

**APPROVED MINUTES
APPROVED ON 11/16/2015**



**CITY OF SCOTTSDALE
AUDIT COMMITTEE**

MONDAY, OCTOBER 19, 2015

**CITY HALL
KIVA CONFERENCE ROOM
3939 NORTH DRINKWATER BOULEVARD
SCOTTSDALE, AZ 85251**

REGULAR MEETING

PRESENT: Suzanne Klapp, Chair
Virginia Korte, Councilmember
Kathy Littlefield, Councilwoman

STAFF: Sharron Walker, City Auditor
Kyla Anderson, City Auditor's Office
Cathleen Davis, City Auditor's Office
Janis Bladine, City Attorney's Office
Henry Garcia, McCormick-Stillman Railroad Park
Steve Geiogamah, Acting Tourism & Events Director
Brett Jackson, Parks & Recreation Department
Nick Molinari, McCormick-Stillman Railroad Park
Carolyn Moyle, McCormick-Stillman Railroad Park
Bill Murphy, Community Services Division
Reed Pryor, Parks & Recreation Department
Brent Stockwell, Assistant City Manager
Margaret Wilson, City Attorney's Office

GUESTS: Lisa Aquilina, Scottsdale Railroad and Mechanical Society
Drew Aquilina
Rachel Cooper, Scottsdale Railroad and Mechanical Society
Marc Miller, Scottsdale Railroad and Mechanical Society
Russ Mosser, Scottsdale Railroad and Mechanical Society

CALL TO ORDER

Chair Klapp called the meeting to order at 4:04 p.m. A formal roll call confirmed the presence of all Committee Members as noted above.

1. Approval of Minutes, Regular Meeting, August 24, 2015

COUNCILWOMAN LITTLEFIELD MOVED TO APPROVE THE MINUTES OF THE AUGUST 24, 2015 REGULAR MEETING. COUNCILMEMBER KORTE SECONDED THE MOTION, WHICH CARRIED BY A UNANIMOUS VOTE OF THREE (3) TO ZERO (0).

2. Discussion and Possible Direction to Staff Regarding Audit No. 1603, Bed Tax Funded Special Event Contract

Senior Auditor Kyla Anderson noted that this audit was conducted to evaluate compliance with the terms of the contracts and the effectiveness of the controls. It did not review the City's special event permitting processes as this is a separate process.

The City invests bed tax dollars in special events to encourage tourism and provide citizens with cultural and sporting activities. Expenditures on special events have increased from \$300,000 in FY 2010/2011 to \$1.5 million in the last fiscal year. The City has four special event funding programs:

- o Community Events
- o Event Venue Fee
- o Matching Event Advertising Funding
- o Event Development

The audit found that the eligibility and evaluation criteria for special event funding could be more effective. Currently, hotel room nights are used as the main criteria for event approval for both the Event Venue and Matching Event Advertising Programs. Therefore an event that may increase tourism to Scottsdale but will not generate the minimum verifiable hotel room nights would not be eligible for funding. Having multiple criteria such as those listed on page 11 of the report would allow events to be evaluated more thoroughly for potential and actual return on investment. The addition of certain clauses into special event contracts, such as an audit clause and requirement for attendance documentation can help protect the City's use of bed tax dollars. An audit clause is important if there is a question about whether requirements were actually met.

Improved contract compliance can help ensure return on the City's investment. For example, reimbursements were made for unallowable expenses such as for event ads that did not include City logos. One event producer of those tested did not submit original detailed invoices, however reimbursement was made anyway. Some post event reports were missing documentation such as confirmation of hotel room nights generated and publication tear sheets to evidence ad placement.

Finally, some events were approved that did not meet current program guidelines. One Event Development event was not required to use City money for marketing expenses as outlined in program guidelines, and two Community Events were funded even though they did not meet location and attendance requirements.

The auditors recommended working with the Tourism Development Commission and bringing updated event requirements to City Council for review and approval. The department agreed with the audit recommendation and expects to have all

recommendations implemented by the end of the current fiscal year. Ms. Anderson noted that Steve Geiogamah of the Tourism & Events Department was present.

3. Discussion and possible direction to staff regarding Audit No. 1607, McCormick Stillman Railroad Park Operations

Senior Auditor Cathleen Davis stated this audit was performed to evaluate controls over and accountability for Park operations. The Parks & Recreation Department operates the McCormick-Stillman Railroad Park. The Scottsdale Railroad and Mechanical Society helps to fund major Park amenities and events.

The audit found that the Park's key third-party agreements were allowed to expire and other aspects of contract administration can be improved. Specifically, the Park's key contract with the Society expired in June 2011 and the model railroad clubs' revocable license agreements were also allowed to expire. The former Park contract administrator served on the Society's board and informal modifications to the Society's agreements occurred. They also found that some City building access seemed excessive.

