



Office of the City Auditor

INFORMATION CALENDAR

September 9, 2014

To: Honorable Mayor and Members of the City Council
 From: Ann-Marie Hogan, City Auditor
 Subject: City Auditor's Office 2013-14 Report

INTRODUCTION

The aim of the City's Auditor's Office is to monitor the effectiveness, efficiency, and equity of City programs, and make recommendations that assist City management in improving operations. As part of our efforts to communicate our success, we are providing the City Council with information on the outcome of our performance audits and special reports, and our efforts to continuously improve our services.

CURRENT SITUATION AND ITS EFFECTS

We succeeded in our goal to improve City operations, save money, promote transparency and accountability, and deter fraud. This includes successfully closing 56 recommendations and nine audits through the efforts of the City Manager and city staff. We took on many challenges to improve city operations and our own practices. We:

- Focused our audits on uncovering the root cause of performance shortfalls, making stronger recommendations to strengthen operations and procedures on a *citywide* basis, and using existing data to improve performance.
- Continued in our mission to send a strong message about the risks of across-the-board budget cuts that eliminate the support, administrative, and oversight staff that help protect City assets and ensure ongoing delivery of direct services.
- Invested time in undergoing a peer review that ensures we conducted our audits objectively, professionally, and fairly. We were awarded the highest rating possible for quality, professionalism, and adherence to auditing standards.
- Completed an overhaul of our audit procedures and nonaudit services, and created electronic workpapers and quality-control systems to help us become more efficient and "green."
- Complied with new federal and state laws related to City payroll operations, and made recommendations for the City Manager to present in the upcoming Berkeley Police Association labor negotiations aimed at reducing costs, clarifying ambiguous language in the current union agreement, and improving City compliance with evolving federal and state laws.

BACKGROUND

We conduct high-quality audits with competence, integrity, objectivity, and independence by following federal government auditing standards. Using these standards to guide our work requires us to undergo regular peer reviews, remain independent from management, publicly disclose our work, and receive sufficient funding for our audits.

ENVIRONMENTAL SUSTAINABILITY

We manage and store our audit workpapers and other documents electronically to significantly reduce our use of paper and ink. The audits we discussed in this report included recommendations that support the City's environmental sustainability goals. They include recommendations that will help management save paper, reduce the use of printer ink, and reduce carbon footprints by providing some services online.

POSSIBLE FUTURE ACTION

The action Council takes to ensure timely action on our open recommendations should result in additional savings and risk reduction, including fraud risk.

FISCAL IMPACTS OF POSSIBLE FUTURE ACTION

Audit work can lead to new revenue, cost recovery, and increased efficiency, with economic impact well beyond the audit costs. Long-range financial benefits of the audits we completed should result in significant improvements to internal controls and improved efficiency and effectiveness of citywide services.

Reducing fraud risk does more than save money; it helps build trust in government. Maintaining a strong audit function and prudent fiscal and program management will reduce future costs and enhance public trust.

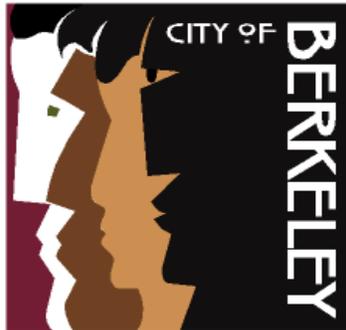
CONTACT PERSON

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Attachments:

1: City Auditor's Office 2013-14 Report

City of Berkeley



City Auditor's Office 2013-14 Report

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Presented to Council on September 9, 2014

TABLE OF CONTENTS

City Auditor’s Message.....	1
City Auditor’s Office Update: Going Green, Efficiencies, and Meeting Standards.....	2
Staffing Losses Put Service Delivery at Risk	2
Better Data, Root-Cause Analysis, and Performance Monitoring Systems Needed.....	3
Prioritize Protection Against Fraud	3
City Auditor’s Budget Impact Reports and Berkeley-Based Budgeting	4
Follow-up on Outstanding Audit Recommendations	5
Transparency and Risk Reduction.....	6
About Us	7
Conclusion.....	7
Appendix A: Summary of Open Recommendations as of June 30, 2014	8
Appendix B: Information on Open Recommendations.....	9

City Auditor's Message

The City Auditor is the oldest continuously elected office in the City of Berkeley, established in the first City Charter in 1895. Serving as part of the checks and balances over City Manager authority, the Auditor's office continues to be an essential element of public accountability.

