

**2021 – 2022 KERN COUNTY GRAND JURY**

**CITY OF BAKERSFIELD**

*Erroneous IRS Filings*

**December 2, 2021**



# **CITY OF BAKERSFIELD**

## ***ERRONEOUS IRS FILINGS***

### **SUMMARY:**

In March 2021, the City of Bakersfield (City) was alerted to erroneous Form 1099-R filings that were transmitted to the Internal Revenue Service (IRS) regarding pension distribution income for current and former employees. Upon becoming aware of this, the City retained outside counsel to work with the IRS to determine the extent of this error and the source of the data filings. An email was sent to all current employees to look for notices from the IRS and contact the City if anything was received. Retirees were not informed until four months later. Subsequently, the City sent corrected 1099-R forms to approximately 1,800 employees and retirees.

The question before the Grand Jury and the public, at this time is...was this an erroneous IRS filing or a data breach?

### **PURPOSE OF INQUIRY:**

The 2021-2022 Kern County Grand Jury (Grand Jury) received a complaint from a concerned City resident regarding the 1099-R notices and the manner in which the City handled these erroneous filings. Pursuant to California Penal Code sub section (§) 925a, the Grand Jury conducted an inquiry.

### **METHODOLOGY:**

The Grand Jury interviewed City officials and affected current and retired City employees. City emails and correspondence to employees and retirees were also reviewed. Additionally, the Grand Jury conducted internet research regarding Kern County data breaches and erroneous IRS filings.

### **DISCUSSION OF FACTS:**

In March 2021, several current and former City employees informed the City Finance Department they received notices from the IRS that they owed taxes on their 2019 tax filings. These notifications stated that the 1099-R forms, filed by the City with the IRS in April 2020, had not been declared on their personal taxes. (See Appendix A)

Since March 2021, the City hired an outside attorney to assist in resolving this error. The City then sent corrected 1099-R forms to the IRS with copies sent to each employee and retiree. (See Appendix B)

The Grand Jury noted the following:

- A. In March 2021, all current City employees were informed of the erroneous filing via interoffice email; however, retirees were not informed until July 21, 2021, via US mail. (See Appendix C)
- B. The City's tax identification number, which is public information, was used in the erroneous filings.
- C. City employee/retiree social security and/or tax identification numbers were accessed and used in the erroneous filings in spite of the fact they are not public information.
- D. The erroneous filings were created using 2016 employee tax data.
- E. As of September 30, 2021, IRS notices were still being received by employees and retirees.
- F. The traditional IRS 1099 Form reports income other than the IRS W-2 Form. The 1099-R is income of retirees. Normally, current City employees do not receive 1099-R Forms:
  - The California Public Employees Retirement System (CalPERS) normally issues 1099-R Forms to City retirees.
  - Beginning in March 2021, current and retired City employees received IRS Notices regarding 1099-R erroneous filings.
  - Not realizing they had the capability to create 1099-R forms and in an effort to help correct the error, City Officials stated they had to procure a software program to create corrected 1099-R forms. These were then sent to the IRS and employees/retirees.
- G. City Officials state that, eventually, an in-depth analysis by the City's software provider revealed that, indeed, the erroneous filing was caused by human error on the part of City employees. City Officials provided a synopsis of the error:

*Recently our outside counsel, retained to look into the 1099-R filing for 2019, was able to receive additional information from the IRS that confirmed that the file submitted was in fact sent to the IRS in January 2020 by the City. This was the first definitive statement we were able to receive from that agency on that particular aspect of the matter since we became aware of the problem. This of course prompted staff to delve deeper into these reports and we were able to confirm that the source of these 1099s was through our Central Square software system and uploaded to the IRS by City staff.*
- H. The City does not consider this a data breach.

