



CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

October 16, 2008

Honorable City Council
Attention: Finance Committee
Palo Alto, California

City Auditor's Fiscal Year 2008-09 Work Plan

RECOMMENDATION

The City Auditor's Office recommends that the Finance Committee review and recommend to the City Council approval of the City Auditor's Fiscal Year (FY) 2008-09 Work Plan.

BACKGROUND

The mission of the City Auditor's Office is to promote honest, efficient, effective and fully accountable City government. To fulfill this mission, the Auditor's Office conducts audits and examinations of City departments, programs, and services. The purpose of these audits and examinations is to provide the City Council and City management with information and evaluations regarding the effectiveness and efficiency with which City resources are employed, the adequacy of systems of internal controls, and compliance with City policies and procedures and regulatory requirements.

The Palo Alto Municipal Code requires the City Auditor to submit an annual plan to the City Council for review and approval. This report presents the City Auditor's Work Plan for FY 2008-09.

As part of our annual review of potential audit subjects, we solicit audit suggestions from City Council members, members of the public, and staff. We also use information from the City's adopted operating and capital budgets and financial statements to prepare a spreadsheet model of potential audit subjects. The model, called the "Citywide Risk Assessment," helps prioritize audit work by comparing the following ten factors: proposed 2008-09 expenditures, three-year expenditure trend, fund type, proposed five-year capital expenditures, estimated 2008-09 revenue, three-year revenue trend, number of staff (budgeted full time equivalents), fund balance, audit requests, and date of last audit. The results of the Citywide Risk Assessment are attached (see Attachment A).

DISCUSSION OF PROPOSED AUDIT ASSIGNMENTS

The list of proposed assignments for FY 2008-09 includes a mix of audits and special projects that address a wide range of concerns and are consistent with the City Auditor's areas of responsibility. We designed the work plan to address what we consider to be the highest priority areas, while limiting the scope of work to align with our staffing and budget resources. Given the six-month vacancy in the City Auditor position, this work plan is being considered partway through the fiscal year and represents an ambitious undertaking.

Our proposed work plan supports two of the City Council's Top 4 priorities -- Civic Engagement (through the Service Efforts and Accomplishments Report) and the Library building (through the Prospective Analysis of Bond Measure Proceeds). Of the top ten highest risk areas identified by our Citywide Risk Assessment, the Wastewater Treatment Fund was ranked the highest risk and is included in the proposed work plan. The Utilities Department had the most number of programs in the top ten areas (six of ten) and is also included in the proposed work plan. We welcome your comments and suggestions to help ensure we prioritize our work plan to meet the City Council's needs. We have also included an outline summary of the work plan, along with the affected City departments (See Attachment B). Following is a description of each of the projects.

AUDIT ADMINISTRATION, FOLLOW-UP, AND OTHER RESPONSIBILITIES:

1. **Annual Audit Work Plan and Quarterly Status Reports** – The Auditor's Office submits quarterly reports to the City Council outlining project status and progress towards completing the assignments on this annual work plan.
2. **Annual Audit Recommendation Status Report** – The Municipal Code requires the City Auditor to issue an annual report on the implementation status of recommendations from recently completed audits. We also meet with departments mid-year to discuss progress towards implementing open audit recommendations.
3. **External Peer Review** – The external peer review (conducted once every three years) will evaluate the quality control of the Auditor's Office and its compliance with Government Auditing Standards (GAS).

REVENUE AUDITS:

4. **Sales Tax Allocation Reviews** (on-going) – Sales tax represents about 15 percent, or \$22 million, of projected General Fund revenue for 2008-09. We contract with MuniServices for quarterly sales tax audit and information services, and we also conduct sales tax audits in-house. The purpose of these audits is to identify misallocations of local sales tax. In addition, MuniServices prepares the quarterly sales tax information reports that are provided to the City Council as information items. Target completion date: on-going

FINANCIAL AUDITS AND PROCEDURAL REVIEWS:

5. **Annual External Financial Audit** (contracted audit service) – The City Charter requires that the City Council engage an independent certified public accounting firm (currently Maze & Associates) to conduct an annual external audit. Target date for completion of the audit of the June 30, 2008 financial statements: Target date: Dec-2008
6. **Controls Review of SAP Upgrade and Utilities Module Implementation** (on-going) – The City's SAP upgrade is occurring in two phases – Phase I on Employee Self-Service/Management Self-Service was completed July 2008. Phase II on Utilities is currently planned to be completed February 2009. The Auditor's Office has reviewed general controls throughout the upgrade. Target date: Feb - 2009
7. **Accounts Receivable Write-Off of Utilities Billing** (in process) – As the Utilities Department implements the SAP Utilities module, the Auditor's Office is evaluating the outstanding accounts receivable balance from the prior system to identify potential recoveries. Target date: Jan – 2009

