TO: Chair and Members  
Audit and Administration Committee  

WARD(S) AFFECTED: CITY WIDE

COMMITTEE DATE: May 19, 2010

SUBJECT/REPORT NO:  
Follow Up of Audit Report 2007-11 - Overstrength and Sewer Surcharge Agreements (AUD10014) (City Wide)

SUBMITTED BY:  
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SIGNATURE:  

RECOMMENDATION:

That Report AUD10014 respecting the follow up of Audit Report 2007-11, Overstrength and Sewer Surcharge Agreements, be received.

EXECUTIVE SUMMARY

Audit Report 2007-11, Overstrength and Sewer Surcharge Agreements, was originally issued in March, 2008 and management action plans with implementation timelines were included in the Report. In March, 2010, Internal Audit conducted a follow up exercise to determine that appropriate and timely actions had been taken. Regarding the implementation of the four (4) recommendations made in the original Report and Addendum, two (2) have been initiated and two (2) have provided alternatives.

Alternatives for Consideration – Not Applicable

Vision: To be the best place in Canada to raise a child, promote innovation, engage citizens and provide diverse economic opportunities.  
Values: Honesty, Accountability, Innovation, Leadership, Respect, Excellence, Teamwork
FINANCIAL / STAFFING / LEGAL IMPLICATIONS (for Recommendation(s) only)

Financial: None.
Staffing: None.
Legal: None.

HISTORICAL BACKGROUND (Chronology of events)

Audit Report 2007-11, Overstrength and Sewer Surcharge Agreements, was originally issued in March, 2008. The Report indicated four (4) recommendations identifying areas for improvement with respect to financial, operational and administrative controls.

It is normal practice for Internal Audit to conduct follow up reviews within a 12-18 month period following issuance of the original report in order to determine whether action plans committed to by department management have been implemented. Due to staff vacancies, Internal Audit was not able to follow up the Report to confirm that appropriate and timely actions had been taken until February, 2010.

POLICY IMPLICATIONS

None.

RELEVANT CONSULTATION

The results of the follow up were provided to management and staff responsible for the overstrength and sewer surcharge agreements in the Environment and Sustainable Infrastructure division of Public Works Department.

ANALYSIS / RATIONALE FOR RECOMMENDATION

(include Performance Measurement/Benchmarking Data, if applicable)

The report attached as Appendix ‘A’ to Report AUD10014 contains the first three columns as originally reported in Audit Report 2007-11, along with an added fourth column indicating Internal Audit’s follow up comments. One (1) item in the Addendum has also been followed up with the appropriate detail provided.
Two (2) of the recommendations have been initiated but with minimal progress. Staff have notified companies with agreements based on old estimates that such estimates require updating. Management has also hired a consultant to research the creation of annual permits to replace the use of existing agreements with indefinite terms to provide a more timely opportunity to update estimates. To facilitate the change, a new by-law is expected to be presented to Council by mid 2011. The recommendation for fines and penalties, as a result of overstrength infractions, is expected to be incorporated into the new by-law mentioned earlier.

Two (2) alternatives have been implemented. The method used for the consumption estimate calculation is formally stated on the cover letter to the companies entering into agreements with the City instead of in sections of the agreements based on legal advice. The restructuring of the Compliance and Regulations unit has resulted in two supervisors overseeing smaller groups of staff which is expected to result in fewer errors due to timely detection.

**ALTERNATIVES FOR CONSIDERATION:**

(include Financial, Staffing, Legal and Policy Implications and pros and cons for each alternative)

Not applicable.

**CORPORATE STRATEGIC PLAN** *(Linkage to Desired End Results)*


**Financial Sustainability**

- Delivery of municipal services and management of capital assets/liabilities in a sustainable, innovative and cost effective manner

**Environmental Stewardship**

- Reduce the impact of Hamilton's industrial and commercial private and public operations on the environment

**APPENDICES / SCHEDULES**

Appendix “A” to Report AUD10014.
### Observations of Existing System

1. Overstrength agreements are negotiated when the companies’ discharge exceeds the limits for one or more of six different parameters treatable at the City’s wastewater treatment facility. Surcharge agreements apply to companies that are discharging water that originates from a source other than the City’s potable water supply (for example, a private well, water drawn from the lake by the company or even water extracted during production). In both cases, proper invoicing requires that the amount of wastewater flow be measured in some manner.

   During the course of this audit, it was noted that in instances where it was not possible for the City to directly measure the discharge flow, the volume was estimated either by an independent third party or using a percentage of the total flow provided by the company itself. However, many of the estimates are based on studies that have not been revised for more than ten (10) years. They may no longer be applicable as conditions or operations may have changed.

   That a procedural change be implemented to periodically and regularly (i.e. minimally every 3 years) review the estimates made when calculating flow volume and require updating, as necessary.