- I. Initially, City Officials reported that they could not generate and/or issue 1099-R forms. Then, the above mentioned synopsis revealed that, indeed, the City can produce them:

*...As a reminder, initial discussions with their support staff months ago was that the system would not have generated a 1099-R because it was not configured to do so. That statement has proved to be incorrect or at the least misinterpreted. We have now been told a 1099-R could be generated in error and the system would pull YTD (year to date) wage info (information), reporting that as a pension distribution. That is despite the fact that the City does not distribute retirement payments and the system is not configured to track pension costs. With that, we now know that a file was created erroneously by staff as finance prepared the tax filings required for City vendor payments (1099-MISC). That data was included in electronic data file submitted by Technology Services to the IRS early in 2020. When no employee or retiree included that reported income, it prompted the numerous IRS notices we have seen in 2021.*

The above mentions synopsis further states...*Moving forward Finance and TS staff will update procedures for 1099 filings to prevent this type of error in the future. This will include confirming with the finance staff that the data filed pulled from the server contains the correct number of records, agreeing to the 1099 file staff had been working from and performing spot checks to that data before submitting the records to the IRS.*

- J. This erroneous filing error has cost the City in terms of outside attorney fees, staffing hours, and employee/retiree worry and anguish. The City synopsis continues:

*This 1099-R issue has taken an extensive amount of time and resources from staff and our departments and caused unnecessary concern among both current employees and retirees of the city. Design deficiencies within the ERP allowed a file to be created that reported pension distributions when no such data even existed. In addition, slow responses from the IRS and misinformation from our software provider have exacerbated the problem. That does not take away the fact that employees made a string of errors that ultimately lead to erroneous information to be reported to the IRS.*

- K. To the best of their ability, the City has extended support to their employees/retirees in spite of the fact the problem has been largely exacerbated by the software issues:

*...The City will continue to offer support and resources to impacted employees and retirees to ensure that they do not face undue harm financially as a result of this error.*

- L. The City conducts independent audits of its Technology Services (TS) system every two years.

- M. The City TS Department currently has a staffing level of 58—up from a low of 37. According to City Officials:
- Ideally, the Department should be staffed at 100.
  - It is difficult to recruit and retain qualified personnel when the private sector pays substantially more.
  - With the current staffing level, the Department only maintains the City’s TS system and has no staff devoted to improvement or innovation. Per the City...the *current ERP needs to be updated to build a more robust and modern financial reporting system. The financial commitment required for that has already begun with \$6 Million dollars currently budgeted towards a project that can ultimately be in excess of \$20 million dollars. The City is also in the process of finalizing a Request For Proposal (RFP) with an outside consultant that is scheduled to be released in November.*
- N. The term *breach* under California Civil Code §1798.29 is defined as an unauthorized acquisition of computerized data that compromises the security, confidentiality or integrity of personal information maintained by the person or business. (See Appendix D)
- O. California Civil Code §1798.29(f) also states that if the data breaches affects more than 500 persons, they must be notified immediately and a report must be submitted to the California Attorney General’s office.
- P. The City hired an outside attorney who specializes in IRS tax matters. Authorization by the Bakersfield City Council was not required because billing records indicate the cost was below \$40,000.
- Q. Previously in another system the City uses to process billing, the City suffered data breaches between August 11, 2018 and October 1, 2018; and between July 30, 2019 and September 5, 2019.
- R. As of October 2021, the City does not have written policies and procedures for dealing with TS data breaches, internet security issues, and erroneous IRS filings. The City does not have a written policy that mandates the immediate notification of employees and retirees that are or may be affected by data breaches and erroneous filings.

## **FINDINGS:**

- F1. The City initially did not realize the magnitude of the erroneous filings until numerous employees and retirees informed them of the problem.
- F2. According to California Civil Code, §1798.29, a data breach did not occur.

- F3. The City's response to the erroneous filing has been adequate, although they should have informed the retirees sooner.
- F4. Because retirees were not informed until four months later, this put them at risk of unnecessarily paying extra taxes, not to mention the risk of identity theft. This is unsettling.
- F5. It is further troubling that the infrastructure of a city as large and prosperous as Bakersfield did not discover the internal source of the error for eight months.
- F6. It is inconceivable that in this age of cybercrime, the City does not have written Policies and Procedures for dealing with data breaches and possible ransomware. A Policies and Procedures Manual will define and mandate the actions to deal with breaches and other information issues regarding sensitive information such as salaries, employee/retiree data.
- F7. It appears the City's TS Department is understaffed, to adequately deal with the current onslaught of cybercrime. This places the City in jeopardy of further information breaches.
- F8. Current City Finance and TS staff are in dire need of ongoing in-service training on quality control issues regarding the current TS system in use.

