



Office of the City Auditor

CONSENT CALENDAR
February 9, 2010

To: Honorable Mayor and Members of the City Council
From: Ann-Marie Hogan, City Auditor
Subject: Audit Report: Public Works Contract Monitoring: Risk of Overpayments / Lack of Inventory Controls

RECOMMENDATION

Request the City Manager to report back on or before January 31, 2011, and every six months thereafter, regarding the implementation status of the audit recommendations in the attached audit report until each recommendation is fully implemented.

SUMMARY

Our review focused on two cost plus contracts and three large purchase orders that Finance identified as warranting review. We found that Public Works needed to clarify contract terms and conditions, and develop procedures to monitor contract compliance. Specifically, Public Works needed to:

- Develop procedures to ensure that fuel and tire purchases were priced according to the vendors' bids.
- Reevaluate overhead and incentive provisions in the Ecology Center contract.
- Require the Ecology Center and Parking Concepts, Inc. to support all claimed costs, including allocated costs.

In addition, Public Works needs to maintain security over tires, and maintain adequate inventory records for tires and other parts.

Effective January 1, 2010, a new multi-year fixed price Ecology Center contract should eliminate problems with the original contract. Public Works staff indicated that, while they were aware of problems in the old contract, our audit was beneficial in developing the new contract.

FISCAL IMPACT OF RECOMMENDATION

Implementing our recommendations should result in cost savings. If total costs of the contracts and purchase orders reviewed could be reduced by just one percent, it would save almost \$62,000 per year. Over a five-year period the cost savings would accumulate to almost \$310,000. Implementing our recommendations would also reduce the risk of theft of tires and other inventory.

RATIONALE FOR RECOMMENDATIONS

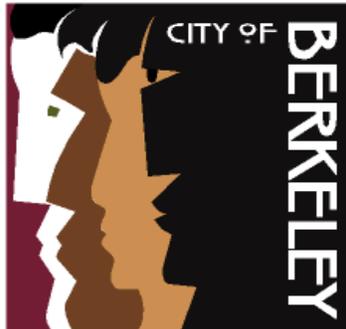
We estimate the annual costs of the contracts and purchase orders we reviewed at over \$6 million. With this level of expenditure, it is critical that Public Works have adequate procedures to monitor contractor performance, ensure goods are priced in accordance with the terms of the contracts or vendors' bids, and safeguard the goods purchased.

CONTACT PERSON

Ann-Marie Hogan, City Auditor, 981-6750

1. Audit Report: Public Works Contract Monitoring: Risk of Overpayments / Lack of Inventory Control

City of Berkeley



Public Works Contract Monitoring **Risk of Overpayments** **Lack of Inventory Control**

Prepared by:

Ann-Marie Hogan, City Auditor, CIA, CGAP
Teresa Berkeley-Simmons, Audit Manager, CIA, CGAP
Jack Gilley, Auditor II, CFE

Presented to Council February 9, 2010

2180 Milvia Street, Berkeley, CA 94704 ♦ Tel.: (510) 981-6750 ♦ Fax: (510) 981-6760
Email: auditor@cityofberkeley.info ♦ Web: www.cityofberkeley.info/auditor

**Public Works Contract Monitoring
Risk of Overpayments
Lack of Inventory Control**

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I. Executive Summary

Audit Objective: Determine if the Public Works Department (Public Works) has procedures and controls in place to ensure that contractors bill consistent with contract specified pricing for goods and services. Provisions in the Ecology Center contract were also evaluated at the City Manager's request.

The City has procedures in place to contract for goods and services. However, Public Works needs to clarify contract terms and conditions, require support for administrative costs, and develop procedures to effectively monitor contract compliance. With Western States Oil, City staff did not monitor billings and several billing errors were not caught or corrected. The Ecology Center contract was complex, and expectations were not clear or independently verifiable, which made monitoring burdensome and inefficient.

