

**TO: HONORABLE CITY COUNCIL**

**ATTENTION: FINANCE COMMITTEE**

**FROM: CITY MANAGER**

**DEPARTMENT: ADMINISTRATIVE  
SERVICES**

**DATE: OCTOBER 20, 2009**

**CMR: 404:09**

**SUBJECT: Update on the Telephone Audit and Direction to Pursue the CalNet Contract  
for Telephone Services**

**RECOMMENDATION**

Staff recommends that the Finance Committee recommend to Council to direct staff to pursue a CalNet 2 contract for telephone services and return to Council for approval of the contract.

**BACKGROUND**

At the September 8 Finance Committee meeting the City Auditor presented a report on the review of City Telephone Rates and Charges (Attachment A). The key finding in the report was that the City could save approximately \$235,000 each year if it had more competitive rates for landline telephone service. Several other findings were identified that were the result of a lack of oversight by the Information Technology Division of the Administrative Services Department (ASD). The report's findings were grouped in three recommendations: 1) ASD should obtain a phone service contract with competitive billing rates; 2) ASD should obtain consolidated billing from the selected provider and develop a process to review bill payments for accuracy and appropriateness; and 3) ASD should review the current telephone oversight policies and procedures and ensure that employees are provided with accurate information when they reimburse the City for personal calls.

The City Manager's response is included in this report as Attachment A. The Administrative Services Department assisted in preparing the response and agrees with the Auditor's recommendations. This report includes a recommendation that would direct staff to pursue a CalNet contract for telephones services that would address the Auditor's recommendation number one.

The Finance Committee directed staff to follow-up on a number of issues. This report also provides a status report on the Finance Committee's direction.

## DISCUSSION

As directed by the Finance Committee on September 8, staff immediately contacted AT&T to discuss possible options for reducing the City's telephone charges. AT&T responded by immediately reducing long-distance rates from an average of \$0.26 per minute to \$0.06 per minute. The City averages 178 hours of long distance per month or \$2,792 under the old rates and \$644 under the new rates. Reducing the long-distance rates will result in a savings for the City of approximately \$2,000 a month, however the majority of costs the City incurs is for local telephone service. In addition, AT&T made the rates effective retroactive to August 2009 resulting in a credit to the City of \$10,814. The new long distance rates will be in place until the CalNet rates for long distance take effect once such a contract is in place, pending Council direction and approval.

The majority of the City's telephone charges are for local calling. In this area AT&T was not willing to immediately adjust rates and they did not provide a credit. AT&T claimed that it was not within the company's ability to immediately adjust rates due to inflexibility within the regulatory system. A new contract must be in place for new rates to take effect. AT&T claimed that new rates take up to three months to put in place. Staff is exploring administrative action against AT&T that would result in the filing of a claim with the California Public Utilities Commission to obtain further credit for these overpayments.

In order to get a contract in place, the City immediately began to pursue a CalNet contract. Pending Council direction staff would expect to return to the Council with a CalNet contract for approval by mid November.

One of the questions raised by the Finance Committee was what other local jurisdictions utilized the CalNet contract for telephone services. A list of other local jurisdictions on CalNet is below:

Town of Atherton	City of Mountain View
City of Burlingame	Redwood City
City of Campbell	City of San Jose
City of Cupertino	City of San Mateo
City of East Palo Alto	City of Saratoga
City of Los Altos	City of Sunnyvale
City of Milpitas	

State-wide there are 303 cities and an estimated 1,800 agencies in total utilizing the CalNet contract.

Another follow-up step that staff completed was the identification and termination of a residential line. The total amount of long distance charges to this line, as confirmed by AT&T, was approximately \$100 over eight years. The line was terminated in October.

Another follow-up step involved confirming that all the City's lines are indeed in use and needed in the future. This inventory has been started. It is anticipated that when this review is completed within three months and the City will be able to eliminate a number of lines that are

currently not in use. In most cases these will be lines that were used by modems or fax machines that are no longer in use due to technology advancements.

