



Executive Summary

Based on the findings and recommendations of a report from the San Mateo Civil Grand Jury, the City of Burlingame contracted with DKG Consultants (DKG) to assess its internal controls and overall risk environment. Overall, the results of the assessment demonstrated Burlingame has strong internal controls and staff that is generally well-trained and aware of related best practices. There were a number of recommendations for consideration for the City to strengthen overall controls, which are discussed in detail throughout the report. A risk assessment framework was also developed for consideration to manage and mitigate financial risk on an ongoing basis.

Methodology

The first step in the assessment process was a review of the Memorandum on Internal Controls and Required Communications, both of which are provided by the external auditor to the City's management, including the City Council. These documents were reviewed for fiscal years 2019-20 through 2023-24. There were no issues or concerns noted with respect to the City's internal controls that were identified by the external auditors in either the Memorandum on Internal Controls or Required Communications.

The next step was a series of interviews with staff in the Finance Department and in the operating departments to assess policies, processes, procedures, documentation, and controls as it relates to the functional areas of:

- Accounts payable
- Revenue management
- Utility billing
- Cash handling
- Payroll
- Procurement and credit cards
- Financial system access
- Budgetary appropriation control

After all interviews, including any necessary follow-ups, concluded, the overall risk assessment and framework were developed and summarized in the subsequent sections of this report.

Operational Summary and Areas of Identified Risk

Accounts Payable – The City's accounts payable function (AP) is decentralized, with departments responsible for receiving goods and services, reviewing and confirming invoices, and entering payment request information into the Tyler financial system (Munis). The Finance Department reviews information provided, confirms adequacy, and issues payments as appropriate. AP staff in Finance effectively serve as the gatekeeper, ensuring compliance with the purchasing policy and that proper payment authorization documentation has been received, and that a purchase order has been established, if appropriate. This includes confirmation of compliance with the travel and employee reimbursement policies. One of the

Financial Services Managers reviews and confirms payments over \$5,000. Overall, the systems, procedures, and processes within Finance and throughout the departments provide strong assurance that the City is accurately paying its vendors for goods and services received and that City policies related to travel and employee reimbursements are being followed. Key aspects of the City's accounts payable operation that support strong internal controls and risk mitigation include:

1. Vendor set up is accomplished by the same person that manages the actual disbursements; however, there are two controls in place to mitigate potential issues:
 - a. The vendor is not active, and thus cannot receive payment, until a Senior Accountant reviews and approves the vendor set up. The system does not allow the AP staff to override or otherwise work around this approval.
 - b. Payments are not finalized and checks are not run until the Financial Services Manager reviews the warrant list and approves payment.
2. Purchase orders are required for single purchases greater than \$5,000, which helps ensure goods/services have been previously approved for purchase. Additionally, payment requests greater than \$5,000 that are on purchase orders are routed to the Finance Director or Financial Services Manager for review/approval prior to moving to AP for final processing.
3. There are no ACH payments to vendors, which is an increasing source of fraudulent activity.
4. While the AP process is decentralized, the Finance Department confirms that contracts submitted have been approved at the appropriate signature level, that the appropriate competitive process has been followed, that all documentation is in order, and that the vendor has a business license.
5. For smaller purchases that fall below the purchase order limit but are sensitive, such as employee reimbursements and travel, AP staff confirm policy compliance prior to final processing.

The one area of risk management that the City should consider is related to changes to vendor files. AP staff are aware that changes to vendor information require confirmation to avoid fraudulent requests, which is an increasing concern for any entity making payments to vendors; however, the process for verification is not documented. Developing a robust verification process, including addressing changes for vendors who receive ACH payments (should that become more prevalent in the future), and documenting and training on that process is recommended.

Revenue Management – The core revenue management function is managed centrally within the Finance Department; however, departments that have revenue-generating operations have a role in revenue management. The two departments that bring in significant revenue outside of the Finance Department are Community Development and Recreation. In both cases, revenue is received through cash, check, and credit card and is managed at the department level through their respective operational software. In each case, revenues are recorded in these systems, with reports generated daily (in most cases) and provided to Finance along with cash and checks received. Finance reconciles the cash, checks, and credit card information with the reports provided, and once any discrepancies are addressed, records the transaction in Munis.

