



## CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

February 13, 2017

The Honorable City Council  
Palo Alto, California

### **Policy and Services Committee Recommendation to Accept the Auditor's Office Quarterly Report as of September 30, 2016**

The Office of the City Auditor recommends acceptance of the Auditor's Office Quarterly Report as of September 30, 2016. At its meeting on November 29, 2016, the Policy and Services Committee approved and unanimously recommended the City Council accept the report. The Policy and Services Committee minutes are included in this packet.

Respectfully submitted,

Harriet Richardson  
City Auditor

#### **ATTACHMENTS:**

- Attachment A: Auditor's Office Quarterly Report as of September 30, 2016 (PDF)
- Attachment B: Policy and Services Committee Meeting Minutes Excerpt (November 29, 2016) (PDF)

Department Head: Harriet Richardson, City Auditor





# CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

November 15, 2016

**The Honorable City Council**  
Palo Alto, California

## **Auditor's Office Quarterly Report as of September 30, 2016**

### RECOMMENDATION

The City Auditor's Office recommends the Policy and Services Committee review and recommend to the City Council acceptance of the Auditor's Office Quarterly Report as of September 30, 2016.

### SUMMARY OF RESULTS

In accordance with the Municipal Code, the City Auditor prepares an annual work plan and issues quarterly reports to the City Council describing the status and progress towards completion of the work plan. This report provides the City Council with an update on the first quarter for FY 2017.

Respectfully submitted,

A handwritten signature in cursive script that reads "Harriet Richardson".

Harriet Richardson City Auditor

### **ATTACHMENTS:**

- Attachment A: Auditor's Office Quarterly Report as of September 30, 2016 (PDF)

Department Head: Harriet Richardson, City Auditor





CITY OF  
**PALO  
ALTO**

# Quarterly Report as of September 30, 2016



## Office of the City Auditor

“Promoting honest, efficient, effective, economical, and fully  
Accountable and transparent city government.”

## Overview

The audit function is essential to the City of Palo Alto's public accountability. The mission of the Office of the City Auditor, as mandated by the City Charter and Municipal Code, is to promote honest, efficient, effective, economical, and fully accountable and transparent city government. We conduct performance audits and reviews to provide the City Council and City management with information and evaluations regarding how effectively and efficiently resources are used; the adequacy of internal control systems; and compliance with policies, procedures, and regulatory requirements. Taking appropriate action on our audit recommendations helps the City reduce risks and protect its good reputation.

## Highlights of Activities During the Quarter

Below is a summary of our audit and project work for the first quarter of FY 2017:

Title	Objective(s)	Start Date	End Date	Status	Results/Comments
Citywide Analytic Development and Continuous Monitoring: Procure-to-Pay	Determine if data analytics and continuous monitoring can help the City detect duplicate vendor or vendor payment records.	06/15	12/16	In Process	This audit is in the reporting phase. The scheduled date of presentation to Policy and Services Committee is February 2017.
Fee Schedules Audit	Evaluate City processes for establishing fees to determine if the fees cover the cost of services provided when expected. The specific fees to be reviewed will be narrowed down during the planning phase of the audit.	06/15	12/16	In Process	The audit is focusing on Community Services fees and is in the field work phase. The estimated date of presentation to Policy and Services Committee is December 2016.
Utilities Customer Service: Rate and Billing Accuracy Audits	Evaluate whether the Utilities Department properly implements rates and accurately bills customers.	06/15	12/16 and TBD	In Process	The audit is in the reporting phase for water billings. Due to the variety of issues we identified, we will issue a report on the accuracy of water billings and do field work for gas and electric billings after we conduct the enterprise resource planning system audits. The estimated date for presenting water billings to Policy and Services Committee is December 2016. We will estimate the date for presenting the gas and electric billings when we begin field work for that audit.

