SANTA CLARA CITY

Special Project
January 2014 – August 2017

Report No. SANT-18-SP

OFFICE OF THE
STATE AUDITOR

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SANTA CLARA CITY

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OFFICE OF THE
STATE AUDITOR

April 25, 2018

Rick Rosenberg, Mayor
Santa Clara City

and

Santa Clara City Council

Dear Mayor Rosenberg and Council Members:

The Office of the State Auditor has a hotline program through which we receive complaints with financial or compliance implications related to state and local governments. We received a complaint alleging that an employee of Santa Clara City ("City") owned an outside business, which the employee allegedly operated on City time, with City resources, and/or by using the employee's position with the City to promote the business. The complaint further stated that the employee did not disclose the conflict of interest in a timely manner.

We gathered information from all involved parties and reviewed relevant documentation as necessary. We appreciate the cooperation received in this matter from both the City and the employee, who has since terminated her employment with the City.

The results of our investigation are included in the attached findings and recommendations section of this report.

Our procedures were more limited than would be necessary to express an opinion on any of the items referred to above or to express an opinion on the effectiveness of the City's internal control or any part thereof. Accordingly, we do not express such opinions. Had we performed additional procedures or had we conducted an audit of the effectiveness of the City's internal control, other matters might have come to our attention that would have been reported to you.

By its nature, this report focuses on exceptions, weaknesses, and problems. This focus should not be understood to mean there are not also various strengths and accomplishments. We appreciate the courtesy and assistance extended to us by the personnel of the City during the course of the engagement, and we look forward to a continuing professional relationship. If you have any questions, please feel free to contact Leslie Larsen, Audit Supervisor, at 801-538-1348 or leslielarsen@utah.gov.

Office of the State Auditor

Office of the State Auditor

BACKGROUND

In early 2014, a Santa Clara City (City) employee (Employee) verbally informed her supervisors that she had begun an outside business venture to develop software designed to assist municipalities to track building inspections and other tasks (Software). When sufficiently complete, the Software was used by the City at no charge for a period of time. In late 2014, City personnel asked Employee to gather and provide comparison information, including pricing, between Software and other competitive products. Employee asked her private business partners to create a comparison document which presented cost, as well as various features, of all competing software products. The City Council relied on this comparison document when it approved the formal contract for use of Software in December 2014.

Due to insufficiently detailed time records, we were unable to substantiate, other than a few minor instances, that Employee operated her private business on City time or used City resources. Employee voluntarily terminated her employment with the City in August 2017.

FINDINGS AND RECOMMENDATIONS

1. CONFLICT OF INTEREST NOT PROPERLY RECOGNIZED OR DISCLOSED

The City did not ensure that proper disclosure of Employee's outside business interest was made to the City. Several City personnel confirmed that Employee had verbally disclosed her secondary employment and business interest and, in February 2015 (which was after the contract decision), had provided written disclosure of secondary employment to her supervisors in accordance with City policy section VII.14. However, these disclosures did not satisfy the requirements of Utah Code 10-3-1307 of the Municipal Officers' and Employees' Ethics Act, which required Employee to publicly disclose her business interest to the governing body immediately prior to the body's discussion of matters related to the business since Employee had not previously filed a sworn disclosure with the mayor. The public disclosure must also be entered in the minutes of the meeting. Neither the audio recording nor the written minutes of the December 2014 City Council meeting reflect such a public disclosure. In addition, we spoke with several City Council members who do not recall being aware that Employee was involved in the business at the time.

Furthermore, due to Employee's improperly disclosed interest in the Software business, as well as the problems with the procurement process discussed in Finding No. 2, Employee was allowed the ability to have influence over the procurement process. When employees who have a personal interest are allowed to influence the procurement process, there is an increased risk of fraud, waste, or abuse.

City personnel who were aware of Employee's business interest should have ensured that the conflict was properly disclosed to the governing body and should not have allowed Employee to have influence over the procurement process.