As stated in the City Manager's response (Attachment B) ASD staff will implement organizational changes to ensure proper oversight of telephone services going forward. These include the assignment of telephone service monitoring to a staff person and oversight of all telephone services and contracts to a manager. Specific oversight steps include:

- Ensuring that bills are distributed to departments monthly for their review
- Holding biennial meetings with AT&T to ensure that the contract is current
- Ensure continuing competitiveness of rates and review of other vendors
- Reviewing telephone line inventory annually to identify any unused lines
- Review requests for addition lines

Below is an action plan and timeline for accomplishing the objectives of new rates and greater oversight of the City's telephone services. Some of these steps have been completed, many are in progress and others will be completed in 2010 once a new contract is fully implemented. A status report on the results of completing the action plan will occur in mid 2010.

<b>Task</b>	<b>Date</b>	<b>Status</b>
Implement new oversight structure for telephone charges	8/09	Staff implemented a new oversight structure that includes staff and supervisor oversight.
Immediately achieve reduced rates without a new contract	9/10/09	Completed for long-distance rates. Reduced rates for local service will be completed with a new contract.
Confirm CalNet cities	9/16/09	Complete.
Research available alternatives to AT&T	10/5/09	Staff contacted two major telephone services providers and they cannot fulfill the City's needs. Staff is awaiting a response from one company.
Researched and canceled residential line	10/9/09	Complete.
Meet with AT&T and discuss credit and contract options	10/13/09	Staff met with AT&T on three occasions. Staff is awaiting a final response from AT&T regarding a possible credit for local service and to confirm the timeline for implementing a CalNet 2 contract.
Initiate CalNet 2 contract process	10/13/09	Staff has initiated the preparation phase of the CalNet 2 contract process. Pending Council direction staff is prepared to complete the process and provide Council with a contract for approval in November.
Revise policies	11/10/09	Staff is in the process of revising the telephone reimbursement policy, the telephone usage policy and the new line and service policy.

		Staff expects to complete this task in November.
Implement CalNet 2 contract (pending Council approval)	12/1/09 (target)	Pending Council approval in November staff would expect to implement the CalNet 2 contract in December.
Complete inventory of existing lines and cancel unused lines	1/4/09 (target)	Staff expects to complete the inventory of lines and the cancellation of unused lines by December.
Start realizing new rates for local service under the CalNet 2 contract	3/1/09 (target)	Once the CalNet 2 contract is in place it will take AT&T approximately three months to implement the new rates into the City's charges.
Implement bill consolidation	4/1/09 (target)	After the inventory of lines and the transition to CalNet is complete bill consolidation can be initiated.
Status report	6/09	After several months on the CalNet 2 contract staff will evaluate the new rates and other changes to ensure expectations have been met.
Ongoing oversight	Ongoing	Under the new oversight structure staff will closely monitor telephone services to ensure compliance with the new rates and policy changes.

**RESOURCE IMPACT**

Immediate savings on long-distance charges will be realized by reduced rates that are now in effect. The estimated monthly savings is \$2,000. A one-time credit of \$10,814 has been realized by the City. Going forward, the City expects to save approximately \$235,000 annually once a new CalNet contract is implemented with AT&T, pending Council approval.

**POLICY IMPLICATIONS**

Approval of this contract is consistent with existing City policies.

**ENVIRONMENTAL REVIEW**

This is not a project under CEQA.

**ATTACHMENTS**

- Attachment A: Auditor's report
- Attachment B: City Manager's response

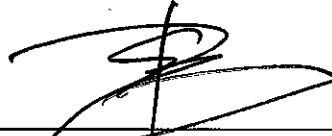
PREPARED BY:



DAVID RAMBERG

Assistant Director, Administrative Services

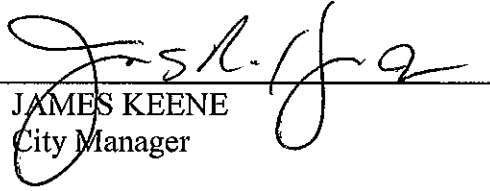
DEPARTMENT HEAD APPROVAL:



LALO PEREZ

Director, Administrative Services

CITY MANAGER APPROVAL:



JAMES KEENE

City Manager



## ATTACHMENT A

# CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

September 8, 2009

Honorable City Council  
Attn: Finance Committee  
Palo Alto, California

## Auditor's Office Review of City Telephone Rates and Charges

### Executive Summary

We estimate the City could save approximately \$235,000 each year if it had more competitive rates for landline telephone service and telecommunication lines and improved oversight of its landline telephone service. A number of issues with the City's current oversight were identified, including: the lack of a contract with its service provider; a cumbersome billing process; potentially inappropriate and unnecessary charges; and an inaccurate and incomplete internal call accounting system for seeking employee reimbursement of personal calls.