We achieve that goal through our performance audits by monitoring the effectiveness, efficiency, and equity of city programs, and making recommendations that assist management in improving operations. We work to prevent fraud and protect City assets. We provide insight into the City's actions by considering the short- and long-term effects.

We conduct high-quality audits with competence, integrity, objectivity, and independence by following federal government auditing standards. Using these standards to guide our work requires us to undergo regular peer reviews, remain independent from management, publicly disclose our work, and receive sufficient funding for our audits.

*You have done it again!
That is, you have
succeeded in putting on
the table a subject the city
badly needs to address.
- Community member*

In 2013-14, we succeeded in our mission to improve performance of City operations, save money, promote transparency and accountability, and deter fraud. The City Manager and city staff

helped this happen by agreeing to implement 42 new recommendations. As reported to Council in [June 2014](#), the City Manager also made it a high priority to have City staff implement our older recommendations.¹ City staff worked to ensure Council received timely status reports, implemented 56 of our recommendations, and closed nine audits.

By emphasizing the root cause of performance shortfalls, demonstrating how recommendations in one audit can yield results when applied citywide, and monitoring the execution of planned improvements, we work together to improve public service.

OUR MISSION

To be a catalyst for improving city government. Our audits, mandated by the City Charter, provide the City Manager, City Council, and the public with objective, timely, and accurate information about how well City programs and activities are performing. We help hold government accountable in its stewardship of the public trust.

AUDITS AND REPORTS²

- [Construction Permits – Monitor Performance and Fee Assessments to Ensure Excellent and Equitable Customer Service](#)
- [Berkeley Based Budgeting](#)
- [\\$52,000 Theft: More Can Be Expected Without Citywide Changes in Culture and Procedures](#)
- [Shelter Plus Care: Fully Compliant but Vulnerable to Staffing Cuts](#)
- [Follow-Up on Outstanding Audit Recommendations](#)
- [City Auditor's Budget Report](#)
- [Peer Review: Audit of the City of Berkeley Auditor's Office](#)
- [City Auditor's Annual Report](#)
- [City Auditor's Annual Report Discussion](#)

¹ June 3, 2104: http://www.ci.berkeley.ca.us/Clerk/City_Council/2014/06_Jun/Documents/2014-06-03_Item_35_Update_on_Outstanding_Audits.aspx

² All our reports can be found on our website at: http://www.ci.berkeley.ca.us/Auditor/Home/Audit_Reports.aspx

City Auditor's Office Update: Going Green, Efficiencies, and Meeting Standards

We made our office more efficient and more “green” by developing electronic workpapers and quality-control systems. By using existing city-supported software, we minimized the upfront and long-term costs to make this happen. We also created a centralized, electronic system to help auditees track their open recommendations. City staff have expressed their appreciation for this system.

We invested time in undergoing a [peer review](#) that ensures we conducted our audits objectively, professionally, and fairly. Our peer reviewers awarded us the highest rating possible for quality, professionalism, and adherence to Generally Accepted Government Auditing Standards.³ The reviewers commented that we excel in our dedication to improvements and efficiencies, earn a high level of trust from management, and operate in a very professional and collaborative manner.

We completed an overhaul of our audit procedures and non-audit services to ensure we meet revised and more rigorous federal standards for independence and quality control. This resource-intensive effort also helped develop a structured audit approach and improve our communication with our auditees. Both have made us more efficient in our work.