Both Community Development and Recreation have controls to mitigate risk with respect to services being provided without revenue being received. In Community Development, final permits and/or the certificate of occupancy is not issued unless any outstanding permit fee balances have been paid. In Recreation, it is possible for a contract instructor to accept payment outside of the purview of the City,

which would result in the City not receiving its 30% to 40% share of the revenue from that participant. To mitigate this, Recreation performs checks of registrations against actual attendance on occasion or if an issue is suspected. This is more prevalent in classes outside of the Recreation Center, where participants must pass by the front counter and allows for additional tracking. It is recommended that Recreation do more frequent and scheduled reviews of registration lists against actual attendance to ensure revenue received is aligned with registration numbers.

Within the Finance Department, revenue management activity includes receiving, reconciling, and recording citywide revenues such as tax revenues. In some cases, like for business license taxes and transient occupancy taxes, a third-party collects (and bills, as appropriate) on behalf of the City. All revenues are reconciled to formal documentation, such as property tax remittances from the County, and recorded appropriately. The Finance Department bills directly for a number of services rendered such as false alarm response, crossing guards, and sewer treatment. Receivables are monitored regularly as a part of standard operations, with follow-ups and referrals to collections as needed to ensure payments due are received.

Utility Billing – The City operates and maintains its own drinking water distribution system, and the Finance Department manages the billing process for the nearly 11,000 customer accounts. Customers are billed every other month for services. There are three employees who have responsibilities for billing the water customers, the Customer Services Supervisor, the Accounting Technician III, and the Accounting Assistant I. Roles and responsibilities amongst the three appear well-defined and appropriate checks and balances are in place in an effort to be proactive with ensuring customers are billed correctly. This includes both the Customer Services Supervisor and Accounting Technician III reviewing the meter reading file to look for usage anomalies that would warrant further investigation by a meter reader. Various members of this group are also responsible for end-of-month reconciliation between billings versus water utilization; review of closed accounts and issuances of refunds for credit balances; delinquency notifications, with a focus on continuous service provision; construction meter deposits; processing daily meter read data into Munis; and processing new applications for services.

Risks related to the utility billing operations mostly relate to customers not being properly billed for services, and overall, the operation has a number of mechanisms in place to ensure proper billing of customers. When issues do arise, there are also mechanisms in place to ensure they are identified in a timely manner so that they can be addressed. There are two areas of concern with this operation stemming from the interviews:

1. Meter read information is provided from the meter readers to Finance staff via a flash drive that is exchanged daily. This is not an efficient process, and it also creates risk with respect to the loss of the flash drive. Developing a mechanism that would allow for an automatic load of meter reading data to either a shared drive/cloud solution or directly to the Census system is recommended as resources allow.
2. Staff consistently indicated that Munis has some deficiencies that resulted in the need for manual workarounds. This includes reported issues with delinquency reporting and other reports/controls. The City should continue to work with Tyler on addressing these issues and improving the functionality of the system for utility billing purposes.

Cash Handling – While the prevalence of non-cash payments has increased over the years, the City still takes in cash for various services. Cash transactions increase the risk of mistakes or fraud, and therefore it is imperative that the City have appropriate systems, procedures, and processes in place to prevent cash-related fraud. Overall, the City has good systems in place to prevent cash-related fraud, including:

1. Daily cash reconciliation in the Finance Department, with \$600 kept on site and the remainder sent to the bank.
2. Cash transactions at the Finance counter involve two receipts and the transaction is entered into the financial system. Any cash transaction over \$200 requires two signatures, and a transaction not entered into the system (for instance if an employee kept the cash), would result in the customer's payment balance not being credited, which would eventually be captured.
3. Finance centrally receives cash from the departments. Recreation, the source of the most significant amount of cash received, has a registration system that provides reports on transaction data that is used by Finance to reconcile prior to entering into Munis.
4. Another division in Finance, the group responsible for the general ledger, performs an additional reconciliation as a part of their standard close process.
5. Recreation has good cash handling procedures with limited access to the safe, which is in a locked office, and more than one person involved in cash counting and reconciliation. As noted, Recreation is also taking in much less cash than it has in previous years, mitigating cash-related risk and exposure.
 - a. The Library, which takes in a relatively small amount of cash, was advised during its interview to add a second person to its cash counting procedure to align with best practices.