### Introduction

We initiated this review in accordance with Article IV, Section 12 of the City Charter and added it to the fiscal year 2009 work plan through our quarterly reporting process. We conducted this review in accordance with generally accepted government auditing standards. These 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.

### Background

In fiscal year 2009, the City paid AT&T approximately \$545,000 for landline telephone service and associated telecommunication lines. According to Administrative Services Department (ASD) staff, the City's telephone system consists of a combination of 1) City-owned telephone lines and 2) lines owned by the City's service provider, AT&T. The telephone system is structured as a private branch exchange (PBX) with some off-premise extensions and business lines. According to information provided by ASD staff, the City telephone system has approximately 1,400 telephone extensions and 550 business lines. The City's Information Technology Services Division, part of ASD, manages the telephone system.

### Objective, Scope and Methodology

The objective of this review was to assess the overall cost effectiveness of the City's landline telephone rates and charges. This review does not include cellular telephone rates and charges. The scope of our review covered local and long distance billing and call accounting data for the period of January through April 2009. We also reviewed telephone charges for fiscal years 2004-

2009 to evaluate historical trends in telephone charges. We selected a sample of telephone calls from the City's internal call accounting system and compared those calls to the City's actual bills to ensure the call accounting system reports were appropriately generated.

To evaluate the appropriateness of the City's telephone rates, we compared the City's local and long-distance rates to the rates of other local jurisdictions, including Redwood City, the cities of San Jose, Milpitas, San Mateo, Santa Clara and Berkeley, as well as the counties of Santa Cruz and Santa Clara.

**Finding 1: The City should seek more competitive telephone rates**

Based on our review, the City could save approximately \$19,600 each month or \$235,000 a year by obtaining a more competitive rate structure for its telephone service. The City's telephone bills currently detail rates based on monthly service charges, per minute usage rates, and additional miscellaneous charges. The City pays approximately 3 cents per minute for local calls, approximately 18 cents per minute for in-state long-distance, and approximately 32 cents per minute for out-of-state long distance calls. These rates are more than 2 to 13 times higher than rates paid by other jurisdictions we reviewed. The following example is a comparison of the City's average per minute rates compared to the rates of jurisdictions we contacted.

**Exhibit 1: Per Minute Rate Comparison**

	Average rate for surveyed jurisdictions (per minute)	Palo Alto's average rate (per minute)
<b>Local Calls</b>	\$ .011	\$ .028
<b>In-state Long Distance</b>	\$ .022	\$ .182
<b>State-to-state Long Distance</b>	\$ .024	\$ .321

Source: Phone bills and information obtained from surveyed jurisdictions

We estimate that if the City obtained similar per minute rates it could save more than \$80,000 per year. Most of the jurisdictions we surveyed participate in the statewide CALNET telecommunications contract which provides government entities in the state with significant cost savings on telecommunications service. For example, the City pays monthly service charges that are more than two times higher than the monthly service rates offered by the CALNET contract. If the City obtained monthly rates similar to those offered under the CALNET contract, it could also save an estimated \$155,000 a year.

According to ASD staff, the City does not have a contract with its provider. The lack of a contract for phone service may weaken provider accountability and protection for the City against future rate increases. If the City were able to utilize the CALNET contract or obtain similar contract terms, the City would have additional protection against rate increases. In response to our findings, ASD staff reported they are currently evaluating options to secure a competitive contract and rate structure for telecommunications service.

## **Finding 2: The City should enhance its oversight of telephone charges and use**

In our opinion, the current telephone billing process is inefficient and prevents a thorough review of phone charges. Although the City provides some limited oversight of landline telephone charges, it does not monitor several key aspects of the service and should take steps to enhance its oversight.

### ***The City should consolidate its telephone billing***

Our review found that the City's telephone bills are disaggregated, labor-intensive, and difficult to reconcile. The City paid an average of 97 telephone bills each month during the period we reviewed. The City receives separate bills for local and long-distance calling, resulting in multiple bills each month for many phone lines. In addition, some extensions are billed under different billing account numbers for local and long-distance calling, making reconciliation difficult.