Staffing Losses Put Service Delivery at Risk

Continued reductions in oversight staff could limit the City's ability to adequately manage and monitor much needed programs. We expressed our concerns about this in our [Shelter Plus Care](#) audit in which we noted that \$2.5 million in federal grant funding used to provide housing assistance to homeless people and their families is at risk. The Shelter Plus Care program's complexity makes it challenging to manage. Remarkably, Health, Housing, and Community Services' experienced and knowledgeable staff successfully administered the program in accordance with federal regulations with just 2.3 employees. This is 62 percent of HUD's suggested level. Further staffing reductions would increase the risk of errors or fraud, and could mean that the City would no longer have the capacity to offer the program.

Further budget cuts could jeopardize programs like Shelter Plus Care's supportive housing assistance, funded by \$2.5 million in grants

Continued, across-the-board budget cuts could have similar effects on other city programs. Council has chosen to keep as many programs as possible, but with fewer staff. This could result in administrative staff being unable to effectively monitor those programs, and could impact management's ability to accurately identify and address risks.

Cuts to oversight and support functions are also potential root causes for our findings in our recently released [Zero Waste](#) audit. City resources are stretched and this problematic trend for oversight will continue as the City slowly recovers from the economic downturn and the effects of insufficiently scrutinized state and local pension decisions.

³ GAO's Generally Accepted Government Auditing Standards: <http://www.gao.gov/yellowbook/overview>

Better Data, Root-Cause Analysis, and Performance Monitoring Systems Needed

We focus on finding the root cause of performance shortfalls and using our audits to demonstrate better ways management can use existing data. As revealed in our [Planning and Development Department's Permit Service Center \(PSC\) Division](#)

Management must monitor performance to ensure excellent and equitable customer service and prevent fraud

audit, management is not using construction permit data to routinely evaluate performance to understand the root causes for not meeting established performance goals and for long customer wait times, and ensuring that customers are assessed fees accurately, consistently, and equitably. Our upcoming audit of [police injuries](#) also looks at how management can improve its practices and data-collections methods to understand the root cause of workplace injuries.

Our PSC audit also touches upon long-standing concerns: staff sharing computer login credentials and performing inappropriate combinations of activities in city systems. These practices could allow staff to improperly initiate or change information without review. In fact, a former employee successfully hid theft by using other staff's log-in information to access the City's financial system. Our detailed investigation of this theft led us to see that the root cause rested with management oversight. We discuss that audit next.

Prioritize Protection Against Fraud

City Council and all City managers need to make protection from fraud a high priority and guard against the common "management myth" that fraud does not exist. Our [Parks, Recreation, and Waterfront \(PRW\)](#) audit revealed a theft of

Staffing reductions have led to insufficient administration and oversight to prevent fraud and errors.

at least \$52,000 because City management had not fully understood and implemented cash-handling procedures and had received insufficient guidance from the Finance Department. We made 129 recommendations to improve cash handling throughout the City in audits we performed during the past ten years, and an outside consultant made 50 such recommendations in 2001. In spite of these efforts, significant weaknesses in procedures continued to exist in City procedures and practices, providing opportunities for thefts to be committed and concealed.

Council's elimination of staff positions responsible for cash-handling and other fiscal activities exacerbates the problem. Across-the-board budget cuts play a role in this area. Without adequate administrative and oversight positions, City staff cannot effectively monitor fiscal operations.

We performed our PRW audit because an observant employee identified a \$650 anomaly in cash receipts records and followed City policy by reporting the error. We identified the specific weaknesses that allowed the theft to occur and made strong and detailed recommendations to ensure that appropriate procedures are implemented on a *citywide* basis to prevent future thefts of City funds. Our work also helped the City recover just over \$47,000 of the stolen funds.

City Auditor's Budget Impact Reports and Berkeley-Based Budgeting

We continue to be concerned about cuts to oversight and support functions. As we have mentioned in this report, these budget cuts have proven to be the root cause of some the problems we identified in our audits. As our audits uncovered, reductions in these functions led to invisible problems. Cuts to direct services, however, lead to visible problems such as service delivery delays and shorter service hours. This puts pressure on Council to save direct services by cutting the much needed oversight and administration functions through across-the-board budget cuts. We expressed our concern that this strategy leads to reductions in the positions that help protect against fraud and help ensure service delivery by monitoring the work of those that provide direct services. We discussed these invisible threats in our [2013 budget report](#). Several Councilmembers mentioned at a [City budget work session](#) that across-the-board budget cutting is not considered a best practice, though it is very common.⁴ Unfortunately, these types of budget cuts continue. Over the last five years, the City Manager has requested annual across-the-board budget cuts ranging from two to five percent of the General Fund. We believe a better approach is for the City to decide what services it can afford to offer and what assets it can afford to maintain, and build administrative and oversight functions around those programmatic goals.

