



## THE CITY OF SAN DIEGO

DATE: April 01, 2010

TO: **Honorable Mayor, City Council, and Audit Committee Members**

FROM: Eduardo Luna, City Auditor

SUBJECT: **SDDPC Governance Recommendations Follow-up**

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In May 2009 and December 2009, we issued two audit reports that reviewed San Diego Data Processing Corporation (SDDPC) budgeting practices and implementation status of prior audit recommendations. These audit reports contained 22 audit recommendations to improve the controls associated with SDDPC governance and oversight. To assist the City Council in their review of the updated SDDPC's Master Service Agreement (MSA), we conducted a follow-up review to determine if our prior recommendations had been implemented and incorporated as appropriate into the updated MSA.

### **Results of our Review**

We found that of the twenty-two recommendations from the May 2009 and December 2009 SDDPC audit reports<sup>1</sup>, thirteen recommendations have been fully implemented, four recommendations have been partly implemented; and five recommendations have not yet been implemented. Of the five unimplemented recommendations, four are planned for implementation after the acceptance of the MSA, and one has been documented as implemented, however we disagree with the assessment of the implementation.

The MSA Recommendations Team have primarily used three methods to implement our recommendations: policies and procedures, SDDPC's Bylaws, and the MSA. Fourteen of the recommendations have been implemented or are going to be implemented through policies and procedures, three have been implemented through SDDPC's Bylaws, five through the MSA, and one through a combination of the MSA and SDDPC's Bylaws. The following table summarizes the implementation status of audit's recommendations.

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<sup>1</sup> For a complete listing of the May 2009 and December 2009 audit report recommendations and their implementation status, see Attachment I and Attachment II respectively.

<b>Status of Recommendations</b>	<b>May 2009 Follow-up Report</b>	<b>December 2009 Follow-up Report</b>	<b>Total Recommendations</b>
Implemented	5	8	13
Partly Implemented	1	3	4
Not Implemented	0	5*	5*
<b>Total</b>	<b>6</b>	<b>16</b>	<b>22</b>

\* For four of the five recommendations not incorporated into the agreement, management has specific plans to implement the recommendations after the acceptance of the agreement.

### **May 2009 Follow-up Report Recommendation Summary**

We found that five of the six recommendations from the May 2009 Follow-up report have been implemented or incorporated into the agreement. The remaining issue has been partly implemented. Specifically, we recommended that the City develop additional controls over the agency budgeting process to ensure that the required budget approvals are obtained. City management is currently in the process of developing new governance procedures. Many of these processes will be documented through the Comptroller's Office, Internal Controls Section, as part of the series of Process Narratives they are compiling. Their approach appears to meet the requirements of our recommendation.

### **December 2009 Follow-up Report Recommendation Summary**

We found that eight of the sixteen recommendations from the December 2009 report have been implemented or incorporated into the agreement, three recommendations are partially implemented; and five recommendations have not been implemented.

- For the first partially implemented recommendation, (recommendation 7, which consists of five components, a-e), the City and SDDPC Management have implemented 7e, which requires SDDPC to provide an annual report to the City summarizing competitive practices. City and SDDPC Management plan to implement the remaining components of the recommendation through policies and procedures once the MSA has been executed. Their approach appears to meet the requirements of our recommendation.
- The second partially implemented recommendation (recommendation 12) requires that the City should establish encumbrances for the Information Technology Business Leadership Group's (ITBLG) approved new project costs procured through SDDPC to ensure actual costs do not exceed approved budgeted costs. City Management is currently in the process of developing new governance procedures for review and approval of IT projects and procurement. Many of these processes will be documented through the Comptroller's Office, Internal Controls Section, as part of the series of Process Narratives they are compiling. Their approach appears to meet the requirements of our recommendation.
- The remaining partially implemented recommendation (recommendation 15a) has been identified as implemented, however we disagree on the completion of the item. Specifically, we recommend the Mayor and City Council approve the hiring of the Executive Director and his/her contract terms. Management has stated they will implement a strict selection and performance policy, place a cap on compensation, and eliminate the bonus. They further stated that the SDDPC's Executive Director will be hired and fired by the SDDPC board, with input from the Mayor and Council. However, the Bylaws do not require that the Mayor and Council approve the hiring and firing of SDDPC's Executive Director as we initially recommended.

