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## City Council Staff Report

**From: City Manager**

**Report Type: ACTION ITEMS**

**Lead Department: City Auditor**

**Meeting Date: September 23, 2024**

Report #:2408-3409

### **TITLE**

Review the Procurement Process Review Audit and Supplemental Information Regarding Competitive Solicitation Outcomes and Approve the Audit

### **RECOMMENDATION**

The City Auditor's Office recommends City Council approve the Procurement Process Review Audit

### **EXECUTIVE SUMMARY**

The Procurement Process Review Audit was presented to the Policy & Services Committee on August 13, 2024. Committee members raised certain questions about the scope of the audit work performed. The Committee did not unanimously approve the audit necessitating presentation of the audit to the full City Council. Both the City Auditor's Office and the Administrative Services Department reviewed prior analysis performed and data from the audit period to provide additional information for Council members to consider which is provided in the *Background* and *Analysis* sections of this staff report.

### **BACKGROUND**

Work for the Procurement Process Review Audit was approved by City Council as part of the FY23 Annual Audit Plan. The audit was completed and a first draft sent to the department in December of 2023. Due to changes in the Administrative Services Department (ASD) and City Auditor' Office Management at the beginning of 2024, the audit report and management response were not finalized and presented to the Policy & Services Committee until August 13, 2024. Policy and Services Committee members raised certain questions about the results of the audit and the scope of work that was completed. The City Auditor has followed up on the Committee's request for additional information and provides answers to these questions in the *Analysis* section of this staff report for City Council consideration.

Additionally, the City Auditor would like to note the general process for City Council to direct the Audit Office's work each year. The Auditor suggests following this process if there is interest in requesting further work related to the procurement function. Each year, the Auditor's Office conducts a risk assessment to identify topics and areas of concern for potential inclusion on the annual audit plan. The Auditor's Office is currently conducting risk assessment interviews with Council Members and the Executive Leadership Team. The information gathered in these interviews will culminate in a draft FY25 Audit Plan. The FY25 Audit Plan will be presented to City Council in November 2024 for approval. The Auditor's Office encourages participation in the risk assessment process as it provides a systematic and consistent approach to identifying risks and elevating those risks for City Council consideration in directing the Audit Office's work for the following fiscal year.

## **ANALYSIS**

The Procurement Process Review audit stated objectives were to:

- 1) Determine whether the needs assessment, budgeting, solicitation, and vendor selection processes are efficient, effective, and transparent to ensure value for money and fair competition.
- 2) Determine whether the procurement process is valid through proper approvals, adequate segregation of duties, and compliance with applicable laws, regulations, and the City's policies.
- 3) Determine whether technology is used appropriately and effectively to enhance integrity, efficiency, transparency of the procurement process and ensure consistency and validity of the relevant information and data.
- 4) Identify the opportunities to improve the efficiency and effectiveness in the procurement process.

The audit objectives, particularly 1 and 4, were stated in broad terms that could apply to many aspects of the procurement system. As a full review of the entire procurement system and its overall performance would far exceed the time and budget allotted for this audit engagement, the audit team scoped and focused their assessment on the City's procurement process design of internal controls, including procurement policies, procedures and processes. These internal controls were assessed for their alignment with best practices associated with the efficient, effective, and transparent procurement of goods and services in order for the City to provide value for money and facilitate fair competition. While the audit did not assess the overall outcomes of the procurement process, it did test a sample of contracts for compliance with established City procurement practices.

A sample of fifty contracts from FY22 and FY23 were tested on the following criteria to determine if:

1. Contracts were appropriate, current, and accurately reflected terms and conditions and whether these conditions aligned with expectations identified within the corresponding

chapter of the City's Purchasing Manual for each type of solicitation and with the City's Municipal Code.