Specific audit concerns include:

- Public Works did not have procedures to ensure fuel and tire purchases were priced in accordance with the vendors' bids (Findings 1 and 2).
- Public Works did not maintain security over tires, and did not maintain inventory records (Finding 3).
- Public Works needed to reevaluate performance incentive provisions, and clarify the basis for overhead and administrative cost allocation in the Ecology Center contract. (Findings 4, 5, and 6).
- Public Works should require Parking Concepts, Inc. to support all claimed costs (Finding 7).

A new Ecology Center contract was negotiated by Public Works and authorized by Council in December 2009. According to Public Works, the City will now pay a flat monthly fee for Ecology Center services.

II. OBJECTIVES OF THE AUDIT

The purpose of the audit was to determine if Public Works has procedures and controls in place to ensure that contractors bill consistent with contract specified pricing for goods and services. The audit was initiated due to Office Depot overcharging the City by more than \$280,000

Because a new Ecology Center contract was being negotiated, the City Manager requested that we look for ways to improve the contract and determine if contractual “bonuses” (provisions that increase payments under the contract beyond the contractor’s costs) are reasonable.

III. BACKGROUND

The Public Works Department is responsible for the City’s infrastructure. Public Works:

- Cleans and repairs City streets, curbs, sidewalks, sewer system, storm drains, streetlights and parking meters;
- Maintains, coordinates, and manages all trails, pathways, traffic signs and signals, and pavement markings;
- Removes solid waste;
- Oversees the City’s recycling program;
- Maintains City owned vehicles;
- Cleans and maintains City owned buildings; and
- Oversees Parking Operations and Services.

Western States Oil Company

The City purchases fuel for the City’s fleet from Western States Oil Company (Western States). Public Works’ Equipment Maintenance Division is responsible for ordering fuel, and reviewing Western States invoices.

The City purchased almost \$1.3 million in fuel from Western States and over \$125,000 in tires from Inland in FY 2009.

Inland Industrial Tire North

Public Works purchases tires for the City's fleet from Inland Industrial Tire North, Inc. (Inland) under a blanket purchase order. The vendor's bid contains a price list for various tire types. It also limits price increases to the lesser of the percentage increase in the Consumer Price Index or four percent per year. The Equipment Maintenance Division is also responsible for ordering tires and reviewing Inland invoices.

Ecology Center

The Ecology Center is a Berkeley based non-profit corporation. The City has contracted with the Ecology Center to operate the curbside recycling program since June 1992.¹ The current contract ended December 31, 2009, and cost approximately \$25 million for the 17 year period.²

The contractor is reimbursed for recycling costs, less revenue from sale of recyclable material. Public Work's Solid Waste Division manages the contract.

In FY 2009 the City paid the Ecology Center over \$2.2 million for curbside recycling, and paid PCI almost \$1 million to manage the City parking garages.

Parking Concepts, Inc, (PCI)

In August 2003, the City contracted with PCI to manage City owned public parking garages. The City reimburses PCI for its cost plus a \$4,000 monthly management fee. The contract amount is \$7,019,000 for a seven year period ending June 30, 2010. Public Work's Transportation Division manages the PCI contract.

The City purchased over \$171,000 in plastic carts for refuse collection from Toter in FY 09.

Toter Incorporated

The City purchases plastic carts from Toter Incorporated for residents to use for refuse collection. The Solid Waste Division is responsible for ordering carts and reviewing the vendor's invoices.

¹ In addition to the City's recycling program, the Ecology Center operates three farmers' markets, a library, and the EcoHouse demonstration house. It also publishes Terrain Magazine. Additional information about the Ecology Center can be found at [Ecology Center](#).

² We could not determine the exact amount due to the way the amendments were written.

IV. FINDINGS AND RECOMMENDATIONS

Finding 1: Ensure Fuel Purchases Are Priced in Accordance with Vendor's Bid

Neither the Equipment Maintenance Division nor Finance staff was checking Western States Oil Company (Western States) invoices to ensure pricing was consistent with the vendor's bid. Also, Public Works did not have written procedures to ensure that fuel purchased from Western States was priced according to the vendor's bid. Both overcharges and undercharges were not detected by City staff. The City spent over \$1,300,000 for fuel from Western States Oil Company in fiscal year 2009.