## **COMMENTS:**

The Grand Jury would like to thank the City of Bakersfield for their participation, cooperation and assistance in being available for interviews and providing information for this report.

## **RECOMMENDATIONS:**

- R1. The TS and Finance departments should generate a written Policies and Procedures Manual, by the end of the current fiscal year, which mandates the immediate notification of all employees and retirees of any data breach or erroneous IRS filing. (Finding 6)
- R2. The TS and Finance departments should create a written Policies and Procedures Manual, by the end of the current fiscal year; one that defines and mandates action necessary to deal with potential data breaches, malware and ransomware information issues. (Finding 6)
- R3. Within the next three months, devote funding to recruit and retain qualified Technology Services staff. (Finding 7)
- R4. Within the next three months, provide training to TS and Finance staff to deal with the inadequacies of the current information data system. (Finding 8)

R5. Make it a priority to complete the Request For Proposal (RFP) process and implementation of an updated software system. (Finding 8)

**NOTES:**

- The City of Bakersfield should post a copy of this report where it will be available for public review.
- Persons wishing to receive an email notification of newly released reports may sign up at: [www.kerncounty.com/grandjury](http://www.kerncounty.com/grandjury)
- Present and past Kern County Grand Jury Final Reports and Responses can be accessed on the Kern County Grand Jury website: [www.kerncounty.com/grandjury](http://www.kerncounty.com/grandjury)

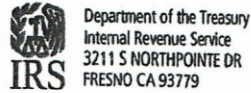
**RESPONSE DEADLINES:**

- **REQUIRED WITHIN 90 DAYS FROM:**
- **PRESIDING JUDGE  
KERN COUNTY SUPERIOR COURT  
1415 TRUXTUN AVENUE, SUITE 212  
BAKERSFIELD, CA 93301**
- **FOREPERSON  
KERN COUNTY GRAND JURY  
1415 TRUXTUN AVENUE, SUITE 600  
BAKERSFIELD, CA 93301**

Reports issued by the Grand Jury do not identify individuals interviewed. Cal. Penal Code § 929 requires that reports of the Grand Jury not contain the name of any person or facts leading to the identity of any person who provides information to the Grand Jury.
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# Appendix A:



notice CP200v  
Tax year 2019  
Notice date August 30, 2021  
Social Security number  
AUR control number 50022-6352  
To contact us Phone 1-800-829-8310 Fax 1-877-477-0962  
Page 1 of 9

014049

We are proposing changes to your 2019 Form 1040 tax return. This is not a bill.

## Proposed amount due: \$16,910

We received information from third parties such as employers or financial institutions that doesn't match the information you reported on your tax return. This notice:

- Proposes a change to tax and/or payments and credits (such as federal income tax withheld, earned income credit, etc.) that you originally reported.
  - Provides you with an opportunity to agree or disagree with the proposed changes.
- If our information is correct, you will owe \$16,910 (including interest), which you need to pay by September 29, 2021.

### What you need to do immediately

If you need more time to respond to this notice, contact us at 1-800-829-8310. Interest will continue to accrue during this period if the information in this notice is correct.

### Summary of proposed changes

Tax you owe	\$13,591
Payments	\$0
Substantial tax understatement penalty	\$2,718
Interest	\$601
<b>Proposed amount due by September 29, 2021</b>	<b>\$16,910</b>

Reminder: This is not a bill. We haven't charged the proposed amount due.

Review this notice, and compare our changes to the information on your 2019 tax return.

#### If you agree with the proposed changes

- Complete, sign, and date the Response form on Page 7 (we require both spouses' signatures if you filed married filing jointly), and mail it to us along with your payment of \$16,910 so we receive it by September 29, 2021.
- Do not file an amended return (Form 1040X) if you fully agree with our changes. We'll make the correction when we receive your signed response.

