

APPROVED MINUTES APPROVED ON 01/27/2020



**CITY OF SCOTTSDALE
AUDIT COMMITTEE
REGULAR MEETING**

Tuesday, November 12, 2019

**City Attorney's Conference Room
3939 North Drinkwater Blvd
Scottsdale, AZ 85251**

PRESENT: Kathy Littlefield, Chair
Virginia Korte, Councilmember
Solange Whitehead, Councilwoman

STAFF: Sharron Walker, City Auditor
Paul Christiansen, Senior Auditor
Brad Hubert, Senior Auditor
Lai Cluff, Senior Auditor
Shelby Trimaloff, Exec. Asst. to City Auditor
Robert Schoepe, Purchasing Department
Jeff Nichols, City Treasurer

GUESTS: Jill Shaw, Heinfeld Meech

CALL TO ORDER

The meeting was called to order at 3:00 p.m. A formal roll call confirmed the presence of all Committee Members as noted above.

PUBLIC COMMENT

There were no members of the public who wished to speak.

REGULAR AGENDA

1. Approval of Minutes, Regular Meeting, September 16, 2019

Chair Littlefield called for comments/changes to the minutes.

COUNCILMEMBER KORTE MOVED TO APPROVE THE MINUTES OF THE SEPTEMBER 16, 2019 REGULAR MEETING AS PRESENTED. COUNCILWOMAN WHITEHEAD SECONDED THE MOTION, WHICH CARRIED 3-0 WITH CHAIR LITTLEFIELD, COUNCILMEMBER KORTE, AND COUNCILWOMAN WHITEHEAD VOTING IN THE AFFIRMATIVE.

2. Discussion and Possible Direction to Staff Regarding Transportation Commission Sunset Review

Brad Hubert, Senior Auditor, stated that the Commission's purpose is to advise City Council on the matters relating to the safe and efficient use of all transportation modes, the transportation network, as well as the City's capital improvement program and operating budget for Transportation. He noted that the Commission's 2018 annual report and two prior annual reports were provided. The Audit Committee is to evaluate whether the reviewed board or commission is serving its intended purpose, whether the purpose should be maintained or modified, and whether the purpose has been served or is no longer required. Specifically, the Audit Committee is to recommend to City Council whether to continue or terminate the board or commission.

COUNCILWOMAN WHITEHEAD MOVED TO RECOMMEND TO CITY COUNCIL TO CONTINUE THE TRANSPORTATION COMMISSION. COUNCILMEMBER KORTE SECONDED THE MOTION, WHICH CARRIED 3-0 WITH CHAIR LITTLEFIELD, COUNCILMEMBER KORTE, AND COUNCILWOMAN WHITEHEAD VOTING IN THE AFFIRMATIVE.

3. Discussion Possible Direction to Staff Regarding Transportation Commission Paths & Trails Subcommittee Sunset Review

Mr. Hubert stated that the Subcommittee advises the Transportation Commission and provides a public forum for issues regarding paths and trails in Scottsdale (not including those in the Preserve). The requested action is the same, to recommend to the City Council whether to continue or terminate the reviewed subcommittee.

COUNCILWOMAN WHITEHEAD MOVED TO RECOMMEND TO CITY COUNCIL TO CONTINUE THE PATHS & TRAILS SUBCOMMITTEE.

Councilmember Korte questioned how often the Subcommittee meets and what its purpose is or what it accomplishes. Sharron Walker, City Auditor, stated that a staff representative was expected to attend today's meeting, but is not present. The Audit Committee may want to postpone this item until the next meeting, and she will ensure the department knows to have someone present in January to address the Audit Committee's questions. Councilwoman Whitehead stated that the City is expanding a lot of paths outside of the Preserve, and the Subcommittee has been providing guidance over the

years. She agreed it would be a good idea to have a staff person present for the discussion.

CHAIR LITTLEFIELD MOVED TO CONTINUE THIS REVIEW TO THE JANUARY MEETING, SO THAT A REPRESENTATIVE CAN ATTEND THE MEETING TO ADDRESS THE COMMITTEE'S QUESTIONS. COUNCILWOMAN WHITEHEAD SECONDED THE ALTERNATE MOTION, WHICH CARRIED 3-0 WITH CHAIR LITTLEFIELD, COUNCILMEMBER KORTE, AND COUNCILWOMAN WHITEHEAD VOTING IN THE AFFIRMATIVE.

4. Discussion and Possible Direction to Staff Regarding Adding New Veterans Advisory Commission to the Audit Committee's Sunset Review Schedule

Ms. Walker commented that because the Sunset Review schedule is Audit Committee-approved, she wanted to provide an update on getting the new Veterans Advisory Commission added to the Sunset Review Schedule. The Commission was approved on July 1st, and the first members were appointed on October 15th, so October 2022 would be a 3-year period. The current sunset review schedule goes through 2021, so this would not be added until the next schedule. Taking into account that it will take a few months to get up and running, such as adopting bylaws, she suggested the Commission's first sunset review should be in January 2023. Councilmember Korte suggested perhaps giving an additional 6 months. Ms. Walker indicated when she brings the next sunset review schedule to the Committee, she can put the Commission around March or April 2023. Chair Littlefield agreed with the longer time frame and recommended letting the Commission know that it will be placed on the schedule and what the purpose and process is. Ms. Walker confirmed that Audit staff will be in touch with the staff representative assigned to work with the Commission.