Improvements could be made in the Park's asset management. Society-donated assets totaling more than \$262,000 during calendar years 2013 and 2014 have not been recorded in the City's capital asset records. Also, creating and maintaining a list of historically significant and high risk items, along with performing periodic physical inventories, could improve oversight and accountability for the Park's assets.

Better rates and fees analysis and implementation, billing, and accounting practices and inventory management can improve the Park's cost recovery results. A comprehensive cost analysis has not recently been conducted for the Park. The train and carousel rides are currently 20-60% lower than similar rides in the area. The Park staff has underestimated carousel staffing costs by more than \$130,000 during the past three fiscal years. These calculations underestimated both the operator and maintenance hours and staffing rates.

Cash handling practices for third-party monies were also not effective. Park staff collected \$95,000 in Society monies during fiscal year 2014/15; these monies were deposited into the City's bank account and certain donations were not collected or counted in dual custody. Almost \$9,800 in direct staffing costs for the Model Railroad Building were not recovered, as associated fringe benefits were not included in the invoices prepared by Park staff. Also, segregation of duties are not in place over the Park's receivables.

Finally, inventory management functions included in the Park's point-of-sale system are not properly implemented, resulting in unreliable inventory records. Park staff did not regularly conduct physical inventories of their food and souvenir items.

The auditors found that certain controls over information technology could be strengthened. Both the Park's point-of-sale system and the website were maintained through third-party support. The auditors found that the IT support and controls were not effective. Additionally, operating procedures have not been documented. While a number of informal documents are located in the Park's shared network, a comprehensive operations manual is not available. Given the unique nature of the

Park's operations, a formal written operating procedure could help staff operate more effectively.

Ms. Davis noted that Bill Murphy, Reed Pryor and Brett Jackson were in attendance, along with other staff from the Community Services Division and members of the Scottsdale Railroad and Mechanical Society.

Councilmember Korte noted it was interesting that the Society had contracted for an ATM to be installed at the Park. Mr. Murphy said that ATMs are also installed at the Stadium during spring training, which are controlled by the Giants. Councilmember Korte commented that there is an agreement in place with the Giants but the agreement with the Society expired. She inquired about the history of that expiration.

Mr. Murphy said Department staff believed the contract with the Society was still in place, adding that the Society has been following the terms and conditions of the contract. Since 2011, there have been three different managers running the Park so it seems that some communications were lost. Staff is committed to quickly re-establishing the agreement. City Auditor Sharron Walker added that the Society went beyond what was in the agreement in offering to reimburse the staffing for the Model Railroad Building so that the Park would not have to charge admission to the building. While they have been following the expired agreement, there are some things happening that should be put in writing so both parties know what is expected.

Councilmember Korte asked whether staff and the Society communicate regarding the therailroadpark.com website. Nick Molinari confirmed that they communicate regularly. He added that staff has secured IT concurrence for the third party website. They believe the site was launched before the City had policies related to third party websites or social media. Councilmember Korte requested that the site link to the City website.

Chair Klapp asked whether it is typical to spend \$252,200 to purchase merchandise, yet only sell \$136,600 worth of merchandise and whether management is monitoring inventory levels. Ms. Davis explained that the inventory purchases amount includes both food and merchandise but food sales are shown separately. Total sales including food is approximately \$436,400. Carolyn Moyle added that physical inventory had been done twice each year until several management changes in the last couple of years. Staff were kept busy helping upper management with Park operations and this was pushed aside. However, Park staff now has a plan in place to take inventory three times a year.

Councilwoman Littlefield commented that she sees a pattern of contract administration weakness in both of the audit reports presented. She wondered whether the area of contract administration in general should be strengthened. It seems as though oftentimes contract administrators change but the incoming staff have not been trained in contract administration. She suggested the Charter Officers review protocols and standard operating procedures on cash handling, recordkeeping, and tracking contracts. The City Clerk could provide input on recordkeeping and the City Attorney on contract obligations. Also, there should be a system that tracks when contracts are due so that the City is not working with expired agreements. Training and regular quarterly or semi-annual reviews to address any questions might help the contract administrators in various departments carry out their duties. With the number of contracts in force, the City should have some standard operating procedures.

Ms. Walker said that Councilwoman Littlefield's suggestions are excellent. Contract administration has been a challenging area for the City. She noted the Purchasing Department has a contract administrator's academy, which includes the City Attorney's office participation and the City Auditor's office has an hour of that. But the academy's content is oriented to purchase contracts, where the City is buying goods or services. The challenge is that agreements such as these do not fit the purchasing mold. The missing link may be contract administrator training for those other types of contracts.

In response to Councilwoman Littlefield's question, Ms. Walker said the auditors have previously made recommendations about having a comprehensive tracking system for City contracts. However, at this point there is not one.

Chair Klapp agreed with Councilwoman Littlefield's comments and that there should be training and oversight on contract administration for those other types of contracts. The level of oversight needs to be raised because this concern surfaces in many audit reports and often staff turnover is the cause.