   **Agreed.** Companies that have billings based on studies will be requested to have these studies updated in 2008 and every 3 years thereafter. It is anticipated that the Sewer Use By-law will be amended in 2008. At that time, the appropriate changes will be made to the By-law to increase the authority the City has to obtain these studies.

   **Initiated.** Environmental Monitoring & Enforcement (EME) staff have identified companies with Overstrength and Sewer Surcharge Agreements based on old estimates and have notified them that the estimates need to be updated.

   Management is contemplating a switch from the use of existing agreements with an indefinite term to permits that will be renewed each year. To facilitate this, a consultant has been hired to help draft a new by-law and research the creation of such permits. The new by-law is expected to be presented to Council by mid 2011.

2. In some instances, it was noted that the sampling program as well as the method used to calculate the overstrength and sewer surcharges were stated explicitly in sections “G” and “H” respectively of the agreement between the company and the City. However, this practice is not consistent across all of the agreements with the companies. For some companies, alternate and less formal understandings are in place and are used to calculate the estimated flow and/or the resultant charge. Without the sampling and calculation methodologies specifically spelled out in a formal agreement, enforcement may prove difficult in times of employee or company ownership turnover.

   That the calculation method used and the manner by which consumption is estimated be specified in the appropriate sections (“G” for overstrength agreement; “H” for sewer surcharge agreements) of all formally executed agreements.

   **Agreed.** It is anticipated that the Sewer Use By-law will be amended in 2008. At that time, the appropriate changes will be made to the By-law and the billing calculation and consumption determination methods will be added in subsequent agreements.

   **Alternative Implemented.** The method used to calculate the consumption estimate is now formally stated on the cover letter issued to the companies that have entered into Overstrength or Sewer Surcharge Agreements with the City. A copy of this letter is retained by EME staff, along with the applicable Overstrength or Sewer Surcharge Agreement, to support the resultant charge billed to the company. This alternate process was implemented based on the advice of Legal Services that sections “G” and “H” reference the sampling methods used and not the flow calculations.
### Observations of Existing System

3. Overstrength agreements already allow companies to discharge various components into the sewer stream in quantities beyond that allowed in the City by-laws. However, there is no provision in the agreement for fines or penalties when companies exceed the overstrength limits. Staff have indicated that there has, to their knowledge, never been a fine or prosecution in court. Many times, companies who become aware of exceeding the limits either by a warning letter from the City or self acknowledgement respond with a request for a new agreement (to increase the limits).

Without provisions for fines or penalties, overstrength agreements lack adequate enforcement capabilities.

### Recommendation for Strengthening System

- That a chart of escalated fines and penalties for overstrength infractions be developed and approved by Council. A reference to such fines should then be incorporated into the overstrength agreements.

### Management Action Plan

- Agreed. The current penalty system will be reviewed in consultation with Legal Services and an external consultant and opportunities to streamline the process will be investigated. Expected completion 4th quarter 2008.

### Follow Up (March 2010)

- Initiated. EME staff have researched the fines and penalties levied by other municipalities, including those outside of Ontario, against companies whose discharges exceed the agreed upon parameters. Fines and penalties will be part of the new by-law referred to in point 1 above.

In addition, staff have prepared a Crown Brief to charge a company that had exceeded its allowable discharge for a lengthy time. The matter is currently before the Court. The Court will decide on the fine and penalties to impose in this case. The procedure used for preparing a crown brief will be incorporated into departmental processes.
ADDENDUM

The following item was noted during the course of the audit. Although it does not present an internal control deficiency, it is indicated in this Addendum so management is aware of the issue and can address it as necessary.

1. During the course of this audit it was noted that of the seven billings reviewed as part of the sample, two were issued invoices that had been calculated incorrectly. In one case the error related to misreading the flow information provided. This resulted in the company being underbilled by approximately $400. In a separate case, an incorrect concentration for one of the parameters was used when calculating the amount charged. This error had gone undetected since September 2006 when the new agreement had come into effect with this company, overbilling by $8,500 over the past five (5) quarters.

Management Response:
Both of the mistakes were due to typographical errors by staff. Beginning in the 1st quarter 2008, the rates for the treatment of each parameter will be “Read Only” protected and linked from a spreadsheet to the invoice request prepared by staff. Further, a buddy system will be initiated and the invoice request prepared by one staff person will be reviewed for accuracy by another as a method of detecting errors.

Follow Up Comment:
Alternative Implemented. The Compliance and Regulations Manager restructured the unit in May, 2008 so that there are now two supervisors, one responsible for Environmental Monitoring and one responsible for Enforcement Operations. This greater oversight of smaller groups of staff is expected to result in fewer errors due to timely detection. The errors noted in the original observation have been corrected in the corresponding companies’ accounts.