

# Office of Audit and Control

## AUDIT REPORT

### National Grid Accounts

**June 2018**

**Susan Rizzo**  
**Chief City Auditor**

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# Audit Team

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**A full copy of this report is available for download at our website:**

**[www.albanyny.gov/Government/Departments/OfficeofAuditandControl](http://www.albanyny.gov/Government/Departments/OfficeofAuditandControl)**

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## Preface

The Office of Audit and Control (OAC) exists to provide oversight, transparency and public accountability as a means to improve The City of Albany Administration accountability. This audit is a part of that function.

When the OAC takes on an audit subject and, setting aside issues of misconduct, that City department(s) or entities concerned respond positively to address the audit's findings; it is OAC to support and encourage use of the audit process by City departments to improve their operations.

This audit was conducted with the full cooperation of National Grid USA Service Company, Inc. ("National Grid") and Constellation NewEnergy Inc. ("Constellation").

The proper use of the audit findings in these circumstances is to provide for oversight of the resulting changes and as the basis for informed public policy discussions.

Given that National Grid and Constellation have given their full cooperation, it would be unfair and damaging to the audit process for this audit's findings to be used for political gain. As such, the OAC will view the political use of this audit's findings as detrimental to our mission.

We thank the National Grid and Constellation employees for their cooperation and commitment.

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# Background

The Office of Audit and Control (OAC) receives over 120 invoices per month from National Grid to approve for payment. In the process of reviewing these invoices, it was noted that the City of Albany was charged sales tax on several of its accounts. Pursuant to Section 116(a)(1) of the New York State Tax Law, purchases made by the City of Albany are not subject to state, local taxes or federal excise taxes.

The OAC initiated an audit of the City of Albany's National Grid accounts in late December 2017.

## Introduction

The preliminary objective of this audit was to assess the billing practices and servicing of the City's numerous National Grid accounts. This included charges from Constellation, for the supply of electricity as part of the utility consolidated billing format. The City entered into a Master Retail Electricity Supply Agreement dated October 2, 2015 with Constellation.

This audit scope did not include analysis regarding the energy rate contracted with Constellation compared to National Grid's rate. The Office of the New York State Comptroller was simultaneously conducting an audit on the procedure followed to enter into a three year fixed rate agreement with an energy service company (ESCO). The NYS audit disclosed the historical energy rates from the third party ESCO compared to National Grid's historical rates. The OAC did not duplicate these efforts.

The OAC began a review of the City's National Grid invoices in late December 2017. An entrance conference was scheduled with personnel from National Grid and completed on January 3, 2018. The purpose of this meeting was to discuss the preliminary audit scope and objectives, the audit process and timing, department and audit staff contacts, access to various types of information, and any additional concerns that arose from the meeting. Concurrently, the City's Energy Manager reached out to Constellation on behalf of the OAC. After being notified of the sales tax charged to the City, Constellation began a review of the City's accounts.

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The audit findings are as follows:

1. In the spring of 2017, per Constellation, a billing system update altered the City's tax exempt status and as a result sales tax was charged on the City's National Grid invoices for Constellation's supply charges.
2. From the beginning of the Master Retail Electricity Supply Agreement, Constellation had been erroneously charging the City Gross Receipts Tax (GRT).
3. Certain National Grid accounts – mainly but not exclusively newly opened accounts for metered traffic lights – charged the City sales tax because its tax exempt status was not entered during the account creation process.
4. Late payment charges (LPCs) were incurred on certain invoices.

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# Scope, Objectives and Methodology

## Scope

The audit covered the time period from when the Master Retail Electricity Supply Agreement and Confirmation was established with Constellation in October 2015 through April 2018.

## Objectives

The objectives of this audit were as follows:

1. Determine why the City was charged sales tax by Constellation on its National Grid invoices for the supply of electricity;
2. Determine why the City was charged sales tax by National Grid on certain accounts;
3. Determine why the City was charged LPCs on some of its National Grid accounts; and
4. Complete a thorough accounting of the sales tax, GRT, and LPCs charged to the City that OAC may find recoverable.

## Methodology

The overall audit methodology consisted of the following:

- Notifying and working closely with National Grid and Constellation personnel to review the City's accounts and historical invoices;
- Working with National Grid personnel on an ongoing basis to ensure proper billing going forward;
- Recommending the reimbursement of sales tax and GRT erroneously charged by Constellation;
- Recommending a one-time settlement with National Grid for sales tax erroneously charged to the City for its delivery and/or supply services; and
- Recommending the crediting of certain LPCs charged to the City by National Grid.