5. Discussion and Possible Direction to Staff Regarding Audit No. 2001, FY 2018/19 External Financial Audit

Jill Shaw, Heinfeld Meech, stated that the audit began in June with preliminary work. The majority of time onsite took place during the last two weeks of September. The process was smooth and wrapped up earlier than years prior. The audit went very well. As a result of the audit, several reports are issued. The largest is the Comprehensive Annual Financial Report (CAFR), which includes the audited financial statements of the City as a whole. The accounting department prepares the report. Heinfeld Meech provides the independent auditor's report, which provides an opinion on the financial statements. They issued an unmodified (clean opinion), which means that they identified no material misstatements in the financial statements. There are separate annual financial reports for each of the component units.

Another part of the audit is the single audit. This is required because the City spends more than \$750,000 in federal awards. Auditors are required to rotate which federal programs they look at each year and select programs based on a risk assessment. This year, they looked at the CDBG and Airport Improvement programs in detail. The audit includes reviewing what monies are spent on, whether they are spent according to the grant agreements, and any compliance requirements that the federal OMB is requiring the auditors review. There were no federal compliance findings, and there were no reported

significant deficiencies or material weaknesses in internal controls over financial reporting or federal compliance.

Auditors are required to report on the progress of prior findings noted. All three findings noted in the previous year's single audit reporting package were determined to have been corrected. The auditing standards require issuance of a communication to governance that provides an overall summary of the audit. Had there been significant issues, they would have been noted in this communication. The communication to governance also addresses whether new accounting policies were implemented. There were a few identified; however, they were not significant to the audit report.

At the end of the audit, management signs a representation letter, which states that they have provided the auditors with all materials and information requested. The letter discusses any audit adjustments that were recommended and are significant or that were passed on. One adjustment was recommended this year but passed on because it was immaterial, and management will look at this in future years and get more information to ensure the adjustment is made. At this point of the audit process, there are always a couple open items. The expenditure limitation report is due by March 31st. This report demonstrates that the City has remained within the statutorily allowable spending levels. The auditor will provide an opinion on this, but the audit has to be completed first, so it's done a bit later. And a HUD electronic filing occurs in the January/February time frame as well.

Audit Committee members commented on the quality of the report.

COUNCILMEMBER KORTE MOVED TO RECOMMEND TO THE CITY COUNCIL ACCEPTANCE OF AUDIT NO. 2001. COUNCILWOMAN WHITEHEAD SECONDED THE MOTION, WHICH CARRIED 3-0 WITH CHAIR LITTLEFIELD, COUNCILMEMBER KORTE, AND COUNCILWOMAN WHITEHEAD VOTING IN THE AFFIRMATIVE.

6. Discussion and Possible Direction to Staff Regarding Audit No. 2010, Warehouse Operations

Lai Cluff, Senior Auditor, stated that the audit was conducted to evaluate management controls over and cost-effectiveness of City warehouse operations. The Purchasing Department operates a warehouse function that receives, delivers and stores items for City departments. It operates as a supply store to provide commonly used maintenance and repair supplies to departments. It manages surplus City property by selling it through public auction online or disposing of items that cannot be sold. The audit found that more appropriate controls are needed to manage the store's operation. For example, supplies issuances are not being entered as they occur and receipts are not being provided to the departmental staff. Inventory counts were not properly conducted and documented. Specifically, annual counts were not performed blind and documentation for periodic counts were not retained. Variances were adjusted by "issuing" more supplies or removing stock from shelves, rather than recording an inventory adjustment. Thus, available information on inventory shrinkages or overages was inaccurate.

Surplus property controls could also be improved. The disposition of some items could not be verified. Inconsistencies in the count and descriptions of surplus items received versus those listed should be verified with the department providing the items. Fleet vehicle transfers to the warehouse also need to be recorded when the vehicles are received.

Several surplus auction policies were not consistently followed, including issuing open vehicle titles for auctioned vehicles and not getting tax exemption certificates before waiving transaction privilege taxes. Over two fiscal years, about \$40,000 in taxes were waived without verification.

In addition, the department occasionally issued auction refunds without direct documentation of the buyer's request and management's approval of an exception from the no refunds policy. The department also delegated some surplus property disposals to other departments, although City code currently does not allow this. The audit also recommended some procedural improvements, such as expanding the pick-up time frame for auction sales, using reserve amounts when appropriate and providing more detailed product information for auctioned items. Additionally, the availability of surplus property has not been effectively communicated to City departments. City code prioritizes internal transfers of surplus property between departments over other disposition methods. These transfers could result in departmental cost savings. As well, record keeping and accountability for departmental property stored at the warehouse needs to be clarified, and shipping responsibilities may be more effectively managed by departmental staff.

