



## CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

September 21, 2009

The Honorable City Council  
Palo Alto, California

### **Finance Committee Recommendation to Accept the Auditor's Office Audit of Police Investigative Fund**

At its meeting on July 21, 2009, the Finance Committee unanimously recommended to the City Council acceptance of the Auditor's Office Audit of Police Investigative Fund. Minutes of the meeting are attached.

Respectfully submitted,

A handwritten signature in cursive script that reads "Lynda Flores Brouchoud".

Lynda Flores Brouchoud  
City Auditor

Attachments:

- *Attachment 1* - Auditor's Office Audit of Police Investigative Fund
- *Attachment 2* - Finance Committee Minutes of July 21, 2009 pgs 17-19



## CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

July 21, 2009

Honorable City Council  
Attention: Finance Committee  
Palo Alto, California

### Audit of the Police Investigative Fund

#### SUMMARY OF RESULTS

In accordance with the City Auditor's Fiscal Year 2008-09 Work Plan, and at the request of the former Chief of Police, the City Auditor's Office performed a surprise audit of the Police Investigative Fund (PIF) on April 7, 2009. The audit objective was to verify the accuracy of the reported cash on hand and assess controls over the use of the funds. The audit scope included a review of transactions since the prior audit in April 2007 through April 2009. We conducted this 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

The Police Department can use the PIF as a cash fund to pay for certain investigative costs such as payments to informants and purchases of narcotics, contraband, stolen property, or other evidence. The PIF balance is limited to \$1,500. The PIF procedures provide guidance on the appropriate use of the PIF. These procedures limit access to the PIF, require accurate bookkeeping and documentation, and specify legitimate uses of the funds. The City Auditor's Office reviewed procedures, performed a cash count of the funds on hand, and examined the fund ledger and supporting documents.

Following is a summary of our review:

- **At the time of our surprise audit, we found that the PIF cash balance was accurately reported in the ledger, the cash was properly secured, and access to the vault was properly controlled.** Specifically, the PIF balance totaled \$928 on the date of our last audit, conducted on April 19, 2007. From April 2007 through April 2009, there were only three PIF transactions: two disbursements totaling \$80, and one reimbursement totaling \$40. The PIF balance as of April 7, 2009 was \$888.
- **These overall findings are consistent with the results of our last surprise audit conducted in April 2007.**

We also noted three areas for improving the Police Department's internal controls of the PIF:

- **The Police Department should ensure each PIF transaction has complete and consistent documentation.** Specifically, we found that the three transactions during the review period had incomplete documentation. For example, the procedures require that payment vouchers to confidential informants include the signature of the informant in addition to the signature of the

supervisor and officer, and that no payment be made if the informant refuses to sign the voucher.<sup>1</sup> One of the disbursements paid an informant; however, the informant's signature was not on the payment voucher. The second disbursement did not list the reason and utilized the "credit voucher" form (used for documenting returns to the fund) rather than the form for fund disbursements. The third transaction had incomplete signatures. Complete and consistent documentation for transactions will help improve internal controls over the use of the funds.

- **The Police Department has not revised the PIF internal procedures since 1997, and as a result, the procedures include outdated information.** For example, as noted above, even though the procedures require the signatures of informants, police officers were not obtaining informants' signatures because it is impractical to do so in the field. However, the informant's signature serves as verification for the use of the funds and if this control is not implemented, another control should be developed and documented. Upon further inquiry, the Police Department stated that although it is not documented, whenever there is a payment to a confidential informant, there are at least two officers present. This "dual custody" or involvement of at least two individuals to check each other, can reduce the risk of a loss occurring and provides some assurance the funds are appropriately used. We also noted inconsistencies between the written procedures and subsequent verbal agreements delineating the timeframe and responsibilities for conducting cash counts of the PIF.
- **The Police Department's PIF procedures are essentially desk procedures and are not part of the department's formalized manual or procedures.** As a result, they may not receive the same level of periodic review, training and authorization as the department's formal procedures.

We shared the above audit results with the Police Department's Investigative Services Division and the Administrative Services Department's Supervisor of Revenue Collections. The Police Department concurred with the audit findings and recommendations and proactively began updating its procedures of the Police Investigative Fund.