Title	Objective(s)	Start Date	End Date	Status	Results/Comments
Citywide Analytic Development and Continuous Monitoring: Overtime	Determine if implementing a continuous monitoring process for overtime could improve the City's oversight and management of overtime.	06/15	12/16	In Process	The project is in the field work phase. The scheduled date of presentation to Policy and Services Committee is February 2017.
Sustainable Purchases	Assess the City's purchasing practices to determine if environmental sustainability is adequately considered in all purchases as appropriate.	03/16	12/16	In Process	The project is in the planning phase. The scheduled date of presentation to Policy and Services Committee is February 2017.
Hydromax Crossbore Contract	Evaluate the work performed under this contract to determine if the City is taking an appropriate approach to this work, getting appropriate line inspection data from this effort, and allocating an appropriate level of contractor oversight.	09/16	12/16	In Process	The project is in the planning phase. The estimated date of presentation to Policy and Services Committee is February 2017.

### Other Monitoring and Administrative Assignments

Below is a summary of other assignments as of September 30, 2016:

Title	Objective(s)	Status	Results/Comments
Sales and Use Tax Allocation Reviews	<p>1) Identify businesses that do business in Palo Alto that may have underreported or misallocated their sales and use tax and submit inquiries to the state for review and tax reallocation.</p> <p>2) Monitor sales taxes received from the Stanford University Medical Center Project and notify Stanford of any differences between their reported taxes and state sales tax information, in accordance with the development agreement.</p> <p>3) Provide Quarterly Status Updates and Sales Tax Digest Summaries for Council review.</p>	Ongoing	<p>1) Total sales and use tax recoveries for the first quarter were \$7,301 from our inquiries and \$254,114 from the vendor inquiries, for a total of \$261,415 year-to-date. Due to processing delays at the State Board of Equalization, there are 65 potential misallocations waiting to be researched and processed: 20 from our office and 45 from the vendor.</p> <p>2) We receive calendar-year sales tax information for the Stanford project about six months after the end of the calendar year. We will report the sales tax information for this project in our June 2017 quarterly report.</p> <p>3) Quarterly sales tax reports are published on the Office of the City Auditor website at <a href="http://www.cityofpaloalto.org/gov/depts/aud/reports/default.asp">www.cityofpaloalto.org/gov/depts/aud/reports/default.asp</a>.</p>

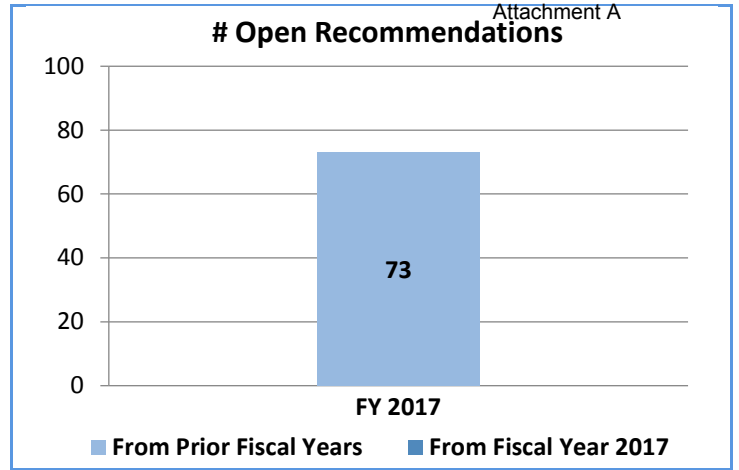
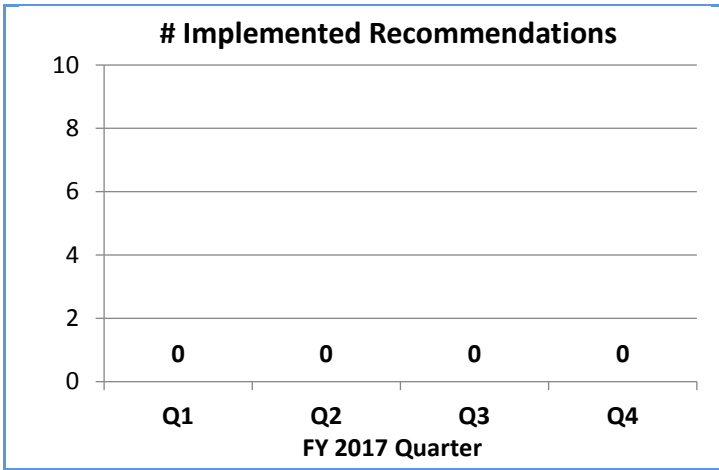
Title	Objective(s)	Status	Results/Comments	Attachment A
City Auditor Advisory Roles	Provide guidance and advice to key governance committees within the City.	Ongoing	The City Auditor serves as an advisor to the Utilities Risk Oversight Committee, Information Security Steering Committee, and Information Technology Governance Review Board. We have recently taken on an advisory role for the strategic and technical planning groups for planning the new Enterprise Resource Planning (ERP) system.	

