

Office of the
City Manager

August 17, 2015

To: Honorable Mayor and Councilmembers

From: John A. Russo, City Manager

CC: Assistant City Managers
Department Heads
Internal Audit Division

**SUBJECT: PROFESSIONAL SERVICES AGREEMENTS PERFORMANCE
AUDIT DATED JUNE 22, 2015 (AU15-05) AND RESPONSE**

At the request of Interim City Manager Lee McDougal, the Internal Audit Manager conducted a Performance Audit of Professional Services Agreements. The final audit, dated June 22, 2015, is attached for your information.

Also attached is a response memo which researched each of the concerns identified in the audit including documenting how they occurred and how they were corrected. Significantly, at the same time that Internal Audit was conducting this audit, the Finance Department was updating the Administrative Policy regarding Requests for Payments (Policy 7.006.00) to strengthen internal controls. The new Policy strictly limits the types of expenses eligible for payment through this process and requires all other payments to follow the Purchase Order Process. Training has been provided on the updated policy.

In addition to providing you with this Performance Audit and response, we will be posting our Internal Audits to the City's web site thereby demonstrating our commitment to transparency, accountability and financial prudence. Please let me know if you have any questions.

PERFORMANCE
AUDIT

Professional Services
Agreements

Citywide Review

AU15-05

June 22, 2015

Office of the City Manager
Internal Audit Division
Cheryl Johannes, Internal Audit Manager

OBJECTIVE, SCOPE and METHODOLOGY

At the request of the Interim City Manager, Lee McDougal, during the month of May 2015 we conducted an audit of Citywide Professional Services Agreements (PSAs). The objective of the audit was to assess:

- Utilization of PSAs by departments to procure specialized services;
- Adequacy of internal controls; and
- Department compliance with the City Charter/Municipal Code and City administrative policies and procedures.

The review focused on Professional Services Agreements and related “professional service”¹ expenditures for the current fiscal year to date (July 1, 2014 through April 30, 2015). To meet our objectives, we queried and extracted data and records from various internal sources/databases; reviewed current administrative procurement and accounting practices and processes for compliance to City administrative policies/procedures and specifically related sections in the City Charter².

BACKGROUND

The City utilizes various types of agreements (contracts) to procure services for construction, engineering, maintenance, temporary personnel, software design, artistic design, of a consulting and/or advisory nature, conducting conferences, etc.

One type of service agreement utilized by City departments is the Professional Services Agreement (also referred to as the Professional Consultant Services Agreement or PSA). As with all agreements or contracts, PSAs are to be:

- Reviewed and approved to form by the City Attorney’s Office (CAO), even if the agreement does not require Council approval (Section 702 (d) of the City Charter);
- Signed by the City Clerk (Section 419 of the City Charter); and
- Filed with the City Clerk (Section 703 of the City Charter); uploaded on City’s document management portal.

The Municipal Code³ gives the purchasing manager the responsibility for the procurement for all of supplies, materials, equipment and contractual services needed by any and all departments, boards, etc. supported by City funds. Departments are responsible for following City purchasing and contracting polices/procedures as outlined in Chapter 7 of the Administrative Manual when soliciting, evaluating and awarding/selecting professional service providers.

In addition, each department is responsible for ensuring that it receives the deliverables and that the service provider performs services per the contract/agreement. The department is responsible for reviewing invoices for accuracy and ensuring timely payment.

¹ Transactions for “professional services” are recorded in GL Object 421000 in the City’s financial system, IFAS.

² City Charter Sections 419, 702 (d) and 703

³ Chapter 3.16 – Centralized Purchasing System

As of April 30, 2015 (FY2014/15) according to the City's financial system, IFAS, \$10.4 million has been expensed and \$2.6 million has been encumbered this fiscal year in the General Fund for Professional Services (GL Object 421000). Refer to the chart below for FY2014/15 year-to-date professional services budget (appropriation) and expenditures for major funds.

MAJOR FUND	Appropriation	Encumbered	Expenditures
101 - GF	\$14.8 million	\$2.6 million	\$10.4 million
510 - Electric	\$7.9 million	\$0.9 million	\$2.0 million
520 - Water	\$3.8 million	\$1.0 million	\$1.4 million
550 - Sewer	\$1.1 million	\$0.5 million	\$0.7 million

In order to identify PSAs, we reviewed all activity in the City's financial system, IFAS, recorded to GL Object 421000 – Professional Services, for the current fiscal year (July 1, 2014 through April 30, 2015). During our analysis we noted that one department was incorrectly using this GL Object for purchases made via their assigned Procurement card (P-card). The department was notified and a year-to-date journal entry correction was recorded in IFAS; the P-card default GL account was corrected.

Based on the transactions recorded in IFAS, we identified 89 vendors that were potentially “professional service” providers. After reviewing this list with the City Clerk files, we narrowed the list to 52 vendors. We reviewed transactions for each of the 52 vendors in order to meet our objectives.