We also found that five recommendations have not been implemented. However, management has plans to implement four of the recommendations after the MSA is approved. The remaining item (recommendation 2) has been identified as implemented, however we disagree on the completion of the item. Specifically, we recommended that the City design controls to ensure a review of compliance with the Operating Agreement (OA) terms is performed annually. Management should consider requiring SDDPC to self-assess their compliance with the agreement terms and submit the assessment to the Mayor, or designee, for their review prior to executing the annual Service Level Agreement. The City indicated that this recommendation was implemented through the annual reporting requirements described in SDDPC's Bylaws. The Bylaws (Article V, Section 4) describe an annual February meeting/update to the city council. However, there is no requirement in the OA/MSA or Bylaws for SDDPC to provide a self-assessment of compliance with the agreement terms or to implement comparable controls to ensure an annual compliance assessment of the MSA occurs and is provided to the Mayor or designee.

We would like to thank the Department of IT and SDDPC for their assistance providing information for this report.

Respectfully Submitted,



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Eduardo Luna  
City Auditor

cc: Jay M. Goldstone, Chief Operating Officer  
Mary Lewis, Chief Financial Officer  
Naresh Lachmandas, Department of IT Director  
Jan Goldsmith, City Attorney  
Andrea Tevlin, Independent Budget Analyst  
Don Del Rio, SDDPC Corporate Counsel

Attachment I - May 2009 SDDPC Audit Report Recommendation Implementation Status

	<b>Audit Report Recommendation</b>	<b>Recommendation Incorporated into Master Service Level Agreement (MSA)/ New Operating Agreement (OA)?</b>	<b>Other action taken or to be taken per the City/SDDPC MSA Team Input/Recommendations/Actions Matrix</b>	<b>Auditor's Review of Implementation Status</b>
1	<p>Amend the SDDPC Operating Agreement to include the following:</p> <ul style="list-style-type: none"> <li>• Require SDDPC to develop a written budget policy;</li> <li>• Require SDDPC to submit salary and wage ranges for each of their job classifications, including actual executive salaries and benefit packages, during the annual budget process.</li> </ul>	<p>Yes – section 3.4.1.4. &amp; Section 3.3.1</p>	<p>We agree. SDDPC is currently working with the City to amend the Operating Agreement. A meeting was held on April 28, 2009 with representatives from the Office of the CIO, City Attorney and SDDPC. A working plan was created at this meeting establishing schedules, assignments, tasks and deadlines. The recommended requirements of developing a written budget policy and submitting salary and wage ranges for each job classification, including actual executive salaries and benefit packages as part of the annual budget process, will be included in the amended Operating Agreement. SDDPC looks forward to working with the City to revise and improve this agreement to increase transparency and strengthen documentation as part of the budget process.</p>	<p>Implemented,</p> <p>Section 3.4.1.4 of the MSA defines the budgeting process.</p> <p>Section 3.3.1 addresses the disclosure of wage ranges.</p>

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2	Develop additional controls over the agency budgeting process to ensure that the required budget approvals are obtained.	NA	We agree. SDDPC has consistently provided its proposed budget to the City Manager (Mayor) on an annual basis. That budget was, in turn, included in the City Manager (Mayor) overall budget proposal submitted to Council. The SDDPC budget was therefore reviewed by Council and was approved as part of the overall City Manager (Mayor) budget. We look forward to working with the City to add controls to this process and ensure that the required approvals are obtained.	Partly Implemented,  City management is currently in the process of developing new governance procedures. Many of these processes will be documented through the Comptroller's Office, as part of the series of Process Narratives they are compiling.

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3	Develop a policy requiring documentation of the Board's evaluation of how the CEO's achievement of goals ties to the bonus awarded.	NA	We agree. The SDDPC Board has been fully, regularly and actively engaged in evaluating the CEO's performance and has established detailed processes as a priority of their board responsibilities. This process has included a great deal of documentation, as described on page 5 of the Audit Report, which the Board has reviewed and verbally addressed when measuring the CEO's performance against the documented goals and objectives. A written matrix was provided and used by each individual Board member as a tool to measure performance. However, the Board did not complete a final consolidated written matrix. SDDPC will develop a Board approved policy along with a consolidated written matrix form which will be required as a part of each Board's evaluation process. This policy and additional documentation will more fully and completely tie the CEO's performance against the goals to any bonuses awarded.	Implemented,  Section 3(b) of the SDDPC Executive Director Selection, Compensation, Performance and Separation Policy clarifies that the CEO will not receive any bonus pay.  "Bonus (includes any and all other merit pay of any kind, other than base salary): There shall exist no other bonus or merit pay."