## RECOMMENDATIONS

In our opinion, the Police Department should continue its update of the Police Investigative Fund procedures. We recommend that the Police Department update the PIF procedures to reflect actual practices including:

1. Integration of the PIF procedures into the Department's approved policies;
2. A requirement for the two officers who had direct knowledge of the disbursements from the PIF to document the final disposition of the funds on an updated fund form and/or updated log; and
3. Clarification of the timing and responsibility for performing periodic cash counts of the PIF.

On behalf of the Auditor's Office, I would like to express my appreciation to the Police Department for their cooperation and assistance during this review.

Respectfully submitted,



Lynda Flores Brouchoud  
City Auditor

Audit staff: Lisa Wehara

Attachment: City Manager's Response

<sup>1</sup> The Police Department has a separate policy to document and approve the use of Confidential Informants in investigations.



## Memorandum

Date: June 18, 2009

From: James Keene, City Manager *JK*

Prepared By: Dennis Burns, Interim Police Chief

SUBJECT: Audit of the Police Investigative Fund (PIF)

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On April 7, 2009, the City Auditor's Office performed a surprise audit of the Police Investigative Fund (PIF). The purpose of the audit was to verify the accuracy of the reported cash on hand and assess controls over the use of the funds.

The PIF is a cash fund available to cover certain costs incurred during investigations such as payments to informants and purchases of narcotics, contraband, stolen property or other evidence. The Captain of the Investigative Services Division (ISD) is the custodian of these funds. The funds are secured in a locked safe which is located in the Captain's office. The ISD Captain and two ISD Supervisors are the only personnel authorized to release these funds.

The Police Department has a separate policy for the development and use of confidential informants. Each potential informant is highly scrutinized and must complete a stringent verification process before they are used as informants. The verification process includes a background investigation to determine their reliability and credibility. Informants must sign the waiver forms indicating that they understand the rules before they are verified.

At the time of the surprise audit, the City Auditor's Office found that the PIF cash balance was accurately reported in the ledger, the cash was properly secured and access to the safe was properly controlled. The audit made several recommendations for improving the process for distribution and tracking of these funds.

***RECOMMENDATION #1 – Integration of the PIF procedures into the Department's approved policies.***

Staff agrees with the recommendation.

The PIF procedure for distribution is currently housed within the Investigative Services Division. The reason for this is that the PIF is controlled by the ISD Captain and any distributions would need to be authorized and approved by the ISD Captain. In order to formalize the procedure and ensure better understanding throughout the entire Department, we will add the PIF procedure to

the end of the Confidential Informant Policy found within the Department's Policy Manual. Each year, every member of the Department receives an updated version of the Policy Manual which also references the new changes.

***RECOMMENDATION #2 – A requirement for the two officers who had direct knowledge of the disbursements from the PIF fund to document the final disposition of the funds on an updated fund form and/or updated log.***

Staff agrees with this recommendation.

We have added a section in the PIF procedures which states that when funds are paid to an informant, two officers who had direct knowledge of the transaction between the informant and third party (person selling the narcotics, contraband, stolen property, etc...) shall sign the second page of the voucher which references the disposition of the funds.

We have updated the voucher form and ledger to include a section for documenting the disposition of funds.

***RECOMMENDATION #3 – Clarification of the timing and responsibility for performing periodic cash counts of the PIF.***

Staff agrees with this recommendation.

The PIF procedure has been updated to reflect that Revenue Collections will complete a random, annual cash count of the PIF. The PIF will also be subject to random audits from the City of Palo Alto Auditor's Office. Revenue Collections is aware of this recommendation and will complete the random cash counts at times of their choosing.



## FINANCE COMMITTEE

Mr. Perez said that Staff didn't know what value a vendor would place on the penalty clause. This would give us an opportunity to not go out again and perhaps to negotiate based on our needs.

**MOTION:** Chair Burt moved, seconded by Council Member Schmid to direct Staff to bid with the proposal on Attachment A-1 only and not the alternative.

Chair Burt said that he thinks these are not onerous penalties but they are large enough to incentivize. It's likely the value of the contract is such that a bidder will want it and perhaps look at improving their efficiency. He said he hopes Staff and the Council will continue to be good innovators, and while this is aggressive it's not over the top.

**MOTION PASSED:** 2-1 Morton no, Klein absent

Mr. Perez said that Staff will incorporate the changes and put the RFP out. They may have to come back directly to Council due to timing.