#### If you don't agree with the proposed changes

- Complete the Response form on Page 7, and send it to us along with a signed statement explaining your disagreement and include any documentation that supports your claim so we receive it by September 29, 2021.
- If you have allowable costs or expenses related to the unreported income that will change our proposal, it may benefit you to include the applicable form or schedule with your response.

Continued on back..

Notice	CP2000
Tax year	2019
Notice date	August 30, 2021
Social Security number	

Page 2 of 9

- It is **not** necessary to file an amended return (Form 1040X) for 2019 if you don't agree with our changes. We'll review your response and make any applicable corrections. However, if you choose to file an amended return, write "CP2000" on top of it and attach it **behind** your completed Response form.

If you need assistance contact us at 1-800-829-8310.

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**If we don't hear from you**

If we don't receive your response by September 29, 2021, we'll send you a Statutory Notice of Deficiency followed by a final bill for the proposed amount due. During this time, interest will continue to accrue and penalties may apply.



Notice CP2000  
 Tax year 2019  
 Notice date August 30, 2021  
 Social Security number  
 Page 3 of 9

**Changes to your 2019 tax return**

Your income and deductions	Shown on return	As corrected by IRS	Difference
Retirement income gross	\$0	\$61,797	\$61,797
<b>Income net difference</b>			<b>\$61,797</b>
<b>Change to taxable income</b>			<b>\$61,797</b>

**Your tax computations**

	Shown on return	As corrected by IRS	Difference
014049 Taxable income, Form 1040, line 11b	\$83,359	\$145,156	\$61,797
Tax, Form 1040, line 12b	\$10,060	\$23,651	\$13,591
Child tax credit and other dependent, Form 1040, line 13a	\$2,500	\$2,500	\$0
Total tax, Form 1040, line 16	\$7,560	\$21,151	\$13,591
<b>Tax you owe</b>			<b>\$13,591</b>

**Payments**

	Shown on return	As corrected by IRS	Difference
Income tax withheld, Form 1040, line 17	\$7,209	\$7,209	\$0
<b>Total payments</b>			<b>\$0</b>

**Explanation of changes to your 2019 Form 1040**

This section tells you specifically what income information the IRS received about you from others (including your employers, banks, mortgage holders, etc.). This information doesn't match the information you reported on your tax return.

Use the table to compare the data the IRS received from others to the information you reported on your tax return to understand where the difference(s) occurred. To assist you in reviewing your income amounts, the table may include both reported and unreported amounts.

**Retirement Income Gross**

Received from	Address	Account information	Shown on return	Reported by others	Difference
CITY OF BAKERSFIELD	1600 TRUXTUN AVE BAKERSFIELD CA 93301		\$0	\$61,797	\$61,797

Form 1099-R  
Distrib CD 7

**Retirement distributions**

We couldn't identify the retirement distribution reported on your return based solely on information your payers reported to us. We need to know if the reported income is a pension, annuity, IRA, lump sum distribution, or employee savings plan.

If it's an annuity and you're recovering your after-tax contributions using the Simplified Method or General Rule, send us a signed statement with the date of your first payment, the amount you receive monthly, and the total amount you contributed.

If it's an IRA or lump sum distribution which you rolled over, send us Form 5498, IRA Contribution Information or similar documentation.

If the income is an employee savings plan, send us a copy of the document showing the gross and non-taxable amount of the distribution you received.

Continued on back...

Tax year 2019  
 Notice date August 30, 2021  
 Social Security number  
 Page 4 of 9

**Misidentified income**

If any of the income shown on this notice isn't yours, send us the name, address, and taxpayer identification number of the person who received the income. To prevent future incorrect reporting to the IRS, notify the payer to adjust their records to show the correct name and taxpayer identification number.

