



THE CITY OF SAN DIEGO

DATE: June 12, 2017

TO: Herman Parker, Park and Recreation Department Director

FROM: Eduardo Luna, CIA, CGFM, City Auditor  
Office of the City Auditor

SUBJECT: Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse

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The Office of the City Auditor received an anonymous Fraud Hotline report alleging that a City employee has been “pocketing” money paid for recreation activities. The report claimed that the City employee is the owner and operator of a for-profit company and has been overcharging participants and inappropriately collecting additional cash payments related to the activities. During our investigation, we identified a second City employee-owner of a different business that provides similar recreation activities to the public. Both City employees operate their businesses under permits at various Recreation Centers throughout the City. The City’s outside employment policy allows employees to operate private businesses under certain circumstances, but requires the employees to notify management about the outside business activity and seek approval prior to starting the business activity.

The City does not restrict or control the fees that private companies charge participants for permitted recreation activities conducted at City facilities. As such, we did not review the initial allegation regarding overcharges for activity fees. However, we identified a risk that the recreation center employees issuing permits for these activities were not charging the appropriate permit fees, or were otherwise abusing the permit process in favor of their coworkers and the private businesses owned by the two City employees. We also identified risks that the two employees were not complying with the City’s policy regarding outside employment, and that the Department’s practices are inconsistent with a recent interpretation of City policy.

## Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse

We determined that 10 Park and Recreation Department employees undercharged their coworkers over \$6,500 for permits. Half of the permits were issued after the start of the permitted activity. One permit was issued 90 days after the start of the permitted activity. Issuing permits after the start of the activity is against Department policy and is an abuse of the employees' authority. The evidence did not support a finding of intentional fraud in this case. However, neither employee-owner fully complied with the City's policy regarding annual outside employment notifications. It also appears that the Department's outside employment practices are inconsistent with a recent interpretation of City policy. Although our investigation did not focus on permit administration throughout the Park and Recreation Department, we identified potential improvements related to the Department's permit processing software that could improve the accuracy of future permit fee calculations.

We made five recommendations to improve internal controls and hold the responsible employees accountable. The Department agreed to implement all five recommendations.

### **City employees undercharged their coworkers over \$6,500 for permits**

Our investigation reviewed and re-computed the fees related to 44 permits issued to both City employee-owned companies between March 28, 2014, and January 11, 2017.

We made the following determinations regarding permit fee calculations:

- 30 permits contained undercharges totaling \$6,563.00 (7 percent of fees charged)
- 9 permits contained overcharges totaling \$2,556.75 (3 percent of fees charged)
- 39 permit errors
- 4 permits contained both undercharges and overcharges in the same permit
- 35 permits incorrectly calculated
- 9 permits were correctly calculated
- 44 total permits reviewed

The majority of the permit calculation errors related to fees payable to Recreation Councils. These funds subsidize recreation activities, special events, and recreation center maintenance projects. A small portion of the permit calculation errors related to General Fund revenues.

## Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse

In total, 10 different Park and Recreation Department employees at six different recreation centers issued the permits we reviewed. Interviews and other data we obtained did not suggest that City employees, other than the employee-owners, had financial interests in the companies. Furthermore, all but nine of the permits were incorrectly calculated, and the errors we identified included both undercharges and overcharges. Therefore, it does not appear that either employee-owner worked in collusion with City staff to receive unauthorized discounts. However, the 80 percent<sup>1</sup> error rate in permit fee calculations we found, and the dollar amounts, were sufficient to support a finding of waste related to the incorrect charges.

According to Department management, after the permits are issued there is currently no independent review of permit fee calculations to ensure their accuracy. At the time the permit is issued, Department policy calls for a second staff member to be present to ensure that the fees shown on the permit are received and processed accurately. The permit data do not include documentation that a second staff person was present and verified the accuracy of the calculations. Thus, we were unable to confirm that Department policy was followed when the 44 permits we reviewed and re-computed were processed. The Department would need to resolve that question through interviews with staff as part of an independent fact-finding investigation, which is part of the City's disciplinary process.