During the course of our review we identified activities with 12 of the 52⁴ vendors selected that:

- Put the City at risk of exceeding financial terms of contracts;
- In the absence of open competition, departments became reliant on select service providers/consultants; and/or
- Misclassified expenditures which skew the line item budgets.

Of the 12 vendors, two had an executed PSA on file; however, invoices/expenditures processed via a *Request for Payment (RfP)* form exceeded the financial terms of the agreement/contract by \$2.5k and \$7k respectively. The following chart summarizes our findings for the remaining 10 vendors with invoices recorded as “professional services⁵.”

No Current PSA on File & \$s	Incorrectly Expensed as Professional Service & \$s
Outsourced educational assistant \$5.9k	Annual subscription print material renewals \$1.5k
Consultant for strategic planning workshop \$22.3k	Monthly non-reserved parking spaces \$1k
Outside consulting/investigation services \$6.2k	Annual subscription fee for licenses \$6.9k
Quarterly investment advisory services \$132.1k	Annual renewal fee for online system maint. \$10.2k
Monthly fee for budget system/application \$1.6k	
Outsourced technical engineer \$154.4k	

⁴ The remaining 40 vendors had purchase orders on file and referenced on the invoices.

⁵ Vendor invoices were attached to an *RfP* form by the originating department; approved and processed by Finance/Accounts Payable.

SUMMARY of FINDINGS

We found through review and discussions with staff in departments/divisions that there is a lack of understanding of the term “professional services” as used by the City; how/when the related expenditure account (GL Object 421000) is to be utilized; and/or lack of awareness of City Administrative Policy [02.005.00](#) - *Contracting for Professional Services* which clearly outlines the procedures for procuring professional services when expenditures/fees for said services do not exceed \$50,000.

The policy also includes the definition of Professional Services:

“Professional Services include architectural, engineering, planning, financial and other consulting services such as advisory, information technology, surveying, research and/or development services, which involve the exercise of professional discretion and independent judgment based on advanced or specialized knowledge, expertise or training gained by formal studies or experience.”

As noted in our analysis of Professional Services financial transactions, departments/divisions have at times misapplied the *RfP* form to pay vendor invoices. City Administrative Policy [07.006.00](#)⁶ – *Request for Payment (RfP)* establishes the procedures for utilization of the form for payment of invoices; clearly defines the types of services/expenditures where the use of an *RfP* is applicable.

RECOMMENDATIONS

To strengthen internal controls, minimize risk and provide improved professional service contract management, we recommend the following process changes which will need to be communicated, enforced and monitored Citywide by Finance/Purchasing/Accounting:

Departments should be required to follow Administrative Policy 02.005.00 when procuring professional consulting/contractual services. This will ensure executed PSAs are recorded in the Purchasing system and assigned a purchase order for tracking payments against the PSA; financial terms of the PSA will be encumbered. Invoices processed for payment should not exceed the financial terms of the PSA/agreement.

Use of the Request for Payment form should be limited and monitored by Finance/Accounting. Departments should be advised when they are not in compliance with Administrative Policy 07.006.00.

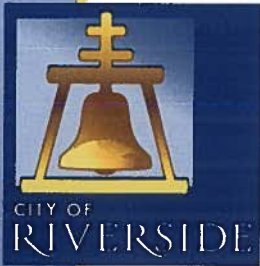
We thank the City Clerk and the Finance Department for their assistance and input during this review.

-Cheryl Johannes, Internal Audit Manager

⁶ This policy was revised effective June 2015, prior to the finalization of the audit report. All department heads were notified of the change; Finance is leading the training on the revised/new policy.

AUDITING STANDARDS


Our review was conducted in accordance with the *Standards for the Professional Practice of Internal Auditing* of the Institute of Internal Auditors. Those standards require that the audit is planned and performed to afford a reasonable basis for judgments and conclusions regarding the department, Division, program, activity or function under review. An audit also includes assessments of applicable internal controls and compliance with requirements of laws and regulations when necessary to satisfy the audit objectives. We believe our audit provides a reasonable basis for our conclusions.



Office of the
City Manager

July 23, 2015

To: John Russo, City Manager

From: Deanna Lorson, Assistant City Manager 

CC: Al Zelinka, Assistant City Manager
Alex Nguyen, Assistant City Manager
Cheryl Johannes, Internal Audit Manager

**SUBJECT: PROFESSIONAL SERVICES AGREEMENTS PERFORMANCE
AUDIT DATED JUNE 22, 2015 (AU15-05)**

The Internal Auditor's recent Performance Audit of Professional Services Agreements (PSAs) identified concerns with 12 of the 52 vendor agreements that were reviewed pursuant to this audit. Following is a description of each of these concerns, how they occurred, and corrective actions.

It should be noted that several of the issues were caused by the use of Request for Payment (RFP) forms to process payment instead of setting up a Purchase Order noting the contract limitations. In order to correct this problem, Finance has updated the Administrative Policy regarding RFPs (Policy 7.006.00) to strictly limit the types of expenses eligible for payment through this process, and requiring all other payments to follow the Purchase Order (PO) process. Finance has conducted training with all departmental staff on the proper use of RFPs and POs and will be strictly enforcing the policy. This corrective action will strengthen our internal controls to prevent misuse, and reduce the opportunity for abuse, in the future.

