



## CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

September 20, 2005

Honorable City Council  
Attention: Finance Committee  
Palo Alto, California

### **City Auditor's Fiscal Year 2005-06 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 2005-06 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 2005-06.

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 (see Attachment A). The purpose of the citywide risk assessment model is to help prioritize audit work. The model compares the following factors:

- Proposed 2005-06 expenditures
- Three-year expenditure trend
- Fund type
- Proposed five-year capital expenditures
- Estimated 2005-06 revenue
- Three-year revenue trend
- Number of staff (budgeted full time equivalents)
- Fund balance
- Audit requests
- Date of last audit

#### **Discussion of proposed assignments**

The list of proposed assignments for fiscal year 2005-06 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 what we can realistically accomplish. Our work plan

supports two of the City Council's Top 5 priorities: City Finances and Infrastructure.

#### **AUDIT ADMINISTRATION, FOLLOW-UP, AND OTHER RESPONSIBILITIES:**

1. **Annual 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. **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. This year audit staff will be meeting at mid-year with all involved departments to discuss progress towards implementing open audit recommendations.
3. **Auditor's Office triennial peer review** (carryover from 2004-05) – Government Auditing Standards require audit organizations to have an external peer review once every three years. The National Association of Local Government Auditors coordinates a peer review program to help member organizations meet these standards. Target completion date: Oct-2005.
4. **Meeting attendance** – To facilitate communication and coordination of efforts, the City Auditor attends the City Council meetings, Finance Committee meetings, and the City Manager's weekly executive staff meetings.
5. **Utility Risk Oversight Committee (ROC)** – Since issuance of our *Assessment of Utility Risk Management Procedures* in Jul-2002, the City Auditor has acted as an advisor to the ROC.
6. **<NEW> Independent Police Review Panel** – The City Auditor will participate in an independent panel to review internal investigations and citizen complaints. The panel will make recommendations to the Police Chief and the City Manager, who will retain final authority on disposition.

#### **REVENUE AUDITS:**

7. **Sales tax audits** (on-going) – Sales tax represents about 16 percent, or \$19 million, of projected General Fund revenue for 2005-06. We contract with MBIA MuniServices (MMC) for quarterly sales tax audit and information services. We also conduct audits in-house. Both types of audits focus on verifying that Palo Alto is getting the appropriate allocation of local sales tax. Audit results are reported in the Auditor's Office Quarterly Report. Sales tax information reports (provided by MMC) are transmitted to the City Council on a quarterly basis. Target completion date: on-going.
8. **Property tax audits** (on-going) – Property tax represents about 14 percent, or \$17 million, of projected General Fund revenue for 2005-06. We contract with MMC for property tax auditing and information services. Audit services are designed to help ensure that County assessment data for properties in Palo Alto is current and accurate. Audit results are reported in the Auditor's Office Quarterly Report. Target completion date: on-going.
9. **Documentary transfer tax** – We contract with MMC to ensure that the City's documentary transfer tax (about \$3 million annually) is levied when residential and commercial properties are sold, properly applied, and remitted in a timely manner. Target completion date: on-going.
10. **Utility users tax** (audit follow-up) – In 2002, we contracted with Tax Compliance Services to

audit telephone company UUT remittances. Audit work is completed, but the Auditor's Office will continue to provide assistance as needed to achieve compliance. Target completion date: TBD.

11. **Audit of cable franchise and PEG fees** (in process) – Our audit of Comcast franchise and PEG fees is complete, and a final response from Comcast is pending. Target completion date: TBD.
12. **Transient occupancy tax** (contracted audit service) – Transient occupancy tax represents about 5 percent of General Fund revenues, or about \$6 million per year. We previously audited revenues through Jun-2002. Target completion date: Jun-2006.

#### **FINANCIAL AUDITS AND PROCEDURAL REVIEWS:**

13. **Annual external financial audit** (contracted audit service) – The City Charter requires that the City Council engage an independent certified public accounting firm to conduct an annual external audit. We have contracted with Maze & Associates to conduct the audit. Target date for completion of the 6/30/05 audit: Dec-2005.
14. **Controls reviews of SAP** (on-going) – The implementation of the SAP system is having dramatic impacts on the City's business operations and financial records. The Auditor's Office will continue to monitor the implementation and provide advice to ASD on the adequacy of controls in the new system. Target completion date: on-going.
15. **Audit of the police investigative fund** – Pursuant to Police Department procedures, the Auditor's Office conducts a surprise review on an annual basis. Target date: TBD.
16. **<NEW> Ethics policies** – This project would review procedures for ascertaining and handling potential conflicts of interest among city employees, and assess the need for an ethics policy.