The Western States bid calls for fuel to be priced based on an index of gasoline and diesel prices for the San Francisco area published by Oil Price Information Service (OPIS). The Equipment Maintenance Division, which orders fuel and reviews fuel invoices, receives price quotes from Western States based on changes in the OPIS index. Equipment Maintenance Division staff did verify that the price quotes were based on the OPIS index. Also, Public Works relied on Western States Oil to provide the OPIS index.

Because we found an error in an April 2, 2009 invoice,³ Western States reviewed all City invoices for the period of the blanket purchase order.⁴ Nine additional erroneous invoices were reported by the vendor with net overcharges of \$3,448, but the vendor incorrectly recalculated the April 2 invoice.⁵ The 10 erroneous invoices plus the error in correcting an invoice highlight the need for Public Works to thoroughly review fuel invoices.

³ The City was undercharged by \$4,658.

⁴ Western States submitted its bid in October 2007. Therefore the invoice review covered billings to the City for more than 1 ½ years.

⁵ The vendor applied the bid specified add-on for gasoline to biodiesel.

Recommendations for Public Works

- 1.1 Develop written procedures to instruct Corporation Yard staff on review of Western States Oil invoices. The procedures should require matching the invoice price to the price quote, and the price quote to the OPIS index.
- 1.2 Ensure that Corporation Yard staff adheres to written procedures to be developed under recommendation 1.1.
- 1.3 Maintain a subscription to the OPIS index for San Francisco independent of Western States Oil Company.
- 1.4 If frequent errors are found in future invoices, consider independently reviewing a sample of past Western States invoices to determine if previous erroneous billings are pervasive.

City Manager's Response

The Director of Public Works agrees with the finding and recommendations. The Senior Equipment Supervisor now matches up and checks each invoice against the OPIS index for the specific day to verify that the City is being charged the correct pricing. The Equipment Superintendant will randomly check to ensure that this procedure is being followed. These procedures were adopted during the audit and documented in November 2009. Public Works now has its own OPIS subscription received daily independent of Western States Oil. If frequent errors are found in future Western States invoices, Public Works will consider reviewing a sample of past invoices to determine if past billing errors are pervasive. Recommendations 1.1 through 1.4 are fully implemented. (Conclusion)

Finding 2: Ensure Tire Purchases Are Priced in Accordance with Vendor's Bid

Public Works staff did not verify that tires purchased from Inland Industrial Tire North (Inland) were priced consistent with the vendor's bid price. As a result, an overcharge would not have been detected. The City purchased more than \$125,000 in tires from Inland in fiscal year 2009.

Incorrect pricing would not have been detected.

Inland's bid contains a price list for various tire types. It also limits price increases to the lesser of the percentage increase in the Consumer Price Index or four percent per year. The Equipment Maintenance Division did not compare billed prices to the price list. There were no written procedures for review of tire invoices.

Recommendations for Public Works

- 2.1 Include tire invoice review in the written procedures developed under Recommendation 1.1. The written procedures should include a requirement to verify that purchased tires are priced not to exceed the vendor's bid price as adjusted for allowable increases, and that such review is documented. The U.S. Bureau of Labor Statistics' inflation calculator at www.bls.gov/data/inflation_calculator.htm can be used to calculate changes in the Consumer Price Index.

City Manager's Response

The Director of Public Works agrees with the finding and the recommendation. Upon receipt of new tire invoices, the Warehouse Operations Specialist matches up and checks each invoice against the stated contract pricing to verify that the City is being charged the correct contract pricing. This procedure was adopted during the audit and documented in November 2009. Recommendation 2.1 is fully implemented.

Finding 3: Improve Physical Security and Accountability for Inventory of Tires and Other Parts (Repeat Finding: March 15, 2005)

Public Works does not keep the inventory of tires at the Corporation Yard in a secured area, and it does not maintain adequate inventory records for tires and other parts. As a result, the risk of a theft going undetected is significantly increased. Public Works cannot determine if all tires and other inventory parts that should be present are in fact present.