**Form W-2 or 1099 not received**

The income reported on your return doesn't match the documents we received from your employer or payers. The law requires you to accurately report all income you receive. If your employers don't send proper information documents or forms (for example, Form W-2, Wage and Tax Statement, Form 1099), you must estimate your income based on your paycheck stubs, bank statements, or other records and include your estimate on your tax return.

**Next steps**

If you agree with our proposed changes, send us your signed Response form so we receive it by the due date of this notice. After you receive the billing notice showing we've adjusted your account, you can use the following online payment options:

- Visit [www.irs.gov/payments](http://www.irs.gov/payments) for information about online payment options including:
  - Pre-assessed installments and payment agreements
  - Payroll deductions
  - Credit card payments
  - Direct debit payments
  - Applicable fees
- To apply for an installment agreement plan by mail, send in your signed Response form AND a completed Form 9465, Installment Agreement Request.

If the same error occurred in another tax year, file a Form 1040X for that tax year.

We send information about these changes to state and local tax agencies. If the changes we made to your federal tax return also impact your state or local tax return, file an amended state or local tax return as soon as possible.

**Penalties**

We are required by law to charge any applicable penalties.

**Substantial tax understatement**

Description	Amount
Accuracy-related penalty substantial understatement of tax - IRC 6662(b)(2); 6662(d)	\$2,718

If we increase your tax and the increase is more than the greater of 10% of your correct tax liability or \$5,000, we're required to charge an accuracy-related penalty for the substantial understatement of tax. The penalty is 20% of the portion of the underpayment of tax attributable to a substantial understatement of income tax. We may reduce or eliminate the penalty if you send a signed statement with one of the following:

- Facts that support your treatment of the understated income and the authority for your decision, such as the Internal Revenue Code, Treasury Regulations, Revenue Rulings, Revenue Procedures, etc.
- An explanation as to how you clearly disclosed the item, such as by attaching Form 8275, Disclosure Statement, or Form 8275R, Regulation Disclosure Statement, and that there is a reasonable basis for your position.

Appendix B:

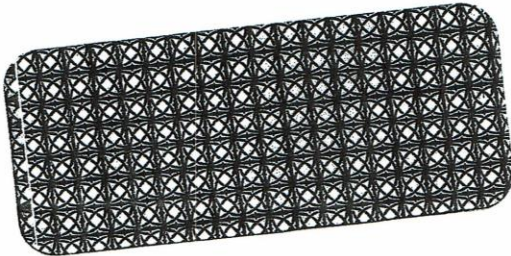
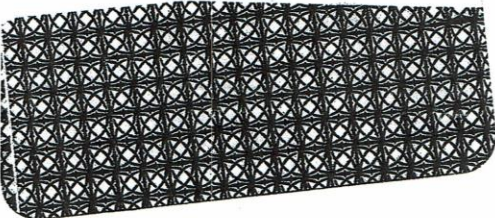
VOID  CORRECTED (if checked)

PAYER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and phone no. City of Bakersfield 1600 Truxtun Ave Bakersfield, CA 93301		1 Gross distribution \$	OMB No. 1545-0119 <b>2019</b> Form 1099-R		Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.
		2a Taxable amount \$ 0.00	Total distribution <input type="checkbox"/>		
PAYER'S TIN	RECIPIENT'S TIN [REDACTED]	3 Capital gain (included in box 2a) \$	4 Federal income tax withheld \$		Copy C For Recipient's Records  This information is being furnished to the Internal Revenue Service.
RECIPIENT'S name  Street address (including apt. no.)  City or town, state or province, country, and ZIP or foreign postal code		5 Employee contributions / Designated Roth contributions or insurance premiums \$	6 Net unrealized appreciation in employer's securities \$		
		7 Distribution code(s) 7	IRA/SEP/SIMPLE <input type="checkbox"/>	8 Other \$ %	
		9a Your percentage of total distribution %	9b Total employee contributions \$		
10 Amount allocable to IRR within 5 years \$	11 1st year of desig. Roth contrib.	FATCA filing requirement <input type="checkbox"/>	12 State tax withheld \$	13 State/Payer's state no.	14 State distribution \$
Account number (see instructions)		Date of payment	15 Local tax withheld \$	16 Name of locality	17 Local distribution \$