### **The Department's software does not automatically compute all permit fees**

Although the Department uses software to record permit fees, the calculation process is manual for some fees. Additionally, the software system lacks an error handling process to check if a fee is missing from the permit. For instance, charges related to keeping the recreation center open beyond the normal operating hours must be manually computed and entered, as necessary. Most of the permits that contained undercharge errors related to manually under-counted hours. Specifically, the under-counted hours reduced the fees collected for keeping the facility open beyond the recreation center's normal hours of operation, and the majority of the errors related to a \$15 per-hour, per-court fee payable to the Recreation Councils.

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<sup>1</sup> In total, 35 out of 44 permits were incorrectly calculated, which corresponds to an 80 percent error rate in permit fee calculations.

**Department staff who issue permits after the start of the activity violate City policy and abuse their authority**

We determined that Department employees allowed their colleagues to conduct scheduled activities for up to 90 days prior to obtaining a paid permit. The Department's Fee Schedule states, "Permits are not issued until payment is received." Allowing City employee-owned companies to begin activities prior to obtaining a valid, paid permit is an abuse of the employees' authority to issue permits and appears to be a violation of the City's Code of Ethics and Conduct. Specifically, Personnel Manual Index Code G-1(II)(K) states:

Employees must adhere to the rules of work and performance established as standards for their positions by the appropriate authority.

As a next step, the Department would need to conduct an independent fact-finding investigation, which is part of the City's disciplinary process, and take the appropriate corrective actions with respect to the identified employees.

**Permits issued after the start of the activity expose the City to liability**

In addition to receiving payments before the start of the permitted activity, the permitting process requires City staff to obtain proof of insurance. Failing to obtain and review proof of insurance coverage in advance could expose the City to legal liability in the event of serious injury, death, or other claims if the business lacks adequate coverage but was allowed to use a City facility. We did not find evidence that the required insurance and liability waiver forms were obtained in advance. Since 22 out of the 44 permits we reviewed were issued after the permitted activities began, we concluded that the insurance reviews and liability waivers were likely not performed in advance. The Department would ultimately need to resolve this question through an independent fact-finding investigation as part of the City's disciplinary process.

Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse

**City employees issued most permits to their coworkers up to 90 days late**

Our investigation determined that nine Park and Recreation Department employees issued permits to the City employee-owned companies after the multi-week activities began. We made the following determinations regarding permit issue dates:

- 22 out of 44 permits were issued between one and 90 days after the activities began
- 20 permits were issued on the same day that the activities began; the Department considers permits timely if they are issued on the same day as the start of the activity
- 2 permits were issued prior to the start of the activity (one permit was issued one day prior to the start of the activity, and the other permit was issued 17 days prior)

As summarized in **Table 1** below, nine out of the ten Department employees who processed permits that were included in our investigation issued permits after the start of the recreation activity, which is a violation of Department policy. The table below illustrates the number of days after the start of the activities that the permits were issued.

**Table 1**  
**Summary of Permits Issued After the Start of the Activity**

Number of Days After Activity's Start	1	2	3	4	5	6	7	8	14	16	21	49	90	Total
City Employee Name Redacted	1													1
City Employee Name Redacted									1					1
City Employee Name Redacted												1	1	2
City Employee Name Redacted	1						1		1					3
City Employee Name Redacted				1										1
City Employee Name Redacted	1													1
City Employee Name Redacted											1			1
City Employee Name Redacted	3	1	1		1	1		1		1				9
City Employee Name Redacted			1			1	1							3
<b>Total</b>	<b>6</b>	<b>1</b>	<b>2</b>	<b>1</b>	<b>1</b>	<b>2</b>	<b>2</b>	<b>1</b>	<b>2</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>22</b>

In summary, we found that 22 out of 44 permits were not issued prior to the start of the activities. This equates to a 50 percent error rate for timely permits.

**Neither employee complied with outside employment policies**

Numerous policies and regulations related to conflicts of interest and employee conduct are contained in the City's Administrative Regulations, Personnel Manual, and Departmental Instructions. For instance, Administrative Regulation 95.60, section 3.5(a) requires City employees to obtain departmental approval prior to engaging in outside business activities and to notify management in writing if they are engaged in an outside business activity. Personnel Regulation Index Code G-6 prohibits conflicts of interest between outside employment and the employee's responsibilities to the City.