Ms. Walker noted that having operating policies and procedures would also help address this, and it is really for the benefit of staff in each department. The current Park staff have had to figure out how to run the Park after staff turnover and can understand how useful a policies and procedures manual would be. She pointed out that this is the first time they have audited the Park so it is not unusual to have a number of recommendations. Mr. Murphy and his staff were great to work with. Chair Klapp noted it appears they are in agreement with the steps that need to be taken. This seems to go beyond that to what we are doing to train people.

Mr. Murphy said they acknowledge that their licensing contracts need attention and review. He noted with several one-year agreements and some in the same months, they are working with the attorney on whether the agreements can be written for longer periods of time. The Public Works Division's Real Estate section is now putting these license agreements into their tickler file and that communication will help with tracking contract expiration dates.

Councilwoman Littlefield stressed that her comments are not directed only to this audit in particular, but this is a question of City policy. Chair Klapp commented that the auditor's emphasis on cash handling procedures is also well placed. This is an area that needs constant monitoring.

4. Discussion and Possible Direction to Staff Regarding CY 2015 3rd Quarter Taxpayer Problem Resolution Officer Report

Ms. Davis presented the Taxpayer Problem Resolution Officer report for the period of July through September 2015. Results continue to be consistently positive.

No tax audit surveys were mailed because administration for transaction privilege tax audits have transferred to the Arizona Department of Revenue, which will handle the surveys for those audits. The City Treasurer's Office communicated that a system error caused some surveys not to be generated, but the issue has been resolved. No taxpayer requests for TPRO assistance were received during the quarter.

5 Discussion and Possible Direction to Staff Regarding FY 2015/2016 1st Quarter Follow-Up on Status of Audit Recommendations

Ms. Walker stated that there is a slight improvement in implementation rate over the first quarter of last year. Attachment D is a new attachment summarizing the recommendations that were not implemented. She asked the Committee Members whether they would prefer a shorter Detail report showing just the most current status of each audit rather than the full historical detail. Committee Members preferred the full detail shown as it is now.

Councilmember Korte discussed the “not implemented” status related to the indirect cost allocation model whereby enterprise fund programs had been undercharged. She noted that in the follow-up, it was found that a further \$8 million in facilities management costs were not allocated and remained designated as direct costs. She asked whether there is a next step that can be taken.

Ms. Walker said the City Treasurer has oversight over that area and the decision on whether to implement the recommendation. The auditors have quantified the difference to show that this decision has a significant effect. Her preference is to work with the audited areas toward implementation rather than to ask the Council to step in. The Audit Committee’s follow up reporting program has encouraged paying attention to audit recommendations.

Ms. Walker pointed out that some of the items shown as not implemented are now no longer applicable because of changes in tax law responsibilities. She left these on the report as not implemented because that was the final status before they no longer applied.

In response to a question from Councilwoman Littlefield, Ms. Walker said the contract administrator for the Scottsdale Cultural Council contract opted to not require anything additional from the SCC for the audit recommendations. Chair Klapp suggested that with the change in management at the Cultural Council it may be worthwhile revisiting this question with the contract administrator.

6 Discussion and Possible Direction to Staff Regarding Proposed 2016 Audit Committee Meeting Dates

Ms. Walker reviewed the Audit Committee proposed meetings she had noted on the 2016 City Council meeting calendar.

Although initially she proposed having the June meeting on the fourth Monday, if they meet on June 20th, the day before a City Council meeting, the last week of June would be free. The Committee Members concurred with this change.

In October the meeting could take place on October 24, 2016, which is the day before a City Council meeting, rather than October 17 as currently proposed. The Committee Members agreed with this change.

The other proposed dates were not changed.

7 Discussion and Possible Direction to Staff Regarding FY 2015/16 Audit Plan Status

Ms. Walker said extra time was allowed for the contractor to respond on the construction contract audit, so this report will be presented in November.

The SkySong residential rent audit will likely be presented in January 2016 rather than November due to delays in getting information.

The SCADA audit, which is the Water Resources IT network vulnerability assessment, may be replaced by a different audit as it is possible that Homeland Security will conduct this audit.

A development impact fees audit is required by statute. Staff issued an RFP in August but received no responses. Ms. Walker said she has made some minor adjustments to the RFP to reissue it and asked Purchasing to reaching out to potential firms that downloaded the RFP but did not bid. Feedback through the Purchasing Department indicated one issue is that the expertise needed is a combination of accounting plus engineering. Staff will continue working to contract for this audit since the statute does not allow it to be done in house.

8 Discussion and Possible Direction to Staff Regarding Agenda Items for Next Audit Committee Meeting (November 16, 2015)

Ms. Walker said the CPA firm will present the financial audit results. Staff will present the EQAB sunset review and the construction audit on Scottsdale Road improvements, Phase 1. If time permits, she may have staff discuss the audit report review process briefly.

Public Comment

No members of the public wished to address the Committee.

Adjournment

The meeting adjourned at 4:57 p.m.

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