### ***The City should review telephone bills to prevent inappropriate and unnecessary charges***

Our review of the City's telephone bills identified a number of potentially inappropriate or unnecessary charges. For instance, we identified more than 200 extensions without usage charges during the April billing period. While some of these extensions serve legitimate purposes, such as fire alarms or receiving in-bound calls, our analysis found that the oversight of these lines could be improved.

We also identified additional charges that could be reduced or prevented through better oversight. For instance, the City paid more than \$100 each month in directory assistance calls during the period we reviewed, even though there are several free directory assistance services available. In addition, the City repeatedly paid minimum long distance charges of \$20.95 per month on several extensions even though long distance services were used infrequently on these lines. We also identified a telephone number on the City's bill that appears to belong to a private residence. ASD staff was not able to identify a legitimate business use for this number.

### ***The City's internal call accounting system should be improved***

The City uses an internal call accounting system, called TeleMate, to document employee calls for the purpose of requesting reimbursement from employees for their personal calls. However, we found this system is configured with an inaccurate rate structure and does not capture all of the City's phone calls. As a result, the City may not be able to effectively oversee telephone use.

Although the City's policy requires employees to reimburse the City for personal calls<sup>1</sup>, according to ASD staff, because of technical issues with the system, it has been about two years since the City last produced the TeleMate report to request reimbursement from employees for personal calls. In May 2009, ASD sent the report to City departments covering calls made between January and March 2009. If an employee reimbursed the City based on the data provided to them by the call accounting system in May 2009, they may have overpaid the City for the three month period. The

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<sup>1</sup> The City's Telephone Use Policy, issued in 1996, requires employees to reimburse the City for personal calls that were not authorized for communicating work schedules, emergency situations, or other work-related information.

following examples are a comparison of the City's actual rates compared to the rates reported in the internal call accounting system.

**Exhibit 2: Comparison of City's Actual Rates and  
City's Internal Call Accounting System Rates**

Type of Call	Actual Average Rate (per minute)	Internal Call Accounting System (per minute)
International	\$2.14	\$11.59
International	\$1.20	\$3.82
State-to-state long-distance	\$.321	\$1.39
In-state long-distance	\$.182	\$.30

Source: Phone bills and TeleMate data for January through April 2009.

Thirteen reimbursements have been filed during the period we reviewed<sup>2</sup>. However, employees submitting telephone reimbursements would have paid the incorrect rates in the TeleMate report. For example, one employee reimbursed the City \$39.60 for personal calls made between January and March, although the actual cost for those calls was only \$22.44.

In conclusion, we recommend the following:

**Recommendation 1:** ASD should obtain a phone service contract with competitive billing rates.

**Recommendation 2:** ASD should obtain consolidated billing from the selected provider and develop a process to review bill payments for accuracy and appropriateness.

**Recommendation 3:** ASD should review the current telephone oversight policies and procedures and ensure that employees are provided with accurate information when they reimburse the City for personal calls.

The City Auditor's Office would like to thank the staff of the Administrative Services Department and Information Technology Services Division for their cooperation and assistance during our review

Respectfully submitted,



Lynda Flores Brouchoud  
City Auditor

Audit staff: Ian Hagerman, Senior Auditor

Attachment: City Manager Response

<sup>2</sup> The City's documentation did not specify if any of these reimbursements were for cellular phone use.

## ATTACHMENT B



# Memorandum

Date: September 8, 2009  
 From: James Keene, City Manager *JK*  
 Prepared by: Lalo Perez, Administrative Services Director  
 Subject: City Manager Response to the Audit of City Telephone Rates

## Background:

Over the past 4 months, the City Auditor's Office performed an audit of City Telephone Rates. The Auditor began a review of the telephone charges when Information Technology reinitiated sending phone statements to departments. The City Manager raised simultaneous concerns after seeing some of the statements and supported the Auditor's review. The objective of this review was to assess the overall cost effectiveness of the City's landline telephone rates. This review only addressed local and long-distance rates for landline telephone service and does not include cellular or international rates and charges. It is acknowledged there was not sufficient oversight for telecommunication services. This was due to staff reductions, including a frozen IT Manager position, and oversight responsibilities were not reassigned. The Information Technology Division is now taking measures to remedy the situation as detailed below. Information Technology would like to thank the Auditor's Office for identifying areas where improvements can be made.