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4	Document in detail how the bonuses awarded to employees tie specifically to program achievements, processes or contributions.	NA	We agree. SDDPC has already established an amended, Board approved human resources compensation policy on December 11, 2008. The past policy required documentation for bonuses. However, the amended policy adds that more complete and detailed documentation will be required which more fully describes the specific performance, achievement and/or contribution made by that employee.	Implemented,  The bonus pay structure is defined in Chapter II of SDDPC's Policy Handbook, requiring detailed documentation of achievements and defining criteria for the award.
5	Recover from the CEO the \$1,335.62 bonus overpayment.	NA	We agree and this item is completed. Tom Fleming will repay the company by taking a reduction in his paycheck (May 15, 2009) for the amount of \$1,355.62.	Implemented,  The paystub for the pay-period ending May 10 <sup>th</sup> , and issued on May 15 <sup>th</sup> has been provided showing that the overpayment has been repaid to SDDPC.



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6	Ensure Board approval of CEO goals objectives within 60 days as specified in the CEO contract.	NA	We agree. These goals and objectives are first determined by the Board at their annual Strategic Planning meeting with the participation of City IT staff. Once adopted these company goals are then incorporated into the CEO goals and objectives and further incorporated as an amendment to the CEO employment contract. The goals and objectives are reviewed and re-established by the Board on an annual basis. The CEO's employment compensation, yearly bonus and goals and objectives are fully documented in this employment contract. This contract is fully managed by the SDDPC Board and fully transparent as to any and all benefits provided to the CEO. The Board will fully comply with meeting these employment contract requirements within the 60 day limit at the end of each fiscal year.	Implemented,  The goals are defined as stated in the Matrix in Article VIII of the SDDPC Bylaws.

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1	SDDPC's Board should require SDDPC to have written policies related to reimbursements to vendors and the retention of bid documents.	Not incorporated into the MSA	SDDPC will revise policies to address this area upon approval of the MSA.	Not Implemented
2	Design controls to ensure a review of compliance with the Operating Agreement terms is performed annually. Consider requiring SDDPC to self-assess their compliance with the agreement terms and submit the assessment to the Mayor, or designee, for their review prior to executing the annual Service Level Agreement.	Not incorporated into the MSA	Annual reporting requirements contained in Bylaws	Not Implemented,  The Bylaws (Article V, Section 4) describe an annual February meeting/update to the city council. They will provide a summary of the corporation and spells out reporting on Bylaws compliance, but there is no mention of an annual OA/MSA review/report.

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3	Modify the Operating Agreement to establish a process by which payments by the City that exceed costs for services are refunded by SDDPC.	Yes – Section 4.8	Implement mid-year rate adjustment process; eliminated refund process.	Implemented, “After SDDPC has closed its accounting records for that fiscal year, such excess revenues or expenses will be incorporated into a rate adjustment as part of the next Mid-Year Rate Adjustment process, provided there are Available Net Assets as described above.”
4	Modify the Operating Agreement to define costs which are unallowable without a justification of benefit to and approval by the City, including the procurement of capital assets.	Yes, Sections: 3.4.1.4	Information Technology (IT) related capital will be vetted with the Dept of IT during the rate process; non-IT capital items are reviewed by City CFO for input and approved by SDDPC Board; Department of IT will manage annual budget process with SDDPC	Implemented, The MSA addresses IT Capital Assets, while non-IT Capital Assets are addressed in Attachment 3(a), sections 1 and 4.

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5	Consult with the City Attorney to ensure pass-through purchases are properly and clearly authorized by Council as required by the Municipal Code and Charter.	NA	Adopt a City Council policy related to IT Procurement through SDDPC; MSA complies with Municipal Code	Implemented,  Auditee Clarification: The draft City Council Policy on IT Procurement is the recommended method from the City Attorney's Office to best achieve compliance with the legal requirements, plus the inclusion of necessary language in the annual Appropriation Ordinance for IT spend through SDDPC (more specific than the general language used in the past AO). In addition, updated IT governance policies and processes will provide further reviews and approvals to ensure necessary compliance.