Tires at the Corporation Yard are stored in unlocked areas on the ground floor work area, and mezzanine. All staff working in these areas have access. There is no back-up when the employee responsible for parts management for the Corporation Yard and Transfer Station is not present. Six employees hold the key to the padlock that secures the tire cage at the Transfer Station.

The only record of tires and other parts is an annual physical inventory, which is ineffective. The annual inventory is not reconciled to the prior year's inventory, or to purchases and usage.

Inventory at the Corporation Yard is vulnerable to theft.

These conditions were also reported in our March 15, 2005, report entitled "[Purchase Order Audit – Select Public Works Divisions at the Corporation Yard.](#)" We reported that tires and other parts were not adequately secured, and no inventory record was maintained. Recommendations 5.1 and 5.2 were intended to remedy these problems.

Reported corrective actions not in place.

On May 16, 2006, the City Manager reported to Council that Recommendation 5.1 and an alternative to Recommendation 5.2 had been implemented. Specifically, a year-end parts inventory would be conducted and the beginning and ending inventory value would be compared and reconciled with parts and services billed. Also tires at the Corporation Yard would be located in the mezzanine, and only two employees would have a key to the tire cage at the Transfer Station. The reported corrective actions are not in place.

Recommendations for Public Works

- 3.1 Keep tires in a locked cage. At a minimum, maintain dual custody with two padlocks, with no employee having the key or combination to both padlocks.
- 3.2 Have an employee independent of the Equipment Maintenance Division reconcile the annual physical inventory to the prior year's inventory of tires and other parts, and report the results to the Director of Publics Works. The reconciliation should account for tires purchased and used during the year. An overage or shortage should be investigated.

- 3.3 Consider establishing perpetual inventory records for tires and other parts. Link inventory additions to purchase orders (or delivery documents, if there is a blanket purchase order). Also link inventory usage to job orders.

City Manager's Response

The Director of Public Works agrees with the finding. Public Works implemented alternative action to manage risk of asset loss. Tires are stored in a locked cage at the Transfer Station. The Supervisor will be the only one with the key to the lock and will pass the key to the Lead Mechanic at the end of his shift. Public Works plans to store all tires at the Corporation Yard in the mezzanine and secure them by locking the elevator access. Only the Warehouse Operations Specialist will have the key, with the Supervisor acting as the backup when the Warehouse Operations Specialist is absent.

Public Works will account for inventory starting with a pilot program for tires. Public Works will perform a reconciliation of tires on hand to those identified in the prior physical inventory count. The reconciliation will use SunGard/HTE⁶ records of tire purchases and installations (inventory additions and deletions) to reconcile to the prior physical inventory. A Public Works employee independent of the Equipment Maintenance Division will participate in or review the reconciliation and verify the count. The reconciliation will be documented in writing. If the pilot program is effective, the process will be expanded to other targeted inventory parts, such as radios. Public Works will evaluate the need to maintain dual custody of tires based on the results of the tire reconciliation.

Public Works would like to establish a perpetual inventory system. However, it was concluded that a perpetual inventory system would not be feasible due to the limitations of SunGard/HTE. Recommendations 3.1 and 3.2 are partially implemented. Recommendation 3.3 is fully implemented.

⁶ SunGard/HTE is the City's financial software.

Finding 4: Reevaluate Overhead Provisions in the Ecology Center Contract

Provisions in the Ecology Center contract are not clear. The contractor is paid a flat 15 percent of incurred costs to cover “reserves and contingencies,” as well as “general organizational overhead.” The provision is ambiguous in that it does not specify what future events are being provided for by “reserves” or “contingencies.”

The contract does not require the Ecology Center to record and submit actual overhead costs, and it does not provide for adjustments to actual overhead costs. Therefore, the City cannot be assured that 15 percent is reflective of the contractor’s actual overhead. The 15 percent overhead rate has been in place unchanged since the contract’s 1992 inception. Based on the amount awarded under the current contract amendment, the City will expend approximately \$442,000 in overhead payments to the Ecology Center in FY 2010.