## Overview:

The City of Palo Alto receives various telecommunication services from AT&T. The City's telephone system is structured as a private branch exchange (PBX) with some off-premise extensions and business lines. It should also be noted that many staff utilize cell phones in lieu of landline telephones. The following are an example of some of the landline telephone services and features that AT&T provides:

Type	~ Quantity	Comments
Business Access Lines (1MB, 1ML)	550	These lines are used for: faxes, alarm systems, credit card machines, and sprinkler systems. Call details are provided in AT&T billing.
Extensions/PBX Trunks: Direct Inward Dialing (DID) Blocks	1400	AT&T provides the trunk line, the City provides the extension. A flat rate is charged for the trunk and usage is billed on top of

		that. Call details are not provided by AT&T; instead, must use internal call accounting system. These lines bill to a 0318 or 2311 line.
Long Distance	180 hours	This includes both In State and Out of State.

Additionally, AT&T provides communication services (not reviewed in this audit) such as:

Type	Quantity	Comments
ADN Circuit Mileage	20	These are monthly flat rates
TI Circuit Mileage	26	These are monthly flat rates

All of the above services are billed to the City by AT&T through numerous bills that totaled approximately \$540,000 for the 08/09 fiscal year.

*Recommendation 1: ASD should obtain a phone service contract with competitive billing rates.*

Staff agrees with this recommendation.

To address the need for obtaining more competitive billing rates, staff is researching the ability to utilize a State contract, "CALNET 2." This contract has aggressively negotiated rates that went through a competitive bid process and extends to other Public Sector entities. The contract was awarded in January 2007 and is a 5 year contract with (2) two (1) year extensions. The Palo Alto Municipal Code stipulates, in Section 2.30.360, J, 2, in order to utilize the CALNET 2 contract, the contract must have been awarded within twelve months of the date the city contracts for the goods and/or services. However, staff is currently working with the Attorney's office and Purchasing Division to execute the contract as the original intent of the contract was for all public agencies to utilize regardless of the time frame. Staff expects to have the CALNET 2 contract on the Council agenda by October 2009.

*Recommendation 2: ASD should obtain consolidated billing from the selected provider and develop a process to review bill payments for accuracy and appropriateness.*

Staff agrees with this recommendation.

Staff is working with AT&T to develop an appropriate billing structure for the multiple services in the State CALNET 2 contract. To identify an appropriate billing structure, staff will first inventory all services that AT&T provides. This includes identifying each line,

what it is used for, and by whom. Once the inventory is complete, staff will then group all like services for billing. Billing groups might consist of the following:

- All business access lines (1MB, 1ML)
- All communication lines (T1 Circuits)
- All Long Distance Charges

By grouping services, fewer bills will need to be processed and information will be properly organized. This will also result in easier bill review and less administrative processing.

*Recommendation 3: ASD should review the current telephone oversight policies and procedures and ensure that employees are provided with accurate information when they reimburse the City for personal calls.*

Staff agrees with this recommendation.

Once the CALNET 2 contract is executed, the new rates will be entered into the Internal Call Accounting system. This will then allow IT to disperse monthly call details to departments, with accurate rates, and will allow departments to review call details for appropriate use and reimbursements. Staff is also reviewing the existing Telephone Use Policy and updating if needed. For any previous reimbursements, staff is following up with individuals to determine if appropriate amounts were reimbursed and resolving any inaccuracies.

In addition to the Auditor's Recommendations, IT is also implementing:

- **New Management Oversight of the Billing**

IT will distribute call details and charges monthly to departments for departmental scrutiny of telephone usage. The expectation is that employees will review their phone bills and reimburse the City for any non work-related phone calls. Managers will also review for any non work-related usage. Additionally, IT has assigned an IT Manager along with a Sr. Technologist to provide more oversight over the telecommunications billing.

- **Telecommunication Contract**

IT will ensure a contract is executed and maintained for all telecommunication services to ensure rates are always competitive and negotiated. This includes communicating with the State to ensure the City of Palo Alto participates with any future State contracts as economies of scale yield more competitive rates.

- **Telecom Assessment RFP**

IT is in the process of executing a contract that will address evaluating the current state of the telecommunication system, performing a needs assessment, recommendations on

technologies to use, and approximate budget requirements necessary to implement. This assessment is expected to begin November 2009.

- **Cellular Phones**

Cellular phones are currently under contract and rates are reviewed annually. In April 2009, IT staff performed an audit and usage review that resulted in rate plan changes and the elimination of any unused devices.