Form 1099-R

(keep for your records)

Department of the Treasury - Internal Revenue Service



**IMPORTANT TAX RETURN DOCUMENT ENCLOSED**

## Appendix C:

**To:** [DDG All Users](#)  
**Subject:** FW: Erroneous 1099-R Filings  
**Date:** Tuesday, July 27, 2021 6:41:29 AM  
**Attachments:** [image001.png](#)  
[image002.png](#)  
[image003.png](#)  
[image004.png](#)

**Warning: This email originated from outside the City of Bakersfield. Think before you click!**

Last March, the email below was sent out to all City employees informing them of an erroneous tax filing with the IRS that has resulted in letters to individuals claiming they received a retirement disbursement by the City which they failed to claim when filing their taxes. Since March, the City hired an outside attorney to assist us in working with the IRS to correct this error. A corrected file was sent to the IRS late June. While letters have continued to trickle out to employees since March, it appears that the last batch that they processed in early July was much larger than previous as the volume of employees reporting receiving one of these letters has increased significantly in the last two weeks. Due to this fact, a copy of your corrected 1099R along with a letter is being mailed to all employees who were affected by the original filing. If you have received a letter and reported it to payroll, a corrected 1099R has already been provided to you. You will still receive a second copy in the mail. We continue to encourage employees who receive letters from the IRS to provide a copy to payroll. If you have any questions, you can reach out to

**From:**  
**Sent:** Thursday, March 25, 2021 11:39 AM  
**To:** DDG All Users  
**Subject:** Erroneous 1099-R Filings

This week, the City received notice from a small number of current and former employees who each had received notifications from the Internal Revenue Service (IRS) stating income had not been included in their 2019 tax filings. Specifically, each were advised that 1099-R forms, supposedly filed by the City of Bakersfield with the IRS in April 2020, had not been included as part of filing their personal taxes.

Based on an initial review by City staff, these forms **were not** transmitted by the City of Bakersfield to the IRS at any time. The City does not file 1099-R forms for City employees in the normal course of business. For the cases involving City employees that we are aware of today, these specific filings are believed to be counterfeit. **Additionally, there is nothing to demonstrate that these erroneous filings were the result of a data breach in the City's network or related to any City business activity.** Staff is continuing to investigate the matter and is currently following up with the appropriate agencies to further understand these filings. However, limited information is available since it is connected to the individual tax-filer.

Should you receive a notice from the IRS regarding a 1099-R form that was supposedly issued by the City of Bakersfield, please contact the IRS and the Finance Department (326-3475) immediately to report this matter. Additional updates will be provided as available to those impacted.



# BAKERSFIELD

THE SOUND OF *Something Better*

City Employees,

July 21, 2021

In March 2021, the City was made aware of erroneous Form 1099-R filings that were transmitted to the Internal Revenue Service regarding pension distribution income for current and former employees of the City. Immediately upon becoming aware of the issue, the City retained an outside attorney to work with the IRS to determine the extent of this error and the source of the data file. We also sent an email to all employees to watch for similar correspondence from the IRS and to contact the Finance Department if anything like that was received. Staff has since been informed that the erroneous filings affected over 1,800 current and former employees of the City.

**There is no evidence that these tax filings came from the City directly nor is there any evidence that these forms were filed as a result of any data breach of City systems.** The City does not file 1099-R for pension distributions for retired employees and their beneficiaries. That pension income is reported by CalPERS. There is also no evidence that these erroneous filings affected individual's retirement accounts with CalPERS or deferred compensation funds held. As of today, the City is working closely with the IRS to identify the original source of the erroneous filings.

In the interim, it was recommended that a "corrected" form be submitted to the IRS by the City showing the pension distribution from the City as zero for all those affected. Those corrected forms were filed with the IRS in June. The volume of the notifications from the IRS to City employees and former employees increased significantly over the last two weeks. It has now been determined that the corrected Form 1099-R will be sent to all affected employees even if they have not been notified by the IRS, along with this accompanying letter to explain the situation.