According to the documents we obtained and reviewed related to the two City employee-business owners, neither employee fully complied with the City's requirement for notification of outside employment. One employee was missing a notification form for one of the years the business was in operation, the other employee had no notification forms disclosing the business operations in question. Furthermore, only one employee file contained the pre-approval form required prior to starting outside business activities.

**The Department's outside employment practices may be inconsistent with a new interpretation of the City's Conflict of Interest policy**

The Department's long-standing policy has been to prohibit employees from working for non-City entities at their assigned work location. Under the policy, the Department allowed employees to work for outside agencies at City facilities other than their assigned work location to avoid the appearance of a conflict of interest. During our investigation, the Human Resources Department and City Attorney's Office reviewed the Department's practices in light of a different sub-section of the City's Conflict of Interest policy. Under the new interpretation, Department employees are prohibited from conducting work at any City facility if the work is within the employee's "discipline or profession" and "subject to issuance of a permit by their City department." Specifically, the City's Conflict of Interest and Employee Conduct Administrative Regulation 95.60, section 3.5(c)(1), states:

Employees shall not work within their discipline or profession for a company or as a self-employed consultant when their work is reviewed, or approved, or is subject to issuance of a permit by their City department.

This apparent inconsistency between the Department's practices and the new interpretation of the City's Conflict of Interest policy raises issues for multiple other Department activities and has Citywide implications.

Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse

**Conclusion**

We reviewed 44 permits issued by 10 different Park and Recreation Department employees at six different recreation centers, and a majority of the permits were incorrectly calculated.

Based on the distribution of error types across multiple facilities and City staff, it does not appear that either City employee and business owner worked in collusion with City staff to receive unauthorized permit discounts. The net dollar amounts of the undercharges and overcharges we found were \$6,563.00 and \$2,556.75, respectively. Thus, the magnitude of the undercharge errors (7 percent of the amount collected) was significant. Additionally, the 80 percent error rate in permit fee calculations we found was sufficient evidence to support a finding of waste related to the incorrect charges. We also determined that 50 percent of the permits were not issued in advance of the permitted activity, as required by the Department's policy, which was sufficient to support a finding of abuse of authority with respect to the permit issuance. Finally, we determined that neither employee-owner complied with the City's policy regarding annual outside employment notifications.

A detailed, confidential version of this report was provided to Department management to allow the appointing authority to review, investigate, and take the appropriate disciplinary action. California Government Code §53087.6 (e)(2) prohibits public disclosure of the identity of the subject employees.

We made five recommendations to improve internal controls and hold the responsible employees accountable. The Department agreed to implement all five recommendations.

## Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse

### **Recommendations and Management's Responses:**

We recommend that the Park and Recreation Department:

1. Review the details of the Confidential Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse report, conduct an independent fact-finding investigation to determine if City policy was violated, and take the appropriate corrective action.

#### **Management Response: Agree.**

Both the public and confidential reports have been reviewed in detail and a fact finding/investigation has been initiated. Park and Recreation Management will take appropriate action based on the findings of the investigation.

Additionally, Park and Recreation Management feel that the following points are important to note as part of the response. First, we disagree with the term 'abuse' as it is used in this report. While it is clear that employees did not follow policy and procedure in the permit process, based on the analysis completed to date by Park and Recreation Management, there were errors/differences in interpretation of the fee schedule; general errors in the fees applied, or not applied; and the permits did not show the specific information upon which the charges were based. While these issues are problematic and are of significant concern to Park and Recreation Management, the repetition of the word 'abuse' in this report lends a sense that the employees issuing the subject permits willfully abused policy in favor of the two businesses. We feel that is both inaccurate and unfair to use that word repeatedly, when the Auditor also states that there was no proven link between the employees and the business owners. It is also important to know that the same Park and Recreation employees both overcharged and undercharged the City employees for their contracts/permits; this fact would seem to also challenge the conclusion that the employees were 'abusing' the system in favor of their colleagues.