Payroll – The City manages the payroll function internally, utilizing City staff to process employee paychecks and direct deposits through the Munis system. Payroll is processed on a bi-weekly basis and pay is issued to between 300 and 350 employees every other week. The variance is the result of seasonal employees related to summer recreation programs. Roles and responsibilities within the payroll function are well defined and documented, as are the internal controls. With payroll constituting such a substantial portion of the City's General Fund budget, ensuring the integrity of the payroll process through strong internal controls is imperative. The following are some of the key internal controls required for a best practice-based payroll process, as well as an assessment of the City's level of compliance.

1. Separation of Duties: To ensure the integrity of the process, it is important that duties are structured such that the person who is responsible for processing payroll is also not the person responsible for the entry of pay and benefits information into system. The City has the appropriate separation of duties in place, as Human Resources staff are responsible for direct data entry into the system, with Payroll staff making limited changes that are documented and subject to review and approval.
2. Oversight and Approvals: The separation of duties is only effective if there is oversight and approval of changes that are made. Otherwise, one person could have the opportunity to make changes to employee pay and benefits without proper authorization. The City has best practice approvals in place related to Finance and HR processes, with HR making changes only based on approved documentation, such as Personnel Action Forms (PAF), and Payroll checking and reconciling changes in pay and benefits based on PAFs. This reconciliation occurs through a review of a report pulled from the Munis system against the PAFs.
3. Overtime: Overtime outside the Police Department and the maintenance operations in Public Works/Parks is limited based on the interviews with the other departments. Both Police and Public

Works/Parks have scheduled and operational need-based overtime. Scheduled overtime is driven by MOU and policies, and the timecard reflects overtime that matches what is scheduled. In the Police Department, operational need-based overtime is tracked and verified through a supervisor's overtime log, the officer's paper log, and the time input in Munis. Overtime is also centrally reviewed within the department, with administrative staff checking Munis against the manual logs. In Public Works, overtime slips are used and are matched by the supervisor to the time entry in Munis.

4. **System Functionality and Access:** The payroll module of the Munis system has a number of features that support best practices and limit data entry related to pay. For instance, the pay range for each position is listed in a salary table that is loaded into Munis. Each position has a specific job code, and a job code is attached to each employee. This prevents pay rates from being manually manipulated or other errors that could occur if pay rates were attached directly to individual employees. Munis also has basic controls that prevent things like more work hours being entered for a day than there are hours in the day. In terms of system access, there are access profiles in Munis that only allow the access that is needed for employees to perform their respective functions.
5. **Post-Payroll Processing Review:** Munis has a feature that automatically posts payroll to the general ledger, which effectively completes the payroll process. In addition to paying employees and administering employee benefits, the payroll process also administers payments to outside entities for related obligations like taxes, pension, healthcare, union dues, etc. As a part of the final stage of the payroll process in Munis, a batch of invoices for these payments is created and payments are made. Some of these payments are made via Accounts Payable, and others are made directly through online portals. All payments made through this process are reviewed for appropriateness by managers in the Finance Department.

The overall risk and controls environment in the payroll function is sound and there are no major concerns to report. Below are a few recommendations for the City's consideration:

1. Each department should have policies and procedures related to overtime that are operationally feasible and allow for appropriate oversight and approvals.
2. Expectations of supervisors related to the approval of payroll, including overtime, should be emphasized as a part of regular training. Payroll accuracy relies on supervisors reviewing timecards for accuracy and alignment with department policy. If reviews and approvals are cursory in nature, the other payroll controls become less useful.

Procurement and Credit Cards – The City maintains a detailed Purchasing and Contracting Procedures Policy (Policy) that covers all aspects of procurement, including purchasing authority levels, competitive requirements, payment procedures, credit card utilization, expense reimbursements, and emergency purchasing. The policy was last updated in late 2022. With a decentralized procurement process that relies on the individual departments and the Finance Department to ensure policy compliance, the policy document, departmental procedures, Finance procedures, and system controls are all necessary components to mitigate risk. Overall, these functions appear to be working well to mitigate risk related to fraud in the procurement process, with one exception. Best practice related to the purchase of goods is for the person ordering the goods to not be the same person receiving the goods. This separation of duties is a key fraud prevention mechanism to ensure goods ordered are properly received, necessary for the operation, and are available for utilization. In the Public Works maintenance operation, to name one, the person buying goods is the same person receiving the goods. While the invoice is ultimately approved by

someone else, that approver is not able to confirm all purchased goods were received and put into operation. If administratively feasible, assigning someone other than the buyer to receive the goods and confirm the contents against the order would provide better risk mitigation. If not, this risk should be identified as a part of ongoing training to ensure approvers are aware that this condition exists.