Recommendation for Public Works

- 4.1 Consider requiring the Ecology Center to periodically provide support for actual overhead costs, and adjust the overhead rate as indicated. For example, the contractor could be asked to submit support every two or three years, or when a new contract or amendment is negotiated. A factor to consider is the costs that both the Ecology Center and the City would incur to document and review actual overhead.

City Manager’s Response

The Director of Public Works agrees with the finding and an alternative recommendation was implemented. The City has negotiated a new contract with the Ecology Center effective January 1, 2010. The new contract was authorized by Council December 2009. The City will pay a flat monthly fee for Ecology Center services. Public Works will no longer need to verify actual costs.

Finding 5: Reevaluate Incentive Provisions in Ecology Center Contract

The Ecology Center contract contains various performance incentives that can decrease or increase payments to the Ecology Center. Some performance incentives are self-reported and not independently verifiable. The contract contains performance incentives to reduce missed routes, missed pick-ups, and litter complaints, with performance targets for each incentive. Payment is increased if the actual number of occurrences is less than the target, but reduced if the actual exceeds the target.

Performance Self-Reported

The City is dependent on the Ecology Center to accurately self-report results of their performance incentives. Customers usually contact the Ecology Center with complaints, and only contact the City if they fail to obtain satisfactory resolution.⁷

Cost Containment Incentive

The contract also has a cost containment incentive target which may not be sufficiently challenging. If actual costs are less than target costs, the Ecology Center receives a bonus of 20 percent of the savings. But if actual costs exceed target costs, payments are reduced by 20 percent of the overrun.

At issue:
Do incentives drive better performance and reduce costs?

There could be potential benefit from the performance incentives, provided the targets are challenging. Public Works should be confident that the incentives motivate recycling workers and their supervisors to strive for fewer missed routes, pick-ups, and litter complaints. Also, the benefits derived from performance incentives should justify the cost of monitoring performance.

The performance incentives only address risks to service delivery, and not other risks to the City. For example, there are no performance incentives for accidents. Recycling crew accidents could drive up the contractor's workers' compensation and general liability insurance premiums enough to substantially increase the contract costs.

⁷ Based on the March 2009 billing, the performance based payments are not large. The Ecology Center claimed \$1,490 in bonuses for these incentives in March.

We expressed our concerns about the overhead (Finding 4) and incentive provisions in a June 9, 2009 memorandum to the Director of Public Works.

Recommendations for Public Works

- 5.1 With input from the Ecology Center, re-evaluate the benefits of the performance incentives. Factors to consider are the reliability of the self-reported performance data, the administrative costs of monitoring performance incentives, and whether they actually result in fewer missed routes, pick-ups, and litter complaints.
- 5.2 With input from the Ecology Center, re-evaluate whether the cost containment incentive reduces the cost of the recycling service.
- 5.3 If Public Works decides to retain the incentives, review bonuses and penalties over a period of three to five years. If the bonus/penalty pattern indicates that the performance targets may not be sufficiently challenging, consider the need to adjust the targets.
- 5.4 Consider the need for performance incentives that address other risks to the City.

City Manager's Response

The Director of Public Works agrees with the finding. The City has negotiated a new contract with the Ecology Center effective January 1, 2010. The new contract was authorized by Council December 2009. The City will pay a flat monthly fee for Ecology Center services. Performance and cost containment incentives are not components of the new contract. An alternative to recommendations 5.1 through 5.4 has been implemented.

Public Works was aware of problems related to the overhead and incentive provisions in the old contract. The audit process informed Public Works' contract development, and the timing of the audit was useful in developing the new Ecology Center contract.

Finding 6: Clarify Basis for Allocating Administrative Costs and Improve Review of Ecology Center Invoices

Administrative Cost Allocations Not Documented

We could not determine if the administrative cost charged to the City was appropriate.