Although a 2 percent reduction may not seem significant, reductions have been cumulative, year after year

In our [2012 annual report](#) and related [discussion](#), we suggested three questions for Council to ask and the City Manager to answer about risks that could result from proposed budget cuts:

1. Are we increasing the risk of fraud by making this budget cut?
2. Will this budget cut hamper our ability to provide the best and most timely information we need for decision-making?
3. Does this budget cut impact our ability to provide oversight of grants, community agencies, vendors, and staff performance?

Council considered our suggestion and requested that the City Manager disclose in future budget proposals whether planned budget cuts will expose the City to these risks.

Since budget problems are by no means unique to Berkeley, we asked [Cal's Goldman School of Public Policy](#) for a report on alternative budgeting practices that Berkeley might consider. The report represents the hard work, vision, and recommendations of four talented Goldman students who expressed their own conclusions about budgeting practices. Their recommendations included:

1. Establishing a Strategic Vision for Berkeley
2. Reorganizing Government Functions Around Programs
3. Developing Performance Measures for Each City Program
4. Allocating Funding to Programs According to Performance and Priorities

⁴ http://www.cityofberkeley.info/Clerk/City_Council/2013/01Jan/Documents/2013-01-22_Worksession_Item_01_Budget_Forecast.aspx

A pilot project is underway that can help the City determine whether priority-based budgeting approach can be successful. The Council requested that the [Public Health Division](#) use the approach to ensure it effectively addresses public-health needs. The Public Health Division and Department of Health, Housing, and Community Services embraced the concept and developed a comprehensive initiative – “Health Happens in Berkeley” – to focus their work, maximize their impact, and improve their accountability for health outcomes.

Follow-Up on Outstanding Audit Recommendations

Our audit recommendations help improve operations, save money, and promote transparency and accountability. We collaborate with department staff during our audits to ensure our recommendations are practical and feasible.

This helps ensure a higher implementation rate and helps achieve the ultimate goal of improved performance. We emphasize the importance of making timely implementation of our recommendations a high priority. The City Manager continued to support our efforts to implement change by making it a priority to implement the 77 recommendations we reported as open in our 2012 annual report. The City Manager [reported](#) to Council the result of City staff's efforts in making that happen. By June 2014, City staff implemented 50 (65 percent) of the open recommendations and closed eight audits. City staff also closed our [Shelter Plus Care](#) audit, with six new recommendations, in less than a year. That's a total of 56 recommendations implemented over the past two years.

65% of recommendations open as of June 30, 2012, have been implemented, which significantly reduces risk.

Many of the older recommendations that remain open are aimed at reducing the risk of fraud and improving oversight functions. Unfortunately, departments have not implemented all of these recommendations. One dates as far back as 1998. When we last [presented](#) information on open recommendations, Council requested more detail about why they remain open and the extent to which there is a fraud risk. The City Manager provided this information in summary report in [June 2014](#). We also recap the information in Appendix A, which identifies open items with continued fraud risk; and Appendix B, which describes the key issues preventing implementation and what is being done to close open items.

Audit recommendations that remain unimplemented pose continued risks to the City. These risks include theft, inaccurate data use in decision making, inappropriate financial system access, and lost opportunities for cost savings, revenue increases, and service delivery improvements. By the end of fiscal year 2014, there were 65 recommendations outstanding.