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# Audit Results

## Sales tax and GRT charged by Constellation

Upon initial review of the National Grid invoices by the audit team, it became clear that the majority of the erroneous sales tax charges were only charged to the supply services portion of the invoice. In October 2015, the City entered into a Master Retail Electricity Supply Agreement with Constellation. Under this agreement, Constellation supplied to the City its electricity for specified accounts at a fixed rate of \$0.06092 per kilowatt hour (kWh). The agreement allowed the City to purchase its electricity for a fixed rate in order to mitigate its cost exposure in the event of rising energy prices. The term of the agreement is three years, beginning 11/2/2015 and ending 11/1/2018.

As part of the agreement, the City opted for “Utility Single Bill Billing” that allowed Constellation to invoice the City via National Grid’s invoices. This option allowed the city to cut down on paperwork and workload to process and pay its energy bills.

Constellation initially billed the City correctly as a tax-exempt customer until the spring of 2017. At this time, per Constellation, it updated its billing system. Constellation concluded that this software update, combined with integration issues with National Grid’s single billing system, removed the City’s tax-exempt status. As a result, Constellation’s billing system began charging the City sales tax for its supply services at the rate of 11%.

Upon discovery of the sales tax charges and notification by the OAC, Constellation corrected the issue in December 2017. Due to open billing cycles, the issue wasn’t fully resolved and sales tax charges weren’t ceased until January or February 2018, depending on the account. When the OAC verified all sales tax billing by Constellation had stopped, Constellation performed a thorough accounting of the itemized sales tax charges to the City. The OAC audit team analyzed the data provided by Constellation to verify its accuracy and completeness.

As a result of the sales tax review, Constellation also realized that it was erroneously charging the City GRT at the rate of 1.01%, which was itemized as “Tariff Surcharge.” These GRT charges dated back to the beginning of the supply agreement in 2015. Constellation corrected the GRT billing error. Once all GRT charges ceased, Constellation performed a thorough accounting of the itemized GRT charges to

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the City. The OAC audit team analyzed the data provided by Constellation to verify its accuracy and completeness.

These erroneously charged taxes went unnoticed due to the summary nature of the National Grid invoices. The City has several National Grid accounts in a “master” account billing format in which the itemized charges for the “subordinate” accounts are less detailed. Sales tax charges were buried in summary categories and the City did not receive hard copies of the individual “subordinate” account invoices.

After a thorough accounting by Constellation and a review by the OAC, it was determined that the City had erroneously been charged fifty-seven thousand nine hundred eighty-five dollars and sixty-three cents (\$57,985.63) for sales tax and twenty-five thousand three hundred sixty-eight dollars and ninety-seven cents (\$25,368.97) for gross receipts tax. These charges totaled eighty-three thousand three hundred fifty-four dollars and sixty cents (\$83,354.60).

The OAC and the Office of the Corporation Counsel negotiated the refund of the total amount of the sales tax and GRT erroneously charged to the city. This payment totaled \$83,354.60 and was received in the form of two checks from Constellation on June 19, 2018.

The OAC considers this matter with Constellation resolved.

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## Sales tax charged by National Grid

At the same time the sales tax charges by Constellation were discovered, the OAC team discovered sales tax charges on additional accounts for which National Grid was the electricity supplier. Most of these accounts were charged 11% sales tax for both delivery services as well as supply services. National Grid serves as the default supplier of natural gas and electricity unless a third party supplier is specified for each account.

The majority of the accounts charged sales tax by National Grid were newly opened accounts. This was due to part of the City's continuing effort to upgrade its traffic signals. The legacy traffic signals had been "non-metered." When the non-metered traffic lights were disconnected, the replacement traffic lights were opened as "metered" accounts. At this point, the City's tax-exempt status was not correctly documented in the National Grid billing system, which resulted in the erroneous sales tax charges.

The OAC team performed a review and analysis of the sales tax specifically charged to the City by National Grid. The billing and tax departments within National Grid were unable to provide a complete and thorough accounting of these charges such as Constellation provided. After reviewing the data and consulting with National Grid, the City is negotiating a one-time settlement for approximately \$2,200. As of the publication of this report, the City is still in the middle of negotiations with National Grid for this settlement. If the City cannot reach a settlement with National Grid, documentation can be submitted to New York State's Department of Taxation and Finance for a sales tax refund.