In its March 2009 invoice, the Ecology Center allocated various administrative expenses between recycling (charged to the City), and other projects, without providing documentation to support the allocations. The Ecology Center contract does not specify how the contractor is to allocate administrative costs. As a result, Public Works had no assurance that the City was charged a fair and equitable share of administrative costs, or that all claimed costs benefited the recycling program. The Ecology Center charged the City over \$26,000 in administrative expenses in March 2009.

The most significant allocated expenses were administrative salaries,⁸ related employee benefits (over \$22,000 in March 2009), liability insurance and professional services. The contractor submitted payroll registers with the monthly invoice to support salaries and payroll taxes. The Ecology Center's Financial Manager stated that the submitted payroll registers only reflect the portion (75%) of the contractor's payroll allocated to recycling. Public Works did not have evidence that payroll expenses had been allocated, or support for the percent allocated to recycling.

Need for More Thorough Invoice Review

The Solid Waste Division is responsible for review and approval of the Ecology Center's monthly billing. The lack of documented support for cost allocations suggests that Solid Waste may not be adequately reviewing the billings.⁹

Public Works did not have written procedures for review of Ecology Center's billings. Written procedures could help Public Works identify the types of issues found in our audit.

⁸ This refers to the salaries of the Director, Deputy Director, and Financial Manager.

⁹ For example, a vendor's quote was billed as an actual expenditure. Although this charge was for a small amount, Solid Waste should have found the error. The Ecology Center acknowledged the error, and we advised Solid Waste to be alert for a credit in a future billing.

Recommendations for Public Works

- 6.1 Require the Ecology Center to provide adequate documentation to support its allocation of administrative salaries and related expenses. Support should include an explanation of the basis for allocation, and demonstration of related calculations. The supporting labor distribution schedules should cover total salaries that are allocated, not just the portion allocated to recycling.
- 6.2 Consider amending the contract to specify the basis for allocating administrative salaries and related costs.
- 6.3 Require the Ecology Center to support allocation of other expenditures between recycling and other projects.
- 6.4 Review the monthly invoice from the Ecology Center more thoroughly. The review should provide assurance that all claimed costs are supported and that all indirect costs are logically allocated between recycling and other projects.
- 6.5 Develop written procedures on how to monitor and review the Ecology Center's performance and billings.

City Manager's Response

The Director of Public Works agrees with the finding. The City has negotiated a new contract with the Ecology Center effective January 1, 2010. The new contract was authorized by Council December 2009. The City will pay a flat monthly fee for Ecology Center services. The new flat fee contract will eliminate the need to document administrative costs. An alternative to Recommendations 6.1 through 6.5 has been implemented.

Finding 7: Require Parking Concepts International to Support All Claimed Costs

Parking Concepts, Inc. (PCI) submitted vendor invoices and other supporting documentation with its monthly billing. But the documentation provided did not support the following expenses claimed for the three months ended March 31, 2009:

We could not determine if the payroll taxes, workers comp, and liability insurance charged to the City were appropriate.

Payroll Taxes	\$20,185
Workers' Compensation Insurance	19,695
General Insurance	<u>2,964</u>
Total	<u>\$42,844</u>

Without adequate documentation, Public Works did not have assurance that the City was billed for the Contractor's actual costs, or for a fair and equitable portion of allocated costs.

Public Works' desk procedures for review of PCI invoices do not require support for these expenses. The procedures state that payroll taxes and workers' compensation should be approximately 11.69 percent each, (presumably as a percent of salaries). They also state that general insurance is \$1,144.60 per month, but only \$1,053 was claimed for March 2009. Public Works does not know if PCI ever submitted support for the 11.69 percent, or the \$1,144.60 amount. Public Works plans to update the desk procedures.

Recommendation for Public Works

- 7.1 Require PCI to submit adequate documentation to support workers' compensation costs, payroll taxes, and general insurance premiums. Support could include payroll registers, invoices for workers' compensation and general insurance premiums, and allocation worksheets.
- 7.2 Update Public Works' written procedures for review of the monthly PCI billings and revenue report. The written procedures should specify what documentation the contractor is required to submit to support each expense.