### Status of Audit Recommendations

Seventy-three recommendations were open at the beginning of FY 2017, and none were closed. We did not add any additional recommendations during the first quarter of FY 2017. Below is a summary of open audit recommendations, by audit, as of September 30, 2016:

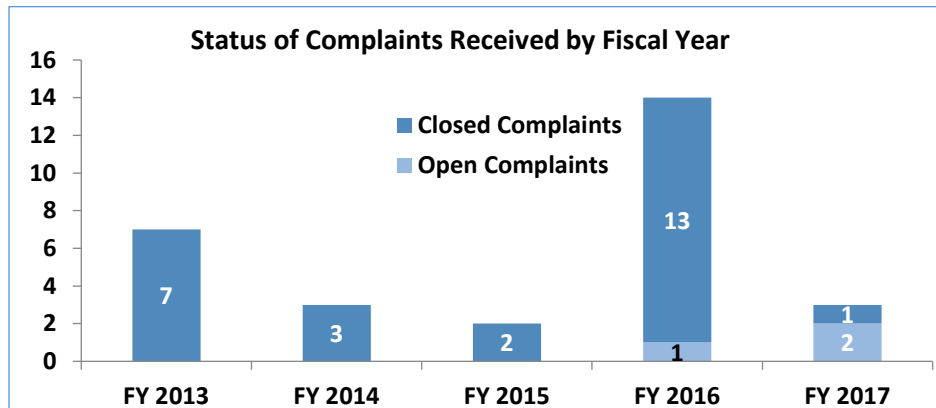
Audit Title	Report Date	Status Report Dates	Due Date of Next Status Report	Total Recommendations	Implemented During Quarter	Open
Citywide Cash Handling and Travel Expense	09/15/10	11/10/15 09/23/14 09/10/13 10/22/12 04/19/11	Past Due	11	0	2
Contract Oversight: Trenching and Installation of Electrical Substructure	11/05/13	12/15/15 09/23/14	Past Due	6	0	2
Inventory Management	02/18/14	09/23/14	Past Due	14	0	14
Utility Meters: Procurement, Inventory, and Retirement	03/10/15	None	Past Due	15	0	15
Police Department: Palo Alto Animal Services	04/22/15	03/22/16	Past Due	8	0	8
Parking Funds	12/15/15	None	Past Due	8	0	8
Disability Rates and Workers' Compensation	05/10/16	None	02/14/17	15	0	15
Cable Franchise and Public, Education, and Government (PEG) Fees	06/14/16	None	03/08/17	9	0	9





### Fraud, Waste, and Abuse Hotline Administration

The hotline review committee, composed of the City Auditor, the City Attorney, and the City Manager, or their designees, meets as needed to review hotline-related activities. We received three hotline complaints during the first quarter of FY 2017, two of which were related to the same case. The chart below summarizes the status of complaints received in each fiscal year since the hotline was implemented.