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## Late Payment Charges

Concurrent with the review of its sales tax charges, the OAC began to document and analyze Late Payment Charges (LPCs) on its National Grid invoices. Due to personnel turnover and increased seasonal workload, the National Grid invoices had been processed slower than normal in the fourth quarter of 2017. As a result, the City incurred LPCs on some of its National Grid invoices. Additionally, the payment period for National Grid invoices is less than 30 days, approximately three weeks, which is shorter than standard business practice. These charges went largely unnoticed due to the summary billing format of the majority of the City's National Grid invoices.

Once the existence of these uncharacteristic charges was discovered, the OAC reviewed and streamlined its method for processing the City's National Grid invoices. These invoices are prioritized for immediate payment upon receipt. Additionally, the OAC began to work with National Grid to review its current and historical invoices for LPCs. The OAC negotiated a credit of LPCs totaling more than \$23,000. The largest of these credits was included in a June 2018 invoice from National Grid.

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# Recommendations

**Recommendation #1** - The OAC recommends that the City's Corporation Counsel continue to negotiate the one-time settlement with National Grid regarding Sales Tax charged in error. If the City is unable to reach an agreement with National Grid, the OAC recommends that the Budget Office pursue a sales tax refund from New York State's Department of Taxation and Finance.

**Recommendation #2** - The OAC recommends that the City Administration review a transition to a monthly summary billing process with National Grid utilizing the Automated Clearing House (ACH) payment system.

**Recommendation #3** - The OAC recommends that the City Administration dedicate an analyst/clerk to manage all of the City's utility vendors, including electric, natural gas, and telephone and telecommunications accounts.

# Conclusion

As a result of the OAC's audit of the City's National Grid accounts, the City has received refunds and credits totaling more than \$108,000. With the receipt of the refund from Constellation (\$83,354.60) and the anticipated one-time settlement from National Grid (\$2,200), the OAC considers the sales tax and GRT matters resolved. OAC personnel will continue to monitor future National Grid invoices to ensure there is not a recurrence of these charges. This includes monitoring invoices for newly opened accounts for sales tax.

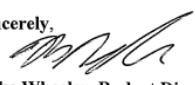
With the credit to the City's accounts for National Grid LPCs, totaling approximately \$23,000, the OAC considers this matter closed. OAC personnel will continue to monitor future National Grid invoices to ensure that its payments are processed in a timely manner by the City and National Grid's lockbox services provider. The OAC will continue to process future National Grid invoices using its streamlined process and priority status.

The OAC is continuing to work with National Grid as issues arise and has biweekly meetings with its account manager. In the future, the OAC recommends that the City transition to a monthly summary billing process with National Grid. This process allows for the city to pay all of its monthly invoices at once via the ACH payment system. National Grid personnel would prepare a master spreadsheet for all of the City's accounts on a monthly basis. This is a service that National Grid provides other customers with many accounts. However, this service is available only to additional customers on a first come, first serve basis depending on National Grid's personnel capacity. The City does not currently make payments to vendors via ACH so this procedure will need to be introduced and instituted if possible. If the City is able to take advantage of this service, it will also have the LPC functionality turned off by National Grid for all of its accounts. This once-a-month summary billing process will save the City significant time and effort as the City currently processes approximately 120 individual National Grid invoices per month.

The OAC recommends that the City dedicate an analyst/clerk to manage all of the City's utility vendors, including electric, natural gas, and telephone and telecommunications accounts. The OAC believes that this is integral to avoiding future issues and uncovering additional cost savings from other utility vendors.

# Appendix I

## Office of Administrative Service's Response

 <p><b>CITY OF ALBANY</b> OFFICE OF ADMINISTRATIVE SERVICES DEPARTMENT OF BUDGET 24 EAGLE STREET ALBANY, NEW YORK 12207 TELEPHONE (518) 434-5078</p> <p>KATHY M. SHEEHAN MAYOR</p> <p>MICHAEL WHEELER BUDGET DIRECTOR</p>		
<p><b><u>MEMORANDUM</u></b></p> <p><b>TO:</b> Susan Rizzo, Chief City Auditor</p> <p><b>FROM:</b> Michael Wheeler, Budget Director</p> <p><b>DATE:</b> September 4, 2018</p> <p><b>RE:</b> City Audits</p> <p>The Budget Department is in receipt of the audit pertaining to National Grid Accounts. After a more thorough review, the Budget Department will consider and determine the best course of follow up on any recommendations made by the Auditor's Office. We would like to thank the Chief City Auditor and her staff for their efforts, and we look forward to working together to explore even greater opportunities for efficiencies and savings.</p> <p>Please feel free to contact me if you have any questions.</p> <p>Sincerely,</p>  <p>Mike Wheeler, Budget Director</p>		

## Auditor's Response

**The Office of Audit and Control will follow-up to verify if recommendations are addressed.**