City Manager's Response

The Director of Public Works agrees with the finding and the recommendations. PCI has been unable to provide documentation for workers' compensation costs, payroll taxes, and general insurance premiums specific to PCI staff working at the City of Berkeley garages. The company's monthly ledgers for these three items are inclusive of all company employees in the State.

The current City of Berkeley/PCI contract expires in 6-months (June 2010). The new contract will likely not be a cost plus contract requiring verification of actual costs, but rather a fee for service contract. If, however, the contract requires verification of these costs, this provision will be included in the new contract language. Public Works will update its written procedures with issuance of the new contract by January 2011. Recommendations 7.1 and 7.2 have not been implemented.

Finding 8: Improve PCI's Accuracy and Accountability for Parking Revenue by Requiring Signatures on Cash Counts

PCI cash count forms were not always signed by the cashier or a verifier (witness), though design of the forms calls for both signatures. As a result, accountability for parking revenue was diminished.

PCI submits a daily Cashier Report Entry Form for each parking garage to support parking revenue. This form is designed to record the count of cash and credit card receipts by each cashier for each shift. The form has lines for the cashier and a verifier (count witness) to sign to attest to the accuracy of the count.

Dual custody when performing cash counts is an internal control to safeguard cash.

Of the six Cashier Report Entry Forms reviewed for the Telegraph/Channing garage for May 2, 2009, two (33 percent) were not signed by the cashier, and three (50 percent) were not signed by a verifier.

Signing the cash count form attests to the accuracy of the count, and holds the signor(s) accountable for its accuracy. A witness to the count reduces the risk of errors and irregularities.

Recommendation for Public Works

- 8.1 Ensure that PCI requires cashiers to always sign the Cashier Report Entry Forms.
- 8.2 Ensure that PCI, to the extent cost effective, requires a second employee to witness the cash counts and sign the Cashier Report Entry Forms as a verifier. If it is not possible to have a second witness, ensure that PCI holds employees accountable for the accuracy of cash counts and that PCI will enforce

disciplinary action on persons who frequently have cash overages or shortages.

City Manager's Response

The Director of Public Works agrees with the finding and the recommendations. As of September 2009, Public Works has taken steps to ensure that PCI requires cashiers to sign each Cashier Report Entry Form. Public Works staff monitors this requirement daily. PCI has procedures in place that requires a second employee to witness the cash count and sign the Cashier's Report Forms as verifier. Recommendations 8.1 and 8.2 are fully implemented.

Finding 9: Request Toter Incorporated to Itemize the Unit Price of Plastic Refuse/Recycling Carts

Toter Incorporated (Toter) invoices do not itemize the cost of each plastic cart option. Therefore, Public Works does not have assurance that carts are priced appropriately. As a result an overcharge would not be detected.

The Solid Waste Division purchases plastic carts for residents' refuse and commercial recycling collection. The carts are purchased from Toter under its agreement with the National Intergovernmental Purchasing Alliance (NIPA), which allows participant jurisdictions to piggy-back a contract with the City of Tucson.

No assurance that the City was properly billed for carts.

Solid Waste cannot verify that the invoiced unit cart price agrees with the Tucson contract. The Tucson unit price is a baseline price as Berkeley has cart options that differ from Tucson's (for example, the City's logo and serial numbers). The Toter invoices do not break out the unit price by showing the Tucson base price plus the price of each Berkeley option.

Recommendation for Public Works

- 9.1 Request Toter to itemize the unit price of each type of cart by showing the Tucson base price, and the price of each Berkeley option.

City Manager's Response

The Director of Public Works agrees with the finding and recommendation. When the next order is placed with Toter, Public Works will ask the vendor to break out the Tucson base price on the invoice from the Berkeley specific additions.