Source: City of Palo Alto hotline case management system as of September 30, 2016

We recently sent a survey to about 60 local government audit offices that manage a hotline to seek input about how they manage their hotlines to ensure they receive calls when fraud, waste, or abuse are suspected and how they triage and investigate valid complaints. We have received about 25 responses so far and are compiling the results. We will present a discussion item on this topic at the Policy & Services Committee meeting on November 29, 2016.

# POLICY AND SERVICES COMMITTEE TRANSCRIPT



Special Meeting  
Tuesday, November 29, 2016

Chairperson DuBois called the meeting to order at 6:09 P.M. in the Community Meeting Room, 250 Hamilton Avenue, Palo Alto, California.

Present: DuBois (Chair), Kniss, Scharff

Absent: Berman

## Oral Communications

None.

## Agenda Items

1. Auditor's Office Quarterly Report as of September 30, 2016.

Chair DuBois: We're going to proceed with Item Number 1: The Auditor's Quarterly Report.

Harriet Richardson, City Auditor: Harriet Richardson, City Auditor, Good evening Mr. Chair and members of the Committee. Harriet Richardson, City Auditor here to present the statues quarterly Report for July through September 2016. We have several audits in progress and I'll say up front, right now, a lot of these dates that we had originally scheduled for presenting these audits to Policy and Services have been pushed out because of other items but I will tell you what the revised states are as we go. The first one is, continuous monitoring audit on procured pay, which is really accounts payable. Looking at whether or not continuous monitoring can help the City detect duplicate vendor or duplicate vendor payment records and identifying a process to minimize that. That audit is in the reporting phase and it scheduled to be presented in February 2017. I do expect that one to be ready to go then. The fees schedules audit, we're looking at the processes for establishing fees with the focus on Community Services Department and whether or not how well those fees align with the City's policy on cost recovery and as of the end of September, that audit was in the field work phase. That audit has now out (Inaudible) so for official response to the City Manager's Office and this is one that's been pushed out. We do expect to publish it by the end of the calendar year but it's been pushed out for presentation to Policy and Services to February. Utilities customer service rate, billing and accuracy audits; so, we are looking at the way the Utilities Department implements rates and whether or not it

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accurately bills customers. This was originally going to be a single audit on water, gas and electricity billings but because of the number of issues we identified in water, we've stopped work on gas and electric and are going to issue a separate report on water. We were originally planning to publish the report by the end of December with presentation now pushed out to February. The auditor who's been working on that has been out sick since early November so, we will be pushing it. Whether or not we'll make that deadline – that time line of publishing by the end of December, we're going to try for that but I'm not sure that we'll make it, depends when she comes back. Then we'll start the second part, the gas and electric after we do the Enterprise Resource Planning (ERP) audits that we have planned, which I consider a higher priority given the time line for the ERP planning process. We have another continuous monitoring audit that was looking at over time and whether or not the City can implement procedures that might help them better monitor than manage their overtime by having more detailed data that could be analyzed by continuous monitoring process. That audit is in progress right now and it's another one that's been pushed out. It's now scheduled for presentation in March 2017. Sustainable purchases audit, we're looking at how well the City's implemented its Sustainable Purchase Policy in the purchases that it makes of products that the City buys. That one is also in progress, it's in filed work right now and I expect that one to be done, either by the end of year or early January. That one was scheduled for February and that one is being pushed out to March Policy and Services Committee. I think all of these dates are on the Policy and Services draft agenda, that they go over at the end of the Committee meeting. The [Hydromax Crossbore Contract], that one's in progress right now. We're looking to see whether or not the work performed under that contract – whether the City took an appropriate approach to identifying the work needed to be done and has applied the appropriate level of contractor oversight. I expect that one to be done either by the end of this month or early January and again that's one that's been pushed out. It's been pushed out for presentation to March. Even though these audits have been pushed out on their presentation dates, we will publish them as they are completed. On the other work that we do, sales and used tax allocation; for the first quarter, we have recovered a total of \$261,415 to date. About \$7,300 of that is from the work that our office does and about \$254,000 of that is from work that our consultant does, \$220,000 of that \$254,000 was a large lump sum recovery due to a reallocation from the third quarter of 2006 thru the second quarter of 2014 and our consultant had done a lot of work appealing to the State franchise – the State Board of Equalization, excuse me, State Board of Equalization regarding this miss allocation that had been throughout the State and recovered a large sum of money for quite a number of jurisdictions. Our quarterly reports, we do get an Information Report from the consultant that we publish regularly and those are available