If you do receive a notification from the IRS stating income was not reported (called a "CP2000" notice) please contact the City Finance Department at (661) 326-3742. The included corrected 1099-R can be sent to your tax preparer or directly to the IRS letting them know you disagree with the assessment of additional income taxes. While we still do not have all the facts on how this occurred, the actions taken to date should address any problems created for individuals who have been understandably concerned and frustrated upon receiving these IRS letters. In the meantime, we continue to investigate this issue and are working to resolve it completely

Sincerely,

Finance Department  
1600 Truxtun Avenue, Bakersfield, CA 93301  
661-326-3742 FAX: 661-852-2040

## Appendix D:

California Civil Code §1798.29:

“(a)Any agency that owns or licenses computerized data that includes personal information shall disclose any breach of the security of the system following discovery or notification of the breach in the security of the data to any resident of California (1) whose unencrypted personal information was, or is *reasonably* believed to have been, acquired by an unauthorized person, or, (2) whose encrypted personal information was, or is reasonably believed to have been, acquired by an unauthorized person and the encryption key or security credential was, or is reasonably believed to have been, acquire by an unauthorized person and the agency that owns or licenses the encrypted information has a reasonable belief that the encryption key or security credential could render that personal information readable or usable. The disclosure shall be made in the most expedient time possible and without unreasonable delay, consistent with the legitimate needs of law enforcement, as provided in subdivision (c), or any measures necessary to determine the scope of the breach and restore the reasonable integrity of the data system.”

California Civil Code §1798.29(f) also states if the data breaches effect more than 500 persons, persons affected must be notified immediately and a report must be submitted to the California Attorney General’s Office.



# CITY OF BAKERSFIELD

## RESPONSE TO ERRONEOUS IRS FILINGS GRAND JURY REPORT

### FINDINGS:

- F1. The City initially did not realize the magnitude of the erroneous filings until numerous employees and retirees informed them of the problem.

**The City agrees with this finding.** However, the City would like to add that the first notification from the IRS came to our attention in the middle March 2021 and by the end of that month the City had obtained outside counsel to work with the IRS to help fully understand the extent of the issue. It was only after working with the IRS that the scope of this erroneous filing became apparent.

- F2. According to California Civil Code, §1798.29, a data breach did not occur.

**The City agrees with this finding.**

- F3. The City's response to the erroneous filing has been adequate, although they should have informed the retirees sooner.

**The City agrees with this finding.** Though the City was not made aware of the total number of affected individuals until May 2021, information regarding the issue was only disseminated to current employees via emails. Retirees should have been notified sooner.

- F4. Because retirees were not informed until four months later, this put them at risk of unnecessarily paying extra taxes, not to mention the risk of identity theft. This is unsettling.

**The City disagrees with this finding.** As mentioned, the City was not made aware of the full extent of the issue until May 2021 and a letter to all affected employees and retirees was sent out in July. During the three months between, the City received phone calls and visits from employees and retirees almost daily where staff let them know that no payments should be made. In fact, no payments were actually made by retirees directly to the IRS with regards to this matter. In addition, this was not a data breach and there is no evidence that this incident put any employees or retirees at more risk for identity theft.

- F5. It is further troubling that the infrastructure of a city as large and prosperous as Bakersfield did not discover the internal source of the error for eight months.

**The City partially disagrees with this finding.** The amount of time it took to fully understand how this erroneous 1099 filing could have occurred is a function of very slow response times from the IRS, misinformation from the current financial software provider and an overall deficiency in that system due to its overall age, technologically speaking. City staff worked continuously during those eight months to both assist affected individuals and work with the IRS to understand how this occurred. The amount of time it took to resolve

this is disconcerting, but the finding implies that extended period was both the City's sole responsibility and that staff was not working daily to resolve the issue.

- F6. It is inconceivable that in this age of cybercrime, the City does not have written Policies and Procedures for dealing with data breaches and possible ransomware. A Policies and Procedures Manual will define and mandate the actions to deal with breaches and other information issues regarding sensitive information such as salaries, employee/retiree data.