Recommendations:

We recommend that the City:

- **Re-procure the City's contract for building inspection software to ensure the City has obtained a fair price for the software and services.**
- **Educate its employees on the importance of compliance with Utah Code 10-3 Part 13, Municipal Officers' and Employees' Ethics Act and ensure proper disclosure of conflicts of interest.**
- **Ensure employees with a conflict of interest are not allowed to have influence over the procurement process.**

2. IMPROPER PROCUREMENT OF INSPECTION SOFTWARE

We reviewed the procurement process and resulting contract for the City's use of Software, as well as the City's written *Purchasing Procedural Guide*. It should be noted that, although the City does have a written *Purchasing Procedural Guide*, because it has not formally established its own procurement code by ordinance, the City is also subject to the Utah Procurement Code, as required by *Utah Code* 63G-6a-103(49)). We determined the following:

- The contract should have been procured through a formal process. Employee informally gathered and provided comparison data, including pricing, between Software and other competitors; however, according to the City's *Purchasing Procedural Guide*, products and services valued at $10,000 should normally be procured through a formal bidding process. The contract was for a term of three years and the total value of the contract exceeded $10,000. As a result, the City is in noncompliance with their *Purchasing Procedural Guide*.
- The City did not retain documentation of the informal quotes obtained by Employee. As a result, we were unable to verify that the competitor's pricing information included in the comparison document, which was created by Employee's business partners and relied upon by the City Council to make the contract decision, was accurate and for comparable product and service. Failure to retain the documentation violates both Utah Procurement Code and the City's record retention schedule.
- The contract would have been more properly procured through a request for proposal (RFP) process. Based on our review of the applicable City Council meeting minutes and the comparison document, it appears that the Council also considered some subjective evaluation criteria, such as "user-friendly platform," when making the contract decision. According to Utah Procurement Code, if an entity uses subjective criteria to make contract decisions, an RFP process should be followed.
- Because the comparison document was prepared by one of the vendors competing for the contract and included all vendors' quote amounts, it was improper for the City Council to rely on the comparison document to make the contract decision. However, it appears the City Council was not aware that the comparison document was created by one of the competing vendors. This situation illustrates the importance of following

appropriate procurement policy and Utah Procurement Code, where applicable, as well as proper recognition and disclosure of potential conflicts of interest, as discussed in Finding No. 1.

Procurement policies ensure transparency, fair and equitable treatment, and increased competition, which results in increased economies. When an entity fails to comply with proper procurement policies and practices, it creates increased risk of fraud, waste, and abuse.

Recommendations:

We recommend that the City:

- **Ensure all procurement is in compliance with Utah Procurement Code and City procurement policy.**
- **Retain all procurement documentation in compliance with Utah Procurement Code and the City's record retention policy.**
- **Ensure that the appropriate procurement method, such as RFP, is used for all procurement transactions.**
- **Educate all City personnel on the importance of adhering to proper procurement policies and procedures, as well as recognizing and disclosing potential conflicts of interest.**

Auditor's Concluding Remark

The City's response to finding No. 2 (see attached) demonstrates a failure to understand what constitutes proper government procurement. It is the governing body's duty to ensure proper use of public funds, which includes compliance with procurement law.

State of Utah Division of Purchasing reviewed the contract and concurs that the contract is for a period of three years. While the City argues that the City Council had only approved the contract for a portion of that period for which that aggregate value was below the procurement threshold, the historical actions of the City indicate that was a meaningless time limit. As such, the City's argument appears to be rationalizing actions that constitute divided procurement, or "bid-splitting," as prohibited by Utah Code 63G-6a-2404.3. To split the three-year contract into smaller purchases, the City would have improperly circumvented the procurement threshold specified in its own procurement policy.

Regardless of the City's compliance or noncompliance with its own procurement policy, the inability of the City to provide documentation of a competitive procurement process nonetheless presents a violation of Utah Procurement Code.

Attachment A

Mayor
Rick Rosenberg

City Manager
Edward O. Dickie III

City Council
Jerry Amundsen
Herb Basso
Mary Jo Hafen
Kenneth Sizemore
Jarett Waite

April 17, 2018

Via email to aburgoyne@utah.gov

State Auditor John Dougall
Utah State Capitol Complex
East Office Building, Suite E310
Salt Lake City, UT 84114-2310

Re: Santa Clara City's Response to Auditor's Report

State Auditor John Dougall:

I am writing in response to the draft Auditor's Report provided to Santa Clara City on April 13. The City's specific responses to your office's findings and recommendations are set forth below. I request that this letter be appended to the final Auditor's Report as indicated in your correspondence.