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on our web site and we present them as information reports to the Council. We also continue with our advisory roles for the Utilities Risk Oversight Committee, the Information Security Steering Committee and the Information Technology Governance Review Board. We've recently taken on an oversight role for strategic and technical planning for the Enterprise Resource Planning System and we're treating that as a separate, non-audit service, where we are looking at things – how the Department of Information of Technology is implementing the process planning – the project and their plans for implementation so that if we see anything that if, for example, if we came in after the fact and then audited, we would have said, oh you should have done this different. We can make some recommendations as we go so, this isn't an actual audit, it's a non-audit service because we are making recommendations as we go rather than producing findings after the fact like we typically do. The status of audit recommendations, we have seven audits – eight audits, excuse me, eight audits that have open audit recommendations. Several of them are past due on the due date for the next Status Report. The contract oversight for utility or the – not the contract oversight, the inventory management and utility meters' ones, we've had some meeting scheduled to talk about where the disagreement is between our office and the departments that are responsible for implementing the recommendations but again the auditor who is responsible for those, is the auditor who's been out sick so, we've had to reschedule those and so those have been postponed to January to have that discussion. On the other audits, we are taking a new approach on how we're going to start doing the status reports. My office is going to take back responsibility for sending out the notifications that the audits are due for status report and we'll start doing that again in January and then we're going to coordinate with the City Manager's Office for – it's still going to be their report to present to Policy and Services but we will validate the recommendation – the status reports first to determine whether the recommendations actually have been implemented when they say they have and then the City Manager's Office will take the Report and present it for Policy and Services Committee. It's taken us a little while to kind of work through how we can make this process work because it wasn't working so well and now I think we've got a plan to get these moving along. No recommendations were implemented during the first quarter of this year and there are 73 open recommendations for those eight audits. The Fraud, Waste and Abuse hotline, we received three complaints during the first quarter of FY 17. Two of those were – one of those was closed and two of them are open right now. Those two will probably be reported as closed during the next reporting period. So, we've only received a total of 29 since inception of the hotline in 2013 and this is another area where we've had to push out the presentation to Policy and Services but I will be coming to Policy and Services, it's currently scheduled for February 2017, to discuss a

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new approach for how we should manage complaints. Get information out there about what appropriate to report through the hotline and what's not appropriate and by doing that, I'm hoping that we'll get complaints that are the right type of complaints and we did recently have one that was actually a very good appropriate complaint for the hotline and it resulted in the expected outcome as far as action taken to resolve the issue. I'm hoping that by getting more information out there about what's appropriate – I think that particular one was a result of a presentation I had given to a department where I was able to explain a little bit about the hotline and the complaint came in shortly thereafter and it was the legitimate type of complaint we would expect to see related to fraud, waste or abuse. That concludes my presentation and if you have any questions, I'm here to answer them.

Council Member Kniss: Looking at Packet Page 6, where we're talking about the calendar year sales tax information and you're saying that comes in about six months after the end of the calendar year.

Ms. Richardson: That's the Stanford – the Stanford information comes in about six months after the end of the calendar year. That's for the Stanford Hospital project.

Council Member Kniss: Right. I don't want to mix apples and oranges but knowing the School Board had difficulties with one of the projections that they had, I'm going to presume this is nothing like that, correct?