8. **Police Investigative Fund (NEW)** - In accordance with the Police Investigative Fund procedures, the City Auditor will conduct a surprise, external audit of the fund. The fund is used to cover certain costs incurred during investigations. Target date: TBD

PERFORMANCE AUDITS AND SPECIAL PROJECTS:

9. **Annual Service Efforts and Accomplishments (SEA) Report** (in process) – This will be the 7th annual SEA report. The purpose of SEA reporting is to strengthen public accountability and help improve government efficiency and effectiveness. Palo Alto's SEA report provides data about the costs, quality, quantity, and timeliness of City services. It includes a variety of comparisons to other cities, and the results of an annual citizen survey (the National Citizen Survey). Target date: Jan-2009
10. **Audit of Ambulance Billing and Revenue Collection** (in process) – The Palo Alto Fire Department responds to between 3,000 to 4,000 medical/rescue calls, and transports between 2,000 to 3,000 individuals annually. The purpose of this review is to assess the overall efficiency and cost effectiveness of ambulance billing and collections. Target date: Jan-2009
11. **Audit of Vehicle Replacement and Maintenance Fund** (in process) – The purpose of this review is to evaluate economy, efficiency and effectiveness of fleet and equipment replacement and maintenance operations. Target date: Spring-2009
12. **Wastewater Treatment Fund** (carryover from FY 2007-08) – The Regional Water Quality Control Plant provides services to Mountain View, Los Altos, Los Altos Hills, Stanford, and East Palo Alto. With proposed revenues of \$20 million, proposed expenditures of \$21 million, a \$45 million five-year capital plan, and 70 full-time equivalent employees, this is one of the areas consistently targeted by our annual citywide risk assessment model. The purpose of our audit would be to review the cost-sharing agreements and allocation of charges to partner agencies. Target date: TBD
13. **Audit of Purchasing Card Transactions** (carryover from FY 2007-08) – The purpose of this audit is to determine the adequacy of controls over purchasing card transactions, and to assess compliance with existing guidelines and procedures. Target date: TBD
14. **Citywide Cash Handling (NEW)** - on July 7, 2008, the City Council voted to have the City Auditor study Citywide cash handling and travel reimbursements, oversight procedures, and the City Auditor's history of audits on cash services. Target date: TBD
15. **Prospective Analysis of Bond Measure Proceeds (NEW)** – subject to voter approval of Measure N) – If voters approve Measure N in the November 2008 election, the City will be preparing to issue general obligation bonds to rebuild the Mitchell Park Library and adjacent community center, and renovate the Main and Downtown libraries. This audit will prospectively evaluate controls for the use of the bond funds to ensure the funds are used efficiently and in compliance with federal regulations for the use of tax-exempt bond funds. Target date: TBD
16. **Utilities Department (NEW)** – Several of the highest risk areas identified in the Citywide Risk Assessment pertain to the Utilities Department. This audit will conduct a preliminary survey of the Utilities Department and develop an audit scope to identify opportunities for improvements in efficiency and effectiveness. Target Date: TBD

Prior Year's Projects Not Included in the FY 2008-09 Work Plan

- **Police Community Survey** (incorporated into the SEA project): This project was

intended to conduct a second survey of persons requesting services from the Police Department and of drivers of vehicles that are stopped to determine how they feel they were treated during the stop. In-lieu of another survey, the Auditor's Office added questions to the National Citizen Survey (used in the SEA Report) to gauge community satisfaction from those in contact with the Palo Alto Police Department. We will incorporate the survey results into the next SEA Report.

- **Property Tax Allocation:** Previous audits revealed low audit recoveries related to property tax allocation and in March 2008, the City Auditor reported to the Finance Committee that this audit would most likely be deferred. If circumstances change in the future, this project could be considered again.

Next Steps

After discussing the proposed Work Plan with the Finance Committee, we will ask the City Council to approve the FY 2008-09 Work Plan in November. Meanwhile, we are continuing work on carryover items from the FY 2007-08 Work Plan.

As audit work proceeds, I will bring to the Finance Committee quarterly reports describing the status and progress towards completing each of the approved assignments (those quarterly reports are forwarded to the City Council for acceptance). Generally, audit reports are heard at the committee level (either by the Finance Committee or the Policy and Services Committee) unless the item is considered to be of interest to the full City Council.

Respectfully submitted,



Lynda Flores Brouchoud
City Auditor

Attachment A: Citywide Risk Assessment Model
Attachment B: FY 2008-09 Work Plan Summary