Payment Exceeded Financial Limits in Contract. Two contracts exceeded the financial limits contained in the respective agreements, one each in the City Manager's Office (\$2,500) and the Community & Economic Development Department (\$7,000).

- In the case of the City Manager's Office contract, an amendment was prepared and processed concurrently with the payment request. However, the vendor signatures on the amendment were rejected by the City Attorney's Office; staff is in the process of obtaining the correct signatures. In the future, procedures will be followed requiring that the amendment be fully executed and effective prior to processing payment.

- In the case of the Community & Economic Development (CED) contract, the agreement was not-to-exceed \$40,000 and they had been paid \$47,047.50 as of the audit. On June 9, 2015 the City Council approved an increase to \$100,000 per year through expiration of the contract on June 30, 2017. In the future, payments that exceed the contract amount will not be processed until an amendment is properly executed and the PO adjusted accordingly.

No Current Agreement on File. The audit indicated that six contracts did not have current agreements on file, as follows:

- Consultant for strategic planning workshop (\$22,500) – City Manager's Office. The City Council authorized hiring of this consultant and directed the City Manager to prepare the contract in October, 2014, however with the retirement both the City Manager and Assistant City Manager it appears that the contract was not prepared. The Interim City Manager approved payment of the invoice using a RRP. As noted above, the RFP policy has been recently updated and this type of payment will no longer be permitted using a RFP. This will ensure that a contract is in place prior to payment.
- Outside consulting/investigatory services (\$6,200) – Community Police Review Commission. The internal audit report erroneously includes this item in the listing of items for which there is no PSA. A PSA was executed in May, 2011 and has been renewed annually. A copy of the latest renewal has been provided to the auditor.
- Outsourced technical engineer (\$154,400) – Community & Economic Development Department (CED). Due to a retirement and resignation, CED had an immediate need in April 2014 for a required Structural Engineer. An existing contract with Adecco was used to temporarily fill this position; it was later discovered that the Adecco contract had expired. CED is creating a panel of qualified consultants for supplemental staffing; it is anticipated that this will go to City Council in August for approval. Additionally, Human Resources is updating all of their contracts for temporary supplemental staffing. Under the updated RFP policy, payments such as this will need to be made pursuant to a PO which will ensure that a valid contract is in place before expenditures are authorized.
- Quarterly investment advisory services (\$132,100) – Finance Department. The contract expired sometime after the transition from the former ACM/CFO to the current Finance Director and the same quarterly services arrangement continued in place without realizing the contract expired and needed to be renewed. The Finance Director is bidding these services and will be preparing a new contract with the selected consultant for approval in accordance with our Purchasing Policy. The new PO requirements will keep this from reoccurring.
- Monthly fee for budget system/application (\$1,600) – Finance Department. The internal audit report erroneously includes this item in the listing of items for which there is no PSA. One has been provided to the auditor, which was created when the original agreement was negotiated with the software and remains current.

- Outsourced educational assistant (\$5,900) – Museum & Cultural Affairs Department. In reviewing this matter, it was determined that this worker was incorrectly charged to professional services and should have been hired as a seasonal employee. This has been corrected. Department staff has been trained in the RFP and PO processes in order to ensure that charges are correctly classified in the future.

Incorrectly Expensed as a Professional Service. The Audit indicates that four vendor payments were incorrectly classified as Professional Services as follows:

- Annual subscription for print material renewals (\$1,500 - Library).
- Monthly non-reserved parking spaces (\$1,000 - IT).
- Annual subscription fee for licenses (\$6,900 - Finance).
- Annual renewal fee for online system maintenance (\$10,200 – Finance).

Further research has revealed that the Professional Services account is also used for various expenses to support departmental operations and there is no specific policy relative to the utilization of the Professional Services Account that would restrict its use to only PSA expenses. The expenses noted in the audit fall within the broader category of professional services which can be charged to this account at the discretion of the respective departments. Thus, no corrections or changes are recommended.

In closing, the PSA Audit revealed some lax practices that allowed payments to be made without valid Professional Services Agreements in place. Further research and corrective actions have resulted in the following:

- Two projects had valid contracts in place and were incorrectly listed in the audit;
- Two contracts have been amended to increase the terms thus bringing payments into compliance with the contract;
- Two projects are being competitively bid which will result in a new contracts;
- One project was erroneously paid via an RFP without a contract in place; since the project was authorized the City Council and is complete no further action is necessary; and
- One project has been reclassified to eliminate the need for a contract.

Additionally, the updated RFP Policy will prevent most of these errors in the future. The Finance Department has trained departmental staff on the updated policy to ensure awareness, and has directed staff to not grant exceptions. These increased controls will prevent the lax practices that were found by the audit. Additionally, the updated policy and the audit have been discussed with the Executive Leadership Team and in more detail with the respective departments identified in the audit thus reinforcing the need to ensure a culture of strong controls.