Transparency and Risk Reduction

Berkeley's Charter gives the City Auditor a role in reducing the risk of management overriding procedures established to prevent fraud. We do this through oversight of payroll and other payments:

Payroll Audit

Payroll Audit is responsible for reviewing the City's payroll for accuracy and for compliance with federal and state laws, union agreements, and personnel rules and regulations. Payroll Audit also makes suggestions to City departments for improving the efficiency and integrity of the City's payroll system. Key accomplishments in fiscal years 2013 and 2014 include:

- Complying with *California's Public Employees' Pension Reform Act of 2013*. The Act instituted major changes in how employers fund employee retirement benefits and includes new reporting requirements.
- Complying with the *Patient Protection and Affordable Care Act*. The new federal health law requires Payroll Audit to review benefited employees' qualifying documentation concerning healthcare coverage, and to track hours worked by non-benefitted employees.
- Recommending 17 changes for the City Manager to present in the upcoming Berkeley Police Association labor negotiations. Our recommendations would reduce costs, clarify ambiguous language in the current union agreement, and improve City compliance with evolving federal and state laws.
- Improving the online Workers' Compensation Management System and issuing improved guidance for staff that outlines the complex rules and regulations governing City workers' compensation claims.

Contracts

The City Charter requires the City Auditor to countersign and register all contracts. As part of our office's ongoing commitment to making our operations more efficient, we reviewed our practices and worked closely with the Department of Finance to identify work that already was or should be completed by the department's Contract Administrator. This helped remove redundancies and streamline our contract registration process.

The most recent revision to the federal auditing standards we follow requires us to ensure our independence from management in both mind and appearance. We carefully assessed our contract registration practices to ensure independence.

The City Clerk posts contracts to [Records Online](http://www.ci.berkeley.ca.us/recordsonline/search.aspx).⁵

⁵ <http://www.ci.berkeley.ca.us/recordsonline/search.aspx>

About Us

We have extensive knowledge of auditing methods and techniques. We attend continuing professional education courses to maintain and improve our knowledge and skills and to learn about topics that affect city government, as required by generally accepted government auditing standards. Collectively, our performance auditors have more than 95 years of professional audit experience and our payroll auditors have more than 165 years of payroll experience. Many of us hold professional certifications, including:

- Certified Internal Auditor (CIA)
- Certified Government Audit Professional (CGAP)
- Certified Payroll Professional (CPP)
- Certified Public Accountant (CPA)
- Certified Fraud Examiner (CFE)

Performance Auditors:

Ann-Marie Hogan, CIA, CGAP
- City Auditor

Harriet Richardson, CPA, CIA, CGAP
- Audit Manager until April 2014

Claudette Biemeret, CGAP
- Audit Manager

Frank Marietti, CFE, CIA, CGAP
- Senior Auditor

Lincoln Bogard, CPA, CFE
- Auditor II

Myrna Ortiz
- Auditor I

Sherren Styles
- Administrative Assistant

Payroll Auditors:

Dr. Brian Zandipour, CPP
- Deputy City Auditor, Payroll

Leo Reyes
Ann del Rosario
- Auditor II

Agnes Celis
Candice Schott
- Accounting Technicians

Raul Chan
Gail Wread
- Accounting Office Specialist III

Conclusion

The Auditor's Office is a good investment because the City saves money and increases performance when the City Manager and department directors act on our recommendations. Management took significant actions to clear open recommendations this year, but there is more work to be done. The value of our work is in the long-term changes that occur when management implements our recommendations. We will continue to provide a roadmap for continuous improvement of City services.