Park and Recreation employees see the issuance of a permit to the public as a service by the City to its patrons and will work to find the most favorable method possible to calculate permit fees to the benefit of the patron. This is a mark of the "heart of service" which Park and Recreation employees strive to achieve in their daily activities. Typically, Park and Recreation employees do not see permits or fees as a revenue source. As the City Auditor staff reviewed the permits, their intention and expectation, quite rightly, was to find an identical process in fee calculation and fee schedule application for each permit. The Park and Recreation Department needs to ensure that the desire to serve the public does not compromise the correct and consistent application of the fee schedule, and that the process used in calculating the fees is clearly identifiable based on the permit materials available to anyone who reviews and/or audits them.

A second point: When Park and Recreation employees calculate the 'per hour' fees (Recreation Council and Non Hours of Operation [NHO] fees), the schedule provided by the permittee to calculate the per hour fees is used. In many cases the number of hours the permittee will use the court is less at the end of the season, primarily in the last two to three weeks, based on playoffs, which require less games and thus less court time. As such, Park and Recreation employees would calculate the number of hours for the



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Recreation Council fee and the NHO fee based on the actual number of hours to be used and not the number of hours the court is reserved in ActiveNet. However, to show this change on the permit, a manual input and override would be required in the ActiveNet system, and in most cases employees issuing the permit did not make that manual change. Park and Recreation Management understand the City Auditor's analysis that if the court is reserved in the online system, and the reservation is shown on the permit, the permittee should be charged for the time the court is reserved. We have committed to re-train staff and reconfigure the system to ensure number of hours to be charged is shown on the permit itself and not just 'understood' from the schedule that may be provided by the permittee, as schedule documentation is not a part of the electronic record of the permit and thus does not have a sound audit trail. The permit should show the actual hours reserved and used for all weeks of the season, and the permittee charged accordingly.

### **Target Implementation Date: September 2017**

2. Review the identified permit fee errors and ensure that the fees due to the permittees, the City, and the Recreation Councils are properly collected and disbursed.

### **Management Response: Agree.**

The Park and Recreation Department has completed the first portion of the recommendation. Park and Recreation Management have reviewed the subject permits and compiled information about the undercharges and overcharges. Park and Recreation Management will take action and work with the Treasurer's Office and other City staff to ensure that accurate fees, according to the actual use of the facility, are collected and/or disbursed, according to City policy and procedure.

### **Target Implementation Date: September 2017**

3. Develop internal control procedures to review permit fee calculations to ensure that the amounts due are computed correctly and verify that the permit was issued in advance of the event, as required.

### **Management Response: Agree.**

It is clear there were mistakes made in the fee calculations and the Park and Recreation Department is in the process of in-depth, multipronged actions to ensure that performance issues and/or misconduct are identified on the part of the employees involved in the permit processes detailed in the reports. Park and Recreation Management will address those issues in the appropriate manner, either through additional training, discipline or both, as warranted in each situation. Park and Recreation Management will also initiate updated training of all staff issuing permits to ensure full compliance with and understanding of the fee schedule as well as permit policies and procedures. This training will include more detailed instructions and procedures so that interpretation of the fee schedule and use of the 'ActiveNet' on line permitting system is consistent from employee to employee and facility to facility.

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Park and Recreation Management also feel it is important to note here that an independent review of each permit, immediately after the permit calculations have been completed, would not be possible without the addition of dozens of staff; the Department issues thousands of permits annually. Park and Recreation supervisors do conduct annual reviews of recreation center revenue and finances, which includes reviews of permits. While there is currently no formal documented procedure for these reviews, Park and Recreation supervisors do review permit work after the fact on an annual and random check basis and provide guidance and correction to their employees when issues are noted. To provide a more formal procedure for this review, the Park and Recreation Department Fee Committee will assist Management in developing clear training, audit and review procedures to ensure the accurate, consistent and timely collection of permit fees. The process to review needed training and audit procedures will begin in July 2017 and conclude with initial recommendations by the end of September 2017. Random audits of permits began in May 2017, with documented results and will be ongoing.

**Target Implementation Date: September 2017**

4. Improve software configuration to reduce permit processing errors and ensure compliance with the existing Fee Schedule and Departmental policies.

