Party

Deborah Strom, Department Administrative Manager

Implementation Date

Partial credit will be given with the 2013 anniversary with full credit thereafter.

**City of El Paso
Internal Audit Office
Friedman Recycling Contract Follow-Up Audit A2014-03**

Current Observation

- Friedman Recycling has adhered to the Revised payment schedule outlined in the Amendment and in Finding #1.
- Friedman Recycling agreed to forego annual credits for the 1,000 tons of residual each year until the unpaid balance of \$122,743.20 was paid in full. With the gate fees remaining at \$26.00 per ton, Friedman Recycling was to receive a partial credit of \$7,256.80 on 3/31/2013 and \$26,000.00 each year thereafter.
- On 2/19/2014, Environmental Services issued a credit to Friedman Recycling Co. in the amount of \$7,256.80 for landfill fees due on 3/31/2013. The \$26,000.00 landfill credit for 2014 is due on 3/31/2014.

Status

Implemented

**REGULAR FINDINGS, RECOMMENDATIONS,
AND MANAGEMENT'S RESPONSES**

Finding: 4

Equipment Concessions

When concessions are made for items of value, it is common practice to identify who retains ownership of the items.

As part of the negotiations to the Amendment, the City applied \$709,902.00 in credit for equipment purchases made by Friedman towards Friedman's "consideration" owed to the City.

- The cost of the equipment was based on an estimate. Installation of the equipment was performed by Bulk Handling Systems (BHS), whom provided Friedman Recycling with an estimated fair market value of the equipment that was installed.
- The Single Stream Curbside Recycling Contract is "silent" as to who retains ownership of the equipment at end of contract. In addition, there is no verbiage in the Contract that addresses the disposal/clean-up costs associated with the equipment in the event the contract goes full term and does not terminate early.

Recommendation:

- Environmental Services should consider establishing an agreement with Friedman Recycling Co. regarding the ownership and liability of the equipment in question.
- In the event concessions are made in the future for equipment purchases, Environmental Services should obtain proof of purchase and identify who will retain ownership of the equipment at the end of the contract.

Management's Response

Although not specifically stated in the contract amendment, both Friedman Recycling Co. and Environmental Services understood that the ownership and liability of the equipment would remain with Friedman Recycling Co. at contract end. This understanding will be documented in memo form as it was inadvertently omitted from the contract language. Should the contract require amendment this language will be added, however, amendment is not anticipated at this time.

Responsible Party

Ellen Smyth, Environmental Services Director

Implementation Date

10/24/2011

Current Observation

- No additional concessions have been made since the completion of the original Friedman Recycling Contract Audit in 2011.
- A memorandum was prepared by Environmental Services to address the ownership and liability of the equipment in question. The Memorandum was referred to the City Attorney’s Office on February 17, 2014 for approval.
- After consultation with the City Attorney’s Office, it was determined that there is no need to document who retains ownership of the equipment. The original contract and the Amendment to the Addendum do not describe any type of City ownership interest in the equipment.

Status

Implemented

Finding: 5

Monitoring of Educational/Outreach Expenditures

According to the First Amendment to Addendum to City of El Paso, Invitation for bids, Single Stream Curbside Recycling Collection and Processing Services for Environmental Services Department Bid No. 2006-015” Section 1.02:

- Subsection 2.1.1.1.1a. *“Contractor shall provide a minimum amount of one thousand dollars per year for the remaining twelve years of the Contract term for an Environmental Summit.”*
- Subsection 2.1.1.1.2 *“As a condition precedent to the City crediting the following against the pending consideration owed by Contractor to the City, Contractor shall also contribute the amount of \$37,000 from its local corporate public relations contract towards a regional campaign to encourage recycling.”*
- Subsection 2.1.1.1.3 *“Contractor shall provide to the City an annual report of Contractor’s public recycling educational/outreach program expenditures stemming from this Contract.”*

Environmental Services has not implemented a process to request and review the annual report that is to be provided by Friedman Recycling Co. identifying Friedman’s public recycling educational/outreach program expenditures.