#### **PERFORMANCE AUDITS AND SPECIAL PROJECTS:**

17. **Service Efforts and Accomplishments (SEA) Report** – This will be the 4<sup>th</sup> 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 issuance date: Dec-2005.
18. **Audit of parks maintenance** (in process) – The purpose of our audit is to assess the cost-effectiveness of parks maintenance services. The Community Services Department (CSD) is one of the areas targeted by our citywide risk assessment model. Target completion date: Fall-2005.
19. **Audit of street maintenance** (in process) – Review of the street maintenance program including criteria for prioritizing street repairs, and coordination of subsurface work. Target completion date: Fall-2005.
20. **Police department survey** (in process) – The Auditor's Office is conducting a random survey of drivers of vehicles that are stopped to determine how they feel they were treated during the stop. The Office is also conducting a comparison survey of persons requesting service. Target completion date: Fall-2005.

21. **Review of police building proposal** – In response to a colleagues' memo regarding a developer's proposal to build a new police building downtown, the City Council directed the City Auditor to review the project and provide her comments and assessment to the City Council. On September 1, 2005, the City issued a request for statements of interest and qualifications for the development of a turn-key police building project. Responses are due on October 4, 2005. Target completion date: Fall-2005.
22. **Audit of CSD class program revenue/cost recovery** (carryover project from 2004-05) – The purpose of this audit is to determine the income/subsidy of class programs net of direct and indirect costs. CSD was one of the areas targeted by our citywide risk assessment model. Target start date: Fall-2005.
23. **Audit of entrepreneurial programs** (carryover project from 2004-05) – The City has a number of "entrepreneurial programs" including IT services, animal control, BLS ambulance service, dark fiber services (the Electric Fund was one of the areas targeted by our citywide risk assessment model), and training programs. The purpose of this review would be to analyze the net revenue and cost/benefit of *one* of these programs. Target start date: Spring-2006.
24. **<NEW> Audit of vehicle replacement and maintenance fund** – This internal service fund has 16 full-time equivalent employees and projected 2005-06 expenditures of \$5.8 million. The vehicle replacement and maintenance fund was one of the areas targeted by our citywide risk assessment model. The purpose of this review would be to evaluate economy, efficiency and effectiveness of fleet and equipment replacement and maintenance operations.
25. **<NEW> Audit of the Waste Management/PASCO contract** – The estimated payment to PASCO for refuse collection, hauling, and disposal in 2005-06 is \$8.5 million. The Refuse Fund was one of the areas targeted by our citywide risk assessment model.
26. **<NEW> Infrastructure report card** – The purpose of this project would be to assess the impact of increased capital spending on the City's infrastructure, including utilities. The Capital Improvement Program was one of the areas targeted by our citywide risk assessment model.

### **Projects considered but NOT included on the 2005-06 work plan**

Again this year there were a number of audit requests and other items that we are unable to accommodate in our work plan due to limited audit resources. Some of those items include:

- *Wastewater Treatment Fund (carryover from 2004-05)* – This enterprise fund has proposed revenues of \$26.2 million, proposed expenditures of \$25.2 million, and \$11.6 million five-year capital plan, and 69 employees. This was one of the areas targeted by our citywide risk assessment model.
- *Municipal fee schedule (carryover request from 2004-05)* – Evaluate the cost-recovery status of fees (about \$16.3 million per year), and differences in fees charged to various users.
- *Housing program (carryover request from 2004-05)* – Evaluate potential uses of the housing impact fee fund including cost-effectiveness of the BMR program.
- *Audit of contracting practices (carryover request from 2004-05)* – Review of Palo Alto's

competitive purchasing processes for openness, fairness, and non-discrimination in requesting and awarding contracts.

- *Controls review of the procurement card program* – Review of controls over the City's CAL-card program.
- *Use of temporary employees*
- *Building permit fee collections*
- *Parking district administration*
- *Palo Alto airport*
- *CSD staffing efficiency*
- *General Benefits and Insurance Fund* – This internal service fund accounts for employee health benefits, retirement pension contributions, the City's self-insured workers' compensation and general liability programs. This was one of the areas targeted by our citywide risk assessment model.
- *Water Fund* – This enterprise fund has proposed revenues of \$26.7 million, proposed expenditures of \$21.9 million, a \$16.2 million five-year capital plan, and 41 employees. This was one of the areas targeted by our citywide risk assessment model.
- *Library services*
- *Disaster preparedness*

### **Next Steps**

We plan to present the City Auditor's Fiscal Year 2005-06 Work Plan to the City Council for approval in October. This is an ambitious audit work plan for a small audit shop. 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.

Respectfully submitted,

Sharon W. Erickson  
City Auditor

Attachment A