1. CONFLICT OF INTEREST NOT PROPERLY RECOGNIZED OR DISCLOSED

The City partially disputes the Auditor's findings in this regard. Although I agree that the Employee did not formally disclose her business interest in writing until February 2015, I believe that certain factors mitigate this issue that were not recognized by the Report.

As noted, the Employee verbally disclosed her work on the building inspection software (the "Software") much earlier than February 2015, but the characterization of her work as "secondary employment" or a "business interest" prior to December 2014 is difficult to justify. It is the City's understanding that prior to the City's approval of the December 2014 contract, Employee received no compensation or revenue for her work on the Software, and she formed a business entity for the Software only later, in February of 2015. It might be more accurately described as a hobby when it was used by the City free of charge. Therefore, I agree that it would have been appropriate for Employee to have disclosed her work in writing as a "business interest" by December 2014, but the City disputes any suggestion that written disclosure should have been required prior to that date.

These points being made, I agree that Employee should have made a formal disclosure in the December 2014 City Council meeting, and the City acknowledges the recommendations of the Report with respect to these issues, and the City responds as follows:

- The City anticipates re-procuring the City's contract for building inspection software prior to July 1st of this year, and will do so using an RFP process which is compliant with

applicable law.

- The City is preparing, and is anticipating adoption of, a new procurement policy to replace its outdated prior policy, and to ensure compliance with state law. The policy will be presented to the City Council for approval at its next regular meeting on April 25th. Anticipating adoption of the new policy on that date, the City has scheduled a procurement training meeting for the morning of April 26th in order to educate all city department heads about the new policy and to encourage full compliance, and at that same time, training will be provided on the importance of compliance with Utah Code 10-3- Part 13, Municipal Officers' and Employees' Ethics Act and proper disclosure of conflicts of interest.
- The City's new procurement policy will reinforce that employees with a conflict of interest will not be allowed to have influence over the process.

2. IMPROPER PROCUREMENT OF INSPECTION SOFTWARE

The City acknowledges that at the time of the relevant events, the City was operating under a purchasing procedure that was outdated, having been adopted by resolution prior to the existence of the current state procurement code. As noted above, the City is currently in the process of preparing and proposing for adoption a new procurement policy, anticipated to be enacted by ordinance at the next regular meeting of the City Council on April 25th.

The City disputes the Report's interpretation of the Software contract as a three-year contract having a total value exceeding $10,000. A review of the contract, and particularly sections 2 and 17 where a 3-year term is referenced, it also says that the fee is to be negotiated annually. The contract further states that the City could terminate the contract at any time with thirty days' notice. Taken together, these provisions suggest that the contract did not actually bind the city for three years, as the option to renew was little more than an opportunity to negotiate an extension, with no obligation for either party to agree to any extensions if they didn't like the price. Under these terms, even with the price remaining the same, the City could have walked away from the contract at the end of any 1-year term without consequence or liability.

Furthermore, this analysis is consistent with the presentation of the contract to the City Council for approval in December 2014. The minutes suggest that the City Council was presented the contract as covering the partial year from Dec. 2014 to June 2015, and the initial contract year of July 2015 to June 2016. This is also consistent with the "payment schedule" attached as Schedule B to the contract, which provides $3,933.36 for the partial year, plus $5000 annually thereafter. There is no indication in the minutes of any discussion of renewals beyond the initial full year (July '15-June '16).

Notwithstanding these points, the City acknowledges the recommendations of the Report with respect to these issues, and the City responds as follows:

- As noted above, the City is preparing to adopt a new procurement policy, by ordinance, which will be fully compliant with state law.
- As part of the procurement policy review, the City is giving due attention to its document and records retention policy.
- The City's new procurement policy will ensure proper procurement methods are

followed.

- As noted above, City department heads will participate in training on the City's new procurement policy the day after its adoption by the City Council is anticipated, and that training will include material regarding the importance of disclosing potential conflicts of interest.

We appreciate the opportunity to respond, and recognize the many hours of work your office completed in order to investigate and prepare the Report.

Respectfully,

Mayor Rick Rosenberg

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