**Management Response: Agree.**

The Department will analyze ways to further automate the fee process and is open to specific recommendations from City Auditor staff or others on ways to reconfigure the ActiveNet software application to further standardize and automate fee calculations and permits. This action will be initiated next fiscal year, after the conclusion of the fact finding processes identified in Recommendations 1 and 2 above, which may provide additional information for possible changes to the ActiveNet software/system.

**Target Implementation Date: July 2018**

Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse

5. Address the apparent conflict between the Department's long-standing policy allowing outside employment at non-assigned work locations and the prohibition as described in Administrative Regulation 95.60, section 3.5(c)(1).

**Management Response: Agree.**

The Park and Recreation Department disagrees with the statement that Department policy and actions are in an apparent conflict with the subject Administrative Regulation (AR). As indicated in the report previously, the City Auditor was made aware of a new interpretation of AR 95.60, specifically, that reviewing Administrative Regulation 95.60, section 3.5(c)(1) the City Attorney stated to City Auditor staff that the regulation specifically prohibits outside employment under specific circumstances. That section states the following:

***“Employees shall not work within their discipline or profession for a company or as a self-employed consultant when their work is reviewed, or approved, or is subject to issuance of a permit by their City department.”***

As was stated above, the Park and Recreation Department's long-standing policy has been to prohibit employees who work for non-City entities from working at their assigned City work location, while the Department allows employees to work for outside agencies at other City facilities as long as that employment did not conflict in any way with their City employment. However, this new application of the AR would apparently prohibit Department employees from conducting work at **any** location if the work is within the employee's "discipline or profession" and most significantly "*subject to issuance of a permit by their City department.*" The Park and Recreation Department worked closely with the City Attorney's office as well as the Human Resources Department to develop the specific prohibitions and review of outside employment currently in practice. Additionally, our current written memo was developed as part of our adoption of an Auditor's office recommendation made in 2012.

Many recreation employees have secondary employment in recreation or related fields, and in working with Human Resources and the City Attorney's office in the past, the language above in bold italics was not understood to include contracts/permits to rent City facilities, but rather was more of a prohibition against a specific piece of work being reviewed and approved by their department in a regulatory fashion, i.e. a building inspector reviewing and approving permits for the company for which he worked. The much broader prohibition now included above was not contemplated previously and has broader implications beyond the two subject employees and this report. This interpretation could prevent employees who have a catering business from applying for a permit for an event to provide catering services at any City facility, or an employee who is an event planner to apply for an event, such as a wedding or party at any City facility, and so on. Both of these employment types could be considered recreation activities.

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On March 30, 2017, Administrative Services Manager Rebeca Cordova requested that the Human Resources Department incorporate clarifying language into Administrative Regulation 95.60 - Conflicts of Interest and Employee Conduct. A new section is being drafted to provide the clarification requested. This language is pending finalization through the Administrative Regulation review process, including completion of the meet and confer process with the recognized employee organizations.

With these contacts and recommendations, Park and Recreation consider their role within this recommendation completed.

**Target Implementation Date: September 2017**

Hotline Investigation of Recreation Activity Permit Calculation Errors and Abuse

The information in this report is being provided to you under the authority of California Government Code §53087.6, which states:

(e) (2) Any investigative audit conducted pursuant to this subdivision shall be kept confidential, except to issue any report of an investigation that has been substantiated, or to release any findings resulting from a completed investigation that are deemed necessary to serve the interests of the public. In any event, the identity of the individual or individuals reporting the improper government activity, and the subject employee or employees shall be kept confidential.

(3) Notwithstanding paragraph (2), the auditor or controller may provide a copy of a substantiated audit report that includes the identities of the subject employee or employees and other pertinent information concerning the investigation to the appropriate appointing authority for disciplinary purposes. The substantiated audit report, any subsequent investigatory materials or information, and the disposition of any resulting disciplinary proceedings are subject to the confidentiality provisions of applicable local, state, and federal statutes, rules, and regulations.

Thank you for taking action on this issue.

Respectfully submitted,

A handwritten signature in black ink that reads "Eduardo Luna". The signature is written in a cursive, flowing style.

Eduardo Luna  
City Auditor