Otherwise, the procurement-related risks are more a function of compliance with the Purchasing and Contracting Procedures Policy. Interviews with the employees involved in this process indicate that employees are aware of and are attempting to follow the Policy. There are aspects of the Policy, however, that could be refined to better clarify Policy intent and facilitate better compliance. It is important to note that these aspects of the Policy as currently written do not represent material risk of fraud.

1. Section A- 1: Dollar Limits – Based on the interviews, the departments are aware of and attempt to comply with the requirements of two verbal quotations (\$5,001 to \$10,000) and three written quotations (\$10,001 to \$25,000). While the departments attempt to get the quotations, they are not always successful. This is documented when the purchase order is being requested; however, this section of the Policy could be revised to indicate the department should solicit the quotations, with the purchase order request including the solicitation information if the required number of quotations is not received.
2. Section B-7: Open Purchase Order/Blanket Purchase Order – This section appears to appropriately address a common issue in procurement, which is a series of relatively small purchases with the same vendor that do not involve a competitive process but in aggregate exceed thresholds for requiring competitive processes and potentially the City Manager’s approval authority. Revising this section (or adding a section elsewhere in the document) to clearly define what constitutes a single purchase and what should be effectively considered an open purchase order is recommended.
 - a. A specific area that should be reviewed is with the Library’s utilization of Baker and Taylor to procure materials. Over the course of the year, the Library procures a considerable number of materials through Baker and Taylor without utilizing a competitive process or considering the aggregate amount spent in relation to approval authority. This practice has been in place for a number of years, and changes should be considered to improve policy compliance. Providing Council-approved delegated authority to the Library to continue this practice is an option for the City’s consideration.
3. Section B-3: Specialized Professional Services – This section excludes specialized professional services, including specialized recreational services, from competitive requirements. This exception is footnoted with a reference to California Government Code Section 4526. This section of the code allows for the selection of specific professional services (private architectural, landscape architectural, engineering, environmental, land surveying, or construction project management) to be based on demonstrated competence. Based on the interviews with the departments, there are cases where this exception is used for professional services that are outside of the scope defined in California Government Code Section 4526. If the City intends to allow all professional services to be procured based on demonstrated competence, it should consider removing this reference to the code.

Financial System Access – Best practice for access to Munis is for access rights to be maintained centrally, which is achieved through management by the Finance Department, and for individual access to be limited based on need. Access profiles have been developed to provide need-based access to various individuals

throughout the organization based on their role. Changes in access rights are handled by the Financial Services Manager, and new employees are assigned the rights of their predecessor by default.

The City's oversight and management of access to Munis is solid; however, an audit of access rights to ensure consistency across positions and that rights granted are appropriate based on job responsibilities should be considered as resources permit. Documenting standard access profiles by job function should be included as a part of this initiative.

Budgetary Appropriation Control

Per the ACFR, the City's budgetary appropriation control is as follows:

- Budget amendments that increase a fund's total appropriation require Council approval.
- Certain budgetary re-allocations within departments require approval by the Finance Director and department heads.
- Budget amendments between departments are approved by the Finance Director and City Manager.

Based on the existing policy, there is broad authority to administratively reallocate funds as long as the total fund appropriation is not increased. In that case, Council approval is required. As a result, if total general fund operating costs are within the Council-approved appropriation, the policy parameters are being met, even if one or more departments exceeds their operating budget. The exercise of moving funds from one departmental budget to another to keep each department within its appropriation is simply an administrative exercise. In practice, it appears that the City does not make these administrative adjustments to ensure all departments are within their appropriation, as evidenced by the budget to actual schedule in the fiscal year 2022-23 ACFR.

Departmental interviews indicated good awareness of budgetary controls and monitoring practices, as well as the utilization of the mid-year budget process to address unknown issues that arise during the fiscal year. Departments also were aware that line-item budget controls were not in place, as they were managing to the bottom line of their departmental appropriation.