Mr. Richardson: No and we don't project what that will be. We get a report – they track – we have an agreement with Stanford, that for all of the work done at the hospital, that the sales tax for that project will come directly to the City for materials that they use; anything that's eligible for sale tax and they track it and then after they've compiled it, it takes them about six months for them to get the report to us. Then, we have a way of validating that that is the right information and then we report it after that. So, usually, we report it in the June Quarterly Report, at the end of the fiscal year.

Council Member Kniss: This, though – without knowing or remembering what the amount are, I'm going to guess that these are certainly a far less amount than what we get from the shopping center?

Ms. Richardson: That information is in our quarterly – the quarterly information reports and I don't know the numbers off the top of my head but I could get those to you.

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Council Member Kniss: I guess I could look at them myself too but it just would seem – this is interesting. This has to do with (Inaudible) project?

Ms. Richardson: Yes, and the numbers that I present here are only the numbers that we pursue, where we think there's been a miss allocation or an under-reporting of sales tax. Everything else that comes through the City, it's millions of dollars, we don't report that in this report.

James Keene, City Manager: What is the figure we're looking at? I might be able to shed some light on.

Ms. Richardson: It's the... (Crosstalk)

Council Member Kniss: Sales and Use tax.

Ms. Richardson: Sales and Use tax.

Mr. Keene: Yes.

Council Member Kniss: For the hospital project.

Mr. Keene: Oh, ok, for the – I'm sorry. I thought you were talking about the shopping center.

Council Member Kniss: I was, I said comparatively because I wouldn't think that the hospital project would be bringing in a lot of sales tax dollars. Hadn't even thought about it as a significant...

Ms. Richardson: My guess is that it's quite a bit less. I want to say...

Mr. Keene: Well, traditionally we would generally estimate that we get about a quarter of our sales tax actually, from the shopping center.

Council Member Kniss: From the shopping center but not from the hospital project?

Ms. Richardson: No.

Mr. Keene: We are running it – you know, we typically run between 25 and 30 million dollars total in sale tax.

Council Member Kniss: Right. We are delighted to have a shopping center but I'm simply looking at this and – just because that odd thing had

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happened with the school. I can see that this is quite different but looking at it, just a flag went off. Thanks.

Vice Mayor Scharff: Alright, just briefly. In terms of closing audit recommendations, we did nothing in the last quarter or in terms of the closing amount it shows that we've worked towards doing it. (Inaudible) Quick status update.

Mr. Keene: I doubt it.

Ms. Richardson: I can tell you that two... (Crosstalk).

Mr. Keene: My apologies.

Ms. Richardson: The two that have been our focus really, have been the inventory management and the utility meters because they have some substantial recommendations in them but like I said, we've had to keep rescheduling these meetings because the auditor who is working on those has been sick for the past month; not in the office. Those really have been our focus. We've had to reschedule those meetings a couple of times before that and right now they're scheduled for January.

Vice Mayor Scharff: That's for which audit?

Ms. Richardson: That's the inventory management and utility meters' audits.

Vice Mayor Scharff: Ok, so the two big ones (Inaudible) (Crosstalk).

Council Member Kniss: Greg, you didn't turn on your mic.

Mr. Keene: I didn't mean to be flipped there Mr. Vice Mayor. I just actually Harriet is in a better position to tell you...

Vice Mayor Scharff: She just took the bullet for you. She said it was their fault.

Mr. Keene: ... what might be blocking...

Ms. Richardson: Yes, I will say the rescheduling has been due to my office and I'm hoping that auditor will be back next week.

Vice Mayor Scharff: So, what about the other ones? You know, like the police department?

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Ms. Richardson: That's the animal services audit.

Vice Mayor Scharff: Yeah.

Ms. Richardson: That one is in the City Manager's hands.

Mr. Keene: I don't know if this is an entirely legitimate rationale but the parallel work that we have going on with the assessment of the shelter operations and the transfer you know, has sort of slowed down our response there as we kind of continue to kind of both work through the meet and confer process with labor and try to arrive to the final conclusion with pets in need folks.