2. Procurement documents including contracts, purchase orders, invoices and approval documents were properly maintained and accessible including the presence of internal documents, Appendix G and Appendix E, and if they were completed in accordance with the City's Purchasing Manual and Municipal Code.
3. Initiation process for purchasing requests at the department level follow the City's signature authority in accordance with the City's Contract Solicitation and Award Limits Summary and approvals were obtained at the department level, purchasing department, and legal department as necessary.
4. Appropriate segregation of duties existed during the procurement process as the preparer, reviewer, and approvers were independent of each other and supporting evidence and documentation were present.
5. The competitive bidding process followed the City's Municipal Code as required and the selection criteria was fair and transparent.
6. The vendor selection, evaluation and approval process were reasonable per review of supporting documentation.

The audit reported four findings based on testing the 50 contracts on the above criteria. A brief summary of these findings follows:

- Finding 1 noted that while most (44) of the contracts reviewed had the appropriate documentation supporting that policies and procedures were followed and internal controls operating as intended, a few contracts were missing key documentation:
  - 4 contracts did not include *Appendix G, Solicitation Plan Checklist* but should have included this documentation.
  - 2 contracts did not include *Appendix E, Exemption from Competitive Solicitation* but should have included this documentation.
- Finding 2 noted that the City's purchasing manual required updates and was missing procedures to execute a "Design Build" contract. However, the City does have policies and procedures in place for different types of contracts and solicitations and the audit evaluated the efficiency, effectiveness, and transparency of the procurement process for these various types of contracts and did not note any additional areas for improvement.
- Finding 3 noted that needs assessments and market analyses are completed by individual departments and these processes are not formalized in the purchasing manual which may lead to inconsistent practices.

- Finding 4 noted that the technological systems used to support the procurement process allow for the ability to create duplicate vendors in the system. While the City has controls related to who can create vendors in the system, there are several risks associated with this practice including the potential for making duplicate payments and generating fraudulent invoices. The audit did not complete any additional testing to determine if errors in billing had been made as a result of the duplicate vendors.

Policy & Services Committee Members specifically asked about testing related to competitive bidding procedures. The audit did evaluate documentation for each contract to confirm whether competitive bidding practices were followed (see Finding 1 and criteria number 5 above). In response to Committee Members questions, the City Auditor completed a second assessment of 11 of the 50 contracts sampled and noted the following characteristics:

- 3 of the 11 contracts were exempted from the competitive bidding process as they were the sole vendor operating in that space in CA at the time of the solicitation
- 6 of the 11 contracts received multiple bids
  - 3 selected the lowest bidder
  - 3 selected the Best Value (2 of these 3 had external panelists serving on the bid review panel in addition to the Palo Alto employees)
- 2 of the contracts failed testing due to not having the appropriate documentation to support the exemption (see Finding 1, above)

In response to questions asked at the August 13<sup>th</sup> Policy & Services Committee meeting, Administrative Services Department (ASD) staff provided the following summary of contract solicitations between July 2023 and July 2024. Please note this information has not been verified by the City Auditor but serves as part of the Management Response.

- 105 formal solicitations
- 3 solicitations (3% of the total) received no bid
- 27 solicitations (26% of the total) received only 1 bid

ASD staff summarized vendor feedback on solicitations that received 1 or no bids. The primary themes of this feedback were:

- Vendors were not available to take on the City project (not enough bandwidth)
- Vendors did not have the requested products and/or expertise

Some vendors did not respond to the City's request for feedback and a few cited forms and/or the e-procurement system as reason for not submitting a bid.

## **FISCAL/RESOURCE IMPACT**

Work conducted for this audit and in responding to subsequent requests for information is within the approved scope and compensation of the contract with Baker Tilly.

**STAKEHOLDER ENGAGEMENT**

The City Auditor's Office met with relevant City leadership and staff and City to gather information and conduct work for this audit activity.

**ENVIRONMENTAL REVIEW**

Council action on this item is not a project as defined by CEQA because the audit activities do not involve any commitment to any specific project which may result in a potentially significant physical impact on the environment. CEQA Guidelines section 15378(b)(4).

**ATTACHMENTS**

Attachment A: Procurement Process Review Audit

**APPROVED BY:**

Kate Murdock, City Auditor