The City's main budgetary control, the requirement that budget amendments that increase a fund's total appropriation be approved by Council, is a common budgetary control and helps ensure that total fund spending remains within appropriations. In many cities, the main budgetary control is at the fund level and the department level, meaning a department-level appropriation within a fund cannot be increased without Council approval. This creates direct accountability at the department level.

Burlingame's current budgetary control policy does not create any additional overall risk, as the fund appropriation set by Council cannot be increased without their approval. If there were a greater desire to have better department-level controls in place, the policy could be amended to require departmental budgets within each fund not be increased without Council authority. Otherwise, this can be an expectation set by the City Manager and does not necessarily need to be a change to the policy.

Risk Mitigation Recommendations

A summary of the risk-mitigation recommendations that were covered previously is below:

1. Document the process for changes to vendor files that includes appropriate verification of the change (Finance).
2. Conduct regular spot-audits of contractor-led classes and camps to ensure alignment between participant registrations and participant attendance (Parks and Recreation).
3. Explore a more automatic process for sharing meter read information as opposed to conducting a daily exchange of a flash drive (Finance).
4. Continue to work with Tyler on improvements to reporting and other functionality in Munis (Finance).
5. Develop department-level policies and procedures related to overtime (Departments).
6. Evaluate the feasibility of separating the purchasing and receiving functions, particularly in operational areas with a higher risk for issues (Departments).
7. Amend the Purchasing Policy to align the language in the policy with current practices (Finance).
8. Conduct an audit of Munis access rights and document standard access profiles by job function (Finance).

Enterprise Risk Assessment Framework

In addition to addressing the above recommendations, as well as to be compliant with the recommendations of the Grand Jury report, the City should implement a risk assessment framework that ensures consistent management, monitoring, and reporting of internal controls. A proposed framework follows that aligns with the principles of the Green Book, which is the standard for internal controls in the Federal Government, as issued by the General Accounting Office. These principles identify five components of an effective internal control system, which are the basis for the proposed framework.

1. Control Environment – This component considers the commitment of the organization to integrity and ethical values, which is established by management and effectuated throughout the organization. To maintain the strong existing controls environment, the City should consider the following:
 - a. Develop and implement a mandatory training as a part of the new-hire training process that reviews the internal controls framework and educates on key internal control practices within the City (as identified throughout this report). For administrative efficiency, this training could be a narrated PowerPoint that employees take at their convenience within a certain time from being hired.
 - b. Add a component to the objectives identified in the employee performance review that encompasses performance against internal controls responsibilities. This does not need to be a separate component of the review and can instead be one component of overall performance standards.
2. Risk Assessment – This component ensures that management effectively identifies and analyzes risk, determines its level of risk tolerance, and mitigates identified risk accordingly. Based on the City's existing controls environment and the risks identified from this analysis, the City should consider the following:
 - a. Document its response, and actions as appropriate, to the nine areas of risk identified as a part of this analysis.
 - b. Create an annual assessment of areas of risk that focuses on:
 - i. Any changes to processes, procedures, or policies that impact existing areas where controls are in place.

- ii. Any new processes, procedures, or policies that introduce new areas of risk.
 - iii. Any changes to key personnel involved in internal controls that require process changes or training.
- 3. Control Activities – This component focuses on the activities the entity puts in place to mitigate risk as identified in the risk assessment. The City already has well-established control activities, so moving forward, the focus for new control activities would be a function of any new controls put in place as a result of this assessment or through the annual risk assessment.
- 4. Information and Communication – This component emphasizes the need for quality information to achieve the entity’s objectives and the need to communicate that information internally and externally. The City’s existing information systems are strong and support a robust internal controls environment, as evidenced by historical results of external audits (unmodified audit opinions, no issues reported on the Memorandum on Internal Controls or Required Communications). Going forward, the City should consider:
 - a. Incorporating a summary of its annual risk assessment and any resulting changes to control activities in its report to Council where the Annual Comprehensive Financial Report is shared.
- 5. Monitoring – This component focuses on ensuring internal controls systems are monitored, evaluated, and remediated, as needed, on a timely basis. Implementing the considerations identified in the prior components will effectively address the monitoring component.