→ 5. Audit of Police Investigative Fund.

City Auditor, Lynda Brouchoud said that Staff is reviewing an audit of the Police Department's investigative funds. This audit was precipitated during the FY 2009 workplan and the former Police Chief asked that this be added to our workplan. The audit consists of a surprise count of the cash on hand in the Police Department Investigative Fund that they use for informants, and narcotics and such, so the fund amount is limited to \$1500. At the time of our audit, we found that the balance was accurately reported as \$888, it was properly secured, and access was controlled. Since our last audit in April 2007 there had only been 3 transactions. We made three minor audit recommendations to insure that the most effective procedures were in place. The Police Department concurred with each one and they have taken steps to implement the recommendations. Part of the reason for this audit request was the Police Department's internal procedures had a requirement to ask us to do this. We are asking for some clarification of the roles to make sure we are not auditing these small funds and the revenue collections staff knows they have this fund on their cash counts as well.

Council Member Schmid asked if Staff does a lot of these small audits



## FINANCE COMMITTEE

Ms. Brouchoud said they do not do a lot of these types of audits. They have typically done this audit for the reasons mentioned. The Revenue Collections Staff are charged with the cash counts around the City. All funds are eligible for being audited but this was an anomaly.

Administrative Services Director, Lalo Perez said that Ms. Stokes is in charge of the Revenue Collections Team and it is her goal to rotate all departments.

Council Member Schmid confirmed that the action of the auditor is fairly unique.

Ms. Brouchoud said that is correct. It's more of a performance audit. The external financial auditors routinely sample different cash funds.

Council Member Schmid said that he was surprised that this fund with \$100 in transactions over two years was picked out.

Ms. Brouchoud said that Staff's hope is this will be resolved with the improved coordination.

Chair Burt asked if it is cost effective to put this type of audit, where only small problems are found, on an annual basis.

Ms. Brouchoud said she believed the Revenue Collections Staff will put this item on their list of cash funds they will review regularly. This fund would be treated as the other funds and subject to random audits.

Chair Burt asked if the fund was set up for an annual audit.

Ms. Brouchoud confirmed that it is not.

Vice Mayor Morton said that he doesn't know that the Committee needs to approve it.

Ms. Brouchoud said that Staff is recommending that the Finance Committee review and recommend that the Council accept the Audit of the Police Department's Investigative Fund.



## FINANCE COMMITTEE

**MOTION:** Vice Mayor Morton moved, seconded by Council Member Schmid, that the Finance Committee recommends that the City Council approve the Audit of the Police Department's Investigative Fund.

**MOTION PASSED:** 3-0 Klein absent

### 6. Auditor's Office Quarterly Report as of June 30, 2009.

City Auditor, Lynda Brouchoud said this report represents the wrap up of the last fiscal year. The report details the completed projects that the Auditors Office has completed including audit projects and other projects such as sales tax allocation reviews. Our sales tax monitoring this year uncovered close to \$85,000 in recoveries. This is lower than our target of \$150,000 and is likely a reflection of the current economy. There is also an increase in the backlog of inquiries at the State. Staff is hoping that will clear out in time. The Auditor's office initiated additional recovery efforts this year through the Federal Alternative Fuel Tax program we hope to see the results of those efforts. We also have a number of projects in process. We have a review of telephone charges, and the Vehicle Replacement and Maintenance Fund. Staff has initiated the City Wide Cash Handling Audit as it was a clear priority of the Committee. She pointed out as part of the proposed budget, Staff asked the external Auditor to voluntarily forgo the CPI that was built into their contract, and they have agreed to do so.

Chair Burt thanked Maze and Associates for doing their part to help financially. He said it affirms the efforts of looking for sharing in this cost burden. It's a reasonable approach that Council and Staff should continue to explore.

Council Member Schmid said it's hard to assess the overall impact of the office. That's why an annual review at the Council level is done. In terms of work projects there are classes of products like the annual survey and sales revenue audit that are major reports. Secondly there are audit topics that have been identified which are the longer term projects like cash handling. A third element is the smaller topics that come up like the Police Investigative Fund. It's the Auditors job to allocate the Audit Department resources. There is value in completing those smaller items. To take a quick look at them is helpful at the Council level for allocating resources.

Ms. Brouchoud thanked the Committee for the input. She reminded the Committee that the Audit team is the smallest work group in the City and