V. FISCAL IMPACT

We estimate the annual costs of the contracts and purchase orders reviewed at almost \$6.1 million, as follows:¹⁰

Ecology Center	\$3,388,000
PCI	1,133,026
Western States Oil	1,271,406
Inland Industrial Tire Company	125,470
Toter Incorporated	<u>171,207</u>
Total	<u>\$6,089,109</u>

If Public Works could reduce the cost of these contracts and purchase orders by just one percent through improved contract administration and more thorough invoice review, the City would save more than \$62,000 per year. Implementing our recommendations would also reduce the risk of theft of City assets such as tires and other inventory.

VI. CONCLUSION

Public Works needed to strengthen oversight of contracts and purchase orders. Identified weaknesses increased the risk of overcharges, and decrease the likelihood of detecting overcharges. Specifically, Public Works needed to:

¹⁰ The amounts shown for the Ecology Center and PCI are based on the amounts awarded in the most recent contract amendments in place on July 31, 2009. The amounts shown for the other vendors are actual FY 2009 expenditures.

- Ensure that the price of fuel purchased from Western States was based on the OPIS index for San Francisco (Finding 1);
- Ensure that tires purchased from Inland were priced according to the vendor's bid (Finding 2);
- Require PCI to support all claimed costs (Finding 7); and
- Request Toter to itemize the Unit Price of plastic refuse and recycling carts (Finding 9).

Also, Public Works needed to improve physical security over tires, and maintain adequate inventory records for tires and other parts (Finding 3, a repeat finding). Furthermore, PCI needed to improve accountability over parking revenue by requiring dual signatures on cash counts (Finding 8).

According to Public Works, a new fixed price contract was negotiated with the Ecology Center (authorized by Council December 2009). The concerns we expressed in the June 9, 2009 memorandum to Public Works were considered in the negotiations. The new contract should eliminate problems that Public Works and Audit found in the original contract (See findings 4 through 6 above).

Also, Public Works plans to negotiate a fixed price contract with PCI when the current contract expires in June 2010.

Decisions to contract for services should always factor in plans for contract monitoring. To effectively contract for goods and services the contract must be clear, and the department must have the resources and procedures in place to monitor contract compliance.

We wish to thank the Director of Public Works, the Executive Director of the Ecology Center, and their staff for their time, cooperation, and responsiveness during the audit.

APPENDIX A

SCOPE AND METHODOLOGY

This report is based on a preliminary survey of contract monitoring procedures in Public Works. It was planned as part of a series of contract oversight improvement reports. We did not perform an audit of the contractors selected for survey work.

We identified concerns with monitoring procedures that merited prompt reporting. Audit work was limited to the contract monitoring procedures in place in the Public Works Equipment Maintenance, Solid Waste, and Transportation Divisions. For information about contract monitoring for construction contracts in Engineering, see our February 2007 [Follow-Up Audit of Public Works Construction Contracts](#).

After Office Depot overcharged the City by more than \$280,000, Audit and Finance met to discuss priorities in auditing contracts. Finance staff discussed the inherent risks of cost plus contracts in general, and identified two cost plus contracts and three large purchase orders.

Preliminary survey work focused on identifying contract monitoring procedures in place in the Public Works divisions responsible for these contracts and purchase orders.

Public Works staff were asked to explain and illustrate procedures for: 1) review of billings to ensure the City was charged according to contract or bid terms, and 2) custody and control of tires and other parts. At least one billing received from each vendor was reviewed to understand Public Works' procedures.

We also determined the status of two recommendations in our March 15, 2005, report entitled "[Purchase Order Audit – Select Public Works Divisions at the Corporation Yard](#)." These recommendations relate to safeguarding of tires and other inventory.

Field work was conducted between April and July 2009 and was limited to those areas specified above. We conducted this survey in accordance with *Generally Accepted Government Auditing Standards (GAGAS)*. 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Section 2.24.050 of the Berkeley Municipal Code requires the City Auditor to review, countersign, number, and register all contracts. We believe this function did not impair our compliance with GAGAS standards for auditor independence.

This performance survey was initiated by the Auditor's Office and scheduled as part of the fiscal year 2010 Audit Plan, which was presented to Council on June 23, 2009.