Appendix A: Summary of Open⁶ Recommendations as of June 30, 2014

Report Title	Risk Category	Open Recommendations		
		Fiscal Year	Total Open	Next Date to Council
Risk Categories: E = Efficiency; F = Fraud; G = Grants; O = Oversight				
Special Report to Council				
Invisible Problems: Weak Internal Controls Require Disclosure by City Manager and Possible Future Council Action on Budget and Workplans	E, F, G, O	2008	1	N/A
Audit Reports				
Public Works Grants Audit	G	1998	1	12/16/2014
Cash Receipts / Cash Handling Audit - Treasury	F, O	2003	1	01/20/2015
Customer Service Cash Receipts / Cash Handling Audit	F, O	2003	3	01/20/2015
Purchase Order Audit - Select Public Works Divisions at the Corporation Yard	E, F	2005	1	09/30/2014
Leases Audit: Conflicting Directives Hinder Contract Oversight	E, O	2009	7	12/16/2014
Public Works Contract Monitoring: Risk of Overpayments / Lack of Inventory Controls	E, F	2010	1	09/30/2014
Audit: City Fuel Operations Need Improvement	F, O	2011	1	09/30/2014
Equipment Replacement Fund - Sustainability and Transparency	E	2011	3	09/30/2014
Payment Card Acceptance Audit: Is Cardholder Information Safe?	F, O	2011	2	12/16/2014
Business License Taxes: Providing Better Guidance and Customer Service Will Increase Revenues	E, O	2012	10	12/16/2014
Construction Permits: Monitor Performance and Fee Assessments to Ensure Excellent and Equitable Customer Service	E, F, O	2014	19	09/16/2014
\$52,000 Theft: More Can Be Expected Without Citywide Changes in Culture and Procedures	F, O	2014	15	10/07/2014
TOTAL			65	

⁶ Open recommendations include those that are in progress and those that the auditee has not yet started to implement. It excludes recommendations that the auditee will not or cannot implement.

Appendix B: Information on Open Recommendations

Special Reports to Council	
Invisible Problems: Weak Internal Controls Require Disclosure by City Manager and Possible Future Council Action on Budget and Workplans City Auditor's Annual Report Discussion City Auditor's Annual Report for Fiscal Year 2012	Identify and quantify the risks of internal control weaknesses not addressed because of insufficient resources; disclose internal control risks of recommended budget cuts in budget reports.

Audit Reports	
Report Title	City Manager's June 2014 Progress Summary
Public Works Grants Audit	Guidance needed for grants; Administrative Regulation is drafted and under review.
Cash Receipts / Cash Handling Audit - Treasury Customer Service Cash Receipts / Cash Handling Audit	Finance must develop policies and procedures to effectively limit City employee and HTE staff FUND\$ access and must write off uncollectable accounts receivable to prevent fraud; in progress.
Leases Audit: Conflicting Directives Hinder Contract Oversight	Vacancy in a key position has delayed Implementation. Clear, documented assignment of responsibilities and coordination with other departments are needed.
Purchase Order Audit - Select Public Works Divisions at the Corporation Yard Public Works Contract Monitoring: Risk of Overpayments / Lack of Inventory Controls, Audit: City Fuel Operations Need Improvement	All recommendations will be closed upon finalization of a contract for services for reconciliations of parts and tires to inventories. Lack of reconciliation and inventory controls poses a fraud risk.
Equipment Replacement Fund - Sustainability and Transparency	Public Works expects to close this audit in FY 2015 when it addresses accounting issues such as: equipment replacement backlog, equipment replacement reserve, loans to other funds, and monthly replacement fees.

Audit Reports	
Report Title	City Manager's June 2014 Progress Summary
Payment Card Acceptance Audit: Is Cardholder Information Safe?	To reduce fraud risk, finalization of the draft A.R. will define the responsibilities, obligations, and requirements for accepting payment cards in City departments.
Business License Taxes: Providing Better Guidance and Customer Service Will Increase Revenues	To close this audit, reduce fraud risk, and increase revenues, Finance must create new procedures, consolidate BLT activities into a single unit, address accounting issues, pursue collection of delinquent accounts and develop reports and performance measures to monitor collection activity, train staff on high risk accounts, amend A.R. on writing-off uncollectable balances, and protect sensitive cardholder information in accordance with industry standards.
Construction Permits: Monitor Performance and Fee Assessments to Ensure Excellent and Equitable Customer Service	Recommendations to improve service and efficiency, increase revenues and reduce fraud risk are outstanding. First report to Council scheduled for September 16, 2014.
\$52,000 Theft: More Can Be Expected Without Citywide Changes in Culture and Procedures	Two recommendations implemented during the audit. All other recommendations outstanding. First report back to Council scheduled for October 7, 2014.