**City partially disagrees with this finding.** At the time of the investigation, the City was already in the process of developing a formalized written security incident management program. The City does have procedures for investigating possible cyber incidents and malware attacks and those procedures were followed to arrive at the determination that there was no breach of any systems.

- F7. It appears the City's TS Department is understaffed, to adequately deal with the current onslaught of cybercrime. This places the City in jeopardy of further information breaches.

**City partially disagrees with this finding.** The City would like to clarify and reiterate that there was no breach of any systems, as stated in Finding number 2. On staffing, the City has been investing in the development of the Technology Services Department with the addition of twenty new staff positions over the last three years (which is a 52% increase). Four of these positions have been utilized for the development of a security team dedicated to enhancing cyber and physical security of City assets. Ongoing identification of strategic staffing positions will be requested to bring the staffing of the department in line with other similarly sized cities over the next five years through the budgeting process.

- F8. Current City Finance and TS staff are in dire need of ongoing in-service training on quality control issues regarding the current TS system in use.

**City partially disagrees with this finding.** Additional training for City staff is always preferable and beneficial. However, the careful review of this case indicated that training would have been unlikely to prevent this specific issue. This incident was related to an erroneous computer software setting which created an anomaly in staff processes. This incident prompted an immediate review of procedures and settings, which resulted in changes to prevent this type of situation in the future. The fact that this type of erroneous filing could have occurred was an unknown and only the chain of events that occurred revealed that changes were necessary. The City is aware of the overall deficiency in the current "TS system" (ERP or core financial software system) and is in the midst of an ongoing project to replace that system. Once implemented, the City expects a more robust quality control system related to the ERP operations that is indicative of a 21<sup>st</sup> century, modern product.

## **RECOMMENDATIONS:**

- R1. The TS and Finance departments should generate a written Policies and Procedures Manual, by the end of the current fiscal year, which mandates the immediate notification of all employees and retirees of any data breach or erroneous IRS filing. (Finding 6)

**This recommendation is currently being implemented.** The Technology Services Department has been developing a formalized and documented Security Incident Management Program. This comprehensive program will contain “run books” to address the various incidents that could occur with detailed steps to mitigate against further harm, implement business continuity plans, and issue required notifications. The Finance Department has made the necessary changes to its procedures to prevent these types of filing errors and to provide notifications to affected parties should future errors occur.

- R2. The TS and Finance departments should create a written Policies and Procedures Manual, by the end of the current fiscal year; one that defines and mandates action necessary to deal with potential data breaches, malware, and ransomware information issues. (Finding 6)

**This recommendation is currently being implemented.** The Technology Services Department has been developing a formalized and documented Security Incident Management Program. This comprehensive program will contain “run books” to address the various incidents that could occur with detailed steps to mitigate against further harm, implement business continuity plans, and issue required notifications.

- R3. Within the next three months, devote funding to recruit and retain qualified Technology Services staff. (Finding 7)

**This recommendation will not be implemented.** It is not feasible to appropriate new funding and create new positions to reach a recommended staffing level within three (3) months. As previously noted, the City has been investing in the buildup of the Technology Services Department over the last three years with the addition of twenty (20) new positions. Due to market competition the City, like other public agencies, experiences difficulties in attracting and hiring highly technical positions, and has particular challenges related to Technology Services. Recruitment efforts are ongoing and additional staffing will be addressed in a strategic manner through the normal mid-year and annual budgeting process over several years.

- R4. Within the next three months, provide training to TS and Finance staff to deal with the inadequacies of the current information data system. (Finding 8)

**This recommendation has been implemented.** Training and procedures have been developed and presented to the staff who work with these transactions to mitigate this from happening again.

- R5. Make it a priority to complete the Request For Proposal (RFP) process and implementation of an updated software system. (Finding 8)

**This recommendation has been implemented.** The City has issued an RFP to replace the current ERP and proposals are due on January 20<sup>th</sup>. The full implementation of any new ERP can take two years or more, but the City recognizes the tremendous improvement to operational effectiveness and efficiency a new system will provide.