Recommendation:

Environmental Services needs to ensure that:

- Friedman Recycling Co. provides an annual report identifying their educational/outreach program expenditures,
- A monitoring system is implemented to ensure that these third party contributions are in fact made by Friedman Recycling Co.

Management’s Response

Annually, Friedman Recycling Co. will provide the department with a copy of the canceled check as proof that they provided support for Environmental Summit. Contractor has also agreed to provide documentation showing the public relations regional campaign costs in excess of \$37,000. Documentation will be reviewed by ESD financial staff for accuracy and contract compliance.

There are no *educational/outreach program expenditures stemming from this Contract*. The \$1,000 annual contribution towards an Environmental Summit (Subsection 2.1.1.1.1a) is the primary outreach program included in the contract. As previously stated, the Contractor will provide annual documentation of contributions for an Environmental Summit. Consequently, this contract does not require educational/outreach program expenditures, thus the contractor is not required to provide annual spending reports.

Responsible Party

Deborah Strom, Department Administrative Manager

Implementation Date

Documentation anticipated by 11/1/2011

Current Observation

- Friedman Recycling did not provide an annual report to Environmental Services identifying their education/outreach program expenditures. Copies of annual contributions to the Environmental Summit were obtained by Environmental Services during the completion of the audit.
- Friedman Recycling has been “providing a minimum amount of ONE THOUSAND DOLLARDS AND NO/100 (\$1,000.00) per year...for an Environmental Summit.” The following contributions have been made by Friedman Recycling to Keep El Paso Beautiful since the effective date of the Amendment:

Contribution Check Date	Amount
9/8/2011	\$1,000.00
9/12/2012	\$1,000.00
8/9/2013	\$1,500.00

- The Internal Audit Office confirmed that Friedman Recycling paid a total of \$39,584.26 to Suzanne Michaels Communications for a regional campaign to encourage recycling during the period of February 2011 to June 2013.

Status

Implemented

INHERENT LIMITATIONS

Because of the inherent limitations of internal controls, errors or irregularities may occur and not be detected. Also, projections of any evaluation of the internal control structure to future periods are subject to the risk that procedures may become inadequate due to changes in conditions, or that the degree of compliance with the procedures may deteriorate.

CONCLUSION

We have concluded our audit work on the objectives of the Friedman Recycling Contract Follow-Up Audit. The audit evidence used in the analysis is sufficient and appropriate for addressing the objectives and supporting the observations and conclusion. In accordance with Generally Accepted Government Auditing Standards we are required to conclude on whether Environmental Services met the objectives of this audit. The following is our conclusion.

Environmental Services Department has met the Audit objectives in the following areas:

- The billing and collection of curbside recycling income streams.
- Ensuring that Friedman Recycling Co. provides a Performance Bond in accordance with Solicitation No. 2006-015 *Single Stream Curbside Recycling Collection & Processing Services*.
- Ensuring that once Friedman Recycling Co.'s unpaid balance was paid, annual landfill credits resumed to Friedman Recycling Co. for the disposal of the first 1,000 tons of contaminants/residuals.
- Establishing a written agreement with Friedman Recycling Co. regarding the ownership of equipment Friedman Recycling Co. installed in lieu of payment.
- Implementing a process to request and review Friedman Recycling's public recycling educational/outreach program expenditures.

With approximately eight years remaining in the *Single Stream Curbside Recycling Collection and Processing Services Contract*, Environmental Services Department should ensure that it continuously monitors Friedman Recycling Co.'s compliance with the Contract.

We wish to thank the management and staff of Environmental Services Department for their assistance and courtesies extended throughout this audit.

Signature on File
Edmundo S. Calderón, CIA, CGAP, CRMA, MBA
Chief Internal Auditor

Signature on File
Liz De La O, CFE, CIA, CGAP, MPA
Lead Auditor

Signature on File
Daryl Olson
Senior Auditor

Distribution:
Financial and Audit Oversight Committee (FAOC)
Joyce A. Wilson, City Manager
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