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6	The City should ensure the appropriation ordinance language clearly authorizes payments to SDDPC for pass-through expenses.	NA	Adopt a City Council policy related to IT Procurement through SDDPC; MSA complies with Municipal Code	Implemented ,  Auditee Clarification: The draft City Council Policy on IT Procurement is the recommended method from the City Attorney's Office to best achieve compliance with the legal requirements, plus the inclusion of necessary language in the annual Appropriation Ordinance (AO) for IT spend through SDDPC (more specific than the general language used in the past AO). In addition, updated IT governance policies and processes will provide further reviews and approvals to ensure necessary compliance.
7	Amend the Operating Agreement with SDDPC to improve best practices by requiring:			

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a.	<p>A dedicated public vendor webpage for posting:</p> <ul style="list-style-type: none"> <li>▪ Requests for quotes or proposals;</li> <li>▪ Results of requests for quotes or proposals; and</li> <li>▪ Justifications for sole source / sole responder vendor contracts;</li> </ul>	Not incorporated into the MSA	SDDPC will revise policies to address this area upon approval of the MSA.	Not Implemented
b	Standard minimum response times to requests for quotes or proposals;	Not incorporated into the MSA	SDDPC will revise policies to address this area upon approval of the MSA.	Not Implemented

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c	Re-advertising for requests for quotes or proposals if an insufficient number of responses are received from vendors for contracts exceeding a specific value, such as \$250,000 unless sufficient justification is documented, presented to the Board and the justification is posted to the website;	Not incorporated into the MSA	SDDPC will revise policies to address this area upon approval of the MSA.	Not Implemented
d	Fixed terms for contracts; and	Not incorporated into the MSA	SDDPC will revise policies to address this area upon approval of the MSA.	Not Implemented

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e	Annual report to the City summarizing competitive practices.	Not incorporated into the MSA  Covered in Article 5, section 4 of SDDPC’s Bylaws.	Covered in annual meeting requirement outlined in the Bylaws	Implemented,  The MSA has not been amended to include the annual report, however the bylaws have been updated to include specific items to be reported including a summary of competitive practices.
8	City management should consider establishing policies and regulations specific to procurement of long term system maintenance contracts.	NA	No Reference	Not Implemented  Auditee Clarification: This recommendation will be covered in separate City IT governance and IT procurement policies that are not part of this package of documents.
9	The City and SDDPC should develop policies and procedures to ensure compliance with competitive standards applicable to federally funded technology projects.	NA	No Reference	Not Implemented  Auditee Clarification: This recommendation will be addressed by City IT governance policies and SDDPC procurement policies that are not part of this package of documents.



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10	Add language to the City’s Purchasing and Contracting Department website directing vendors to SDDPC web site for technology procurement opportunities.	NA	No Reference	Implemented,  Auditee Clarification: This recommendation has been completed by the addition of a statement on the City Purchasing “Bid & Contract Opportunities” web page under the sub-category listing for “Computer/Data Systems Related” ( <a href="http://apps.sandiego.gov/bcweb/setupSubCatList.do?subCatDesc=Computer%2FData+Systems+Related&amp;subCatCd=1&amp;catCd=1">http://apps.sandiego.gov/bcweb/setupSubCatList.do?subCatDesc=Computer%2FData+Systems+Related&amp;subCatCd=1&amp;catCd=1</a> ).

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11	<p>Either SDDPC should permit view access by City employees to their contract, invoice, and vendor payment history for procured goods and services in order to verify the accuracy of SDDPC billings, or the procurement of these goods and services should be made directly through the City's procurement process in consultation with SDDPC staff. The selected process should ensure the best operational efficiencies for the City that incorporates strong internal controls.</p>	NA	No Reference	<p>Not Implemented,</p> <p>Auditee Clarification: This recommendation may become part of the amended SLA, which won't be completed until after the approval of the MSA; or it may be addressed through other policies that are not part of this package of documents. The City and SDDPC are still in discussion on how this will be addressed.</p>

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12	The City should establish encumbrances for the Information Technology Business Leadership Group's (ITBLG) approved new project costs procured through SDDPC to ensure actual costs do not exceed approved budgeted costs.	NA	City IT governance and City processes will provide controls; project managers are responsible for proper monitoring and managing costs; monthly or quarterly reports provided to City IT BLG	Partly Implemented,  Auditee Clarification: The IT BLG working with the Dept of IT have been developing new governance procedures for review and approval of IT projects and procurement. Those processes will be documented through the Comptroller's Office, Internal Controls Section, as part of the series of Process Narratives they are compiling. Some of the policies and procedures relate to current business practices that needed to be better documented or updated and others that are new processes. The final IT-related Process Narratives (with related Workflows) will be part of the package presented to the Audit Committee by the Comptroller.