Vice Mayor Scharff: That makes total sense. What about disability rates and workers comp? Those are still 15 out of 15 (Inaudible).

Ms. Richardson: That one wasn't actually due yet till February so, that we're good on.

Vice Mayor Scharff: Oh, we're good on that? Ok, you're right because I see past due and then I don't see past due, you're right. Ok. Alright.

Mr. Keene: Took a bullet and dodged a bullet.

Vice Mayor Scharff: She's all good for you tonight. That's all I have.

Council Member Kniss: So, let's follow up on that though with someone who has – this person has been out for quite a while?

Ms. Richardson: She's been out for pretty much all of November.

Council Member Kniss: Do you ever consider ever using a contractor in that case?

Ms. Richardson: We haven't and I don't have the budget for contractors.

Chair DuBois: Couple questions on the continuous monitoring kinds of studies. How are those designed and how are you evaluating whether they're effective?

Ms. Richardson: For example, on the Accounts payable Audit, what we were looking at is we looked at the vendor master file and we also looked at a sample of invoices. We have some software called ACL, it's an audit software that can look at the full database of records without having to do a sample



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and you can put some commands in there to tell it to pull out things that would likely be duplicates and so by doing that, we get a list of potential and then we sort through those to identify which ones are actuals and which ones may be considered false positives and that did help us identify some issues with the vendor master file and also some duplicate payments. Then we worked with Administrative Services Department (ASD) to identify -- for example, those duplicates, did they catch them and correct them or where they still duplicate that they needed to pursue. So, by doing that sort of script with that software, you can monitor on an ongoing basis, did we have a potential duplicate and check it out if you didn't -- if it didn't come to your attention just through the normal process.

Chair DuBois: Ultimately, are you saying, yes this is worthwhile and then there's some software being purchased or?

Ms. Richardson: ASD was looking at the software but I'm not sure if they're going to purchase it. They're going to look at the cost benefit to see if it's worth purchasing, given what we've found in the audit.

Chair DuBois: Same thing with over time...

Ms. Richardson: Yes.

Chair DuBois: ...if you see enough that it pays for the software.

Ms. Richardson: Right.

Chair DuBois: Ok, I don't know if you have any early results from the [Crossbore Contract] or should we just wait?

Ms. Richardson: Yeah, it's a little bit early on that on. We are looking at the potential risk with that contract and we've had some preliminary meetings with utilities so, we know where some of the issues likely are but we haven't confirmed any of that yet.

Chair DuBois: Then, do you know what the year to date -- the previous year to date was? How are we doing on total recovered sales tax?

Ms. Richardson: I don't have that number with me. This year -- last year was quite low, it was lower than normal. I believe it was less than 70,000 for the year...

Chair DuBois: For the year? Ok.

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Ms. Richardson: ... and this is going to be quite a bit higher, primarily because that \$220,000 that the vendor – our consultant recovered... (Crosstalk).

Chair DuBois: That what I was just (Inaudible) (Crosstalk) that was pretty significant.

Ms. Richardson: It's a number that fluctuates quite a bit. Last year was quite a bit low compared to prior years but this year's going to be quite a bit higher, compared to prior years.

Chair DuBois: My last question on the audit recommendation status report. Do we ever end up with recommendations that we just agree that we're not going to fix and should we show that on here?

Ms. Richardson: One of the things since I've been here that I've talked with the City Manager's office about and departments. If a recommendation doesn't make sense at this point, things change – some of these recommendations are quite old and they may not make sense anymore. If that's the case, I've been open to saying, we can close it out and then we treat it as a closed recommendation so, it would just not show up in the open column anymore.

Chair DuBois: So, these are really 73 significant open issues?

Ms. Richardson: Correct.

Chair DuBois: That's good to know. I think that's it. Any other questions? Alright, thank you.

**MOTION:** Council Member Kniss moved, seconded by Vice Mayor Scharff to recommend the City Council accept the Auditor's Office Quarterly Report as of September 30, 2016.

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