In response to a question from Councilmember Korte regarding the time frame for the last audit, Ms. Walker stated that audit staff did a special investigation in 2015/2016 in response to information received through the integrity line.

Councilmember Korte asked Mr. Schoepe, Purchasing Department, how long he has been overseeing the operation. Mr. Schoepe stated that he has been overseeing it for a little over a year. Councilmember Korte surmised that he had inherited some issues. Jeff Nichols, City Treasurer, commented that the audit was requested in response to concerns communicated by Mr. Schoepe. Mr. Schoepe stated that historically, the roles and responsibilities of the warehouse have been divided into thirds: The stores, receiving and delivery, and surplus. Over the years, surplus has grown tremendously. It is time to review the roles and responsibilities of the three areas and to modernize policies and procedures. There is a need to move from paper notes and delayed data entry to a modern system that provide scanners. The modernization has to be balanced with the resources available.

In response to a question from Councilmember Korte, Mr. Schoepe said that the inventory is computerized only in the sense that it is organized on spreadsheets. Ms. Cluff commented that the warehouse is using SmartStream for the Stores. Ms. Walker added that the detail is in SmartStream, however many of their processes are manual so they are using spreadsheets for some things that could be done with more effective use of the system. Mr. Schoepe commented on the limitations of SmartStream for trying to modernize inventories, but also noted that they need to take care of what's on the shelves first and work their way through some of the other solutions as they progress.

Councilwoman Whitehead inquired about delegation and the efficiency of departments having to send items to the warehouse for disposal. Ms. Cluff commented that now City Code states that Purchasing (the warehouse) has the responsibility. Ms. Walker added that disposal of electronic devices is one of the areas, with both Police property and evidence and IT having Apple products that cannot be resold due to issues with the IDs attached to them. The intent of City Code was likely to have a centralized approach or a hub, where one department (Purchasing) figures out how to handle the disposition rather than two departments having to figure out solutions.

In response to a question from Councilmember Korte, Mr. Schoepe stated that they are considering several options, including software to better manage the department. The audit report provided a framework for modernizing and increasing efficiency in the warehouse.

Chair Littlefield expressed concern for the level of inventory not being tracked and categorized. There should be a listing of what items sold at what price, as well as keeping data on what remains in stores and in the warehouse. There are particular concerns in terms of potential sales of weapons, who they are being sold to and for what prices. Ms. Cluff commented that the process for firearm sales was fairly smooth. As they can only be sold to authorized dealers, a solicitation for purchase process is used rather than the auction process. Ms. Walker added that in response to the previous investigation report, they also made changes to how they handle jewelry. While the process is not as clean as it should be, they now have an appraiser review and identify items of higher value and provide a full appraisal. They have found the certificate of appraisal for those items results in getting better prices than what they used to get. Mr. Schoepe commented that the audit provides a framework, for them to improve and arrive at systemic solutions. Chair Littlefield suggested that department staff continue to work with the Audit department as they move forward with modernizing.

COUNCILMEMBER KORTE MOVED TO ACCEPT AUDIT NO. 2010. COUNCILWOMAN WHITEHEAD SECONDED THE MOTION, WHICH CARRIED 3-0 WITH CHAIR LITTLEFIELD, COUNCILMEMBER KORTE, AND COUNCILWOMAN WHITEHEAD VOTING IN THE AFFIRMATIVE.

7. Discussion and Possible Direction to Staff regarding 1st Quarter FY 2019/20 Follow Up on Status of Audit Recommendations

Ms. Walker addressed follow-ups for the first quarter. The first quarter results are significantly improved over the same quarter last year. For the current quarter, approximately 66 percent of recommendations were implemented or partly implemented, and 29 percent in progress. The same quarter last year had 61% completed and 34% in progress. The Fire Department and the Human Resource Department put significant effort into getting their audit recommendations implemented in about one year. On the other end of the spectrum Facilities Management, in response to the Preventative Maintenance & Repair audit three years ago, still has not implemented written policies and procedures for its operations and data quality management. In response to a question from Councilmember Korte, Ms. Walker confirmed that she meets regularly with the City Manager including on these issues.

8. Informational Report Regarding 3rd Quarter Calendar Year 2019 Taxpayer Problem Resolution Officer Report

Ms. Walker invited questions on the informational report. There were no questions.

9. City Auditor Updates, Including Status of FY 2019/20 Audit Plan and Tentative Meeting Dates for Calendar Year 2020

Ms. Walker stated that, as shown in the graphic, the audit plan schedule is essentially on track in comparison to the previous five years.

10. Discussion and Possible Direction to Staff Regarding Potential Agenda Items for Next Audit Meeting

Ms. Walker noted that the next meeting will be on January 27th. Besides the potential agenda items listed in the draft, it will include the Path & Trails Subcommittee sunset review.

Adjournment

With no further business to discuss, the meeting adjourned at 3:44 p.m.

SUBMITTED BY:

eScribers, LLC