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13	<p>Consult with the City Attorney and amend the Operating Agreement to a more traditional professional services contract to provide the City with specific IT services and as-needed services. The agreement should have a fixed term and incorporate appropriate levels of approval at the City prior to SDDPC processing a request for services.</p>	<p>Yes, MSA Sections 2.2 and 6.1</p>	<p>NA</p>	<p>Implemented,</p> <p>Section 2.2 of the MSA defines the responsibilities and process for Review and Approval of Information Technology Services.</p> <p>Section 6.1 defines the Term of the MSA to be one year from the approval date, and automatically renews for two additional years unless terminated (180 day notification prior to renewal).</p>

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14	Amend the Operating Agreement to establish a timeline for execution of the annual SLA and to establish the level of City approval required prior to making payments if an SLA is not executed within the timeframe.	Yes, MSA Section 3.2	MSA, amended SLA, and SDDPC Budget & Fiscal policy implement these comments	Implemented,  Section 3.2.1 of the MSA requires that the SLA be approved no later than July 1 <sup>st</sup> of each year. In the case where the SLA is not approved, a temporary “memorandum of agreement which will state the hourly rates and fixed cost allocations that will be paid” will be executed until the SLA is approved.
15	City management, in consultation with the City Attorney, should advise the City Council to consider amending SDDPC’s bylaws to include the following:			

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a	The Mayor and City Council shall approve the hiring of the CEO and the CEO's contract terms;	NA	<p>Implement strict selection &amp; performance policy, place cap on compensation, and eliminate bonus; range of \$180K to \$225K (cap); based on other City agency CEOs</p> <p>SDDPC Executive Director hired/fired by SDDPC Board, with input from Mayor and Council</p> <p>Create SDDPC Audit Committee consistent with SEDC/CCDC</p>	<p>Not Implemented,</p> <p>The Bylaws do not require approval only input from the Mayor and City Council</p>

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b	The Board shall approve the compensation of the CFO unless increases in compensation are applicable to all employees;	NA	Amended Bylaws implement these comments	Implemented,  Addressed in Article 7, section 3 of the Bylaws which states: The compensation, if any, of the Officers, shall be fixed or determined by resolution of the Board, except that the compensation for the President shall be determined as set forth in Article VIII, Section 1(a) of these Bylaws.
c	The CEO shall provide an annual report to the Mayor and City Council on SDDPC’s compliance with its Bylaw requirements;	NA	Amended Bylaws include this provision for the Executive Director	Implemented,  Article 5, section 4 of SDDPC’s Bylaws requires “a summary of Bylaws compliance during the preceding Fiscal Year” among other key items reported.

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d	SDDPC shall provide to the Mayor and City Council an annual report on its performance, including its strategy, current year’s goals, status of major projects, and comparison of prior year’s goals to performance; and	NA	Amended Bylaws and policies include these provisions	Implemented,  Article 5, section 4 of SDDPC’s Bylaws states “an annual report of the Corporation which shall provide an assessment of the Corporation and describe its operations and financial outlook and include a copy of its Strategic Plan for its past and present Fiscal Year as provided for in Article VII of these Bylaws, and such other issues related to technology, fiscal outlook and operations, the status of major projects”...
e	SDDPC’s CEO and CFO shall certify to the City that SDDPC management assumes full responsibility for the completeness and reliability of the information contained in the financial report.	Yes, MSA section 4.4	Bylaws, MSA and SDDPC Budget & Fiscal policy implement these comments	Implemented,  The MSA, Section 4.4, requires the SDDPC CEO & CFO to assume responsibility for the financial report.



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16	City management, in consultation with the City Attorney, should advise the City Council on the appropriate action to be taken regarding delegation of member rights.	NA	Amended Bylaws address this area	Implemented,  Article 5, Section 2 of the Bylaws addresses the appointing of a “Designee” by the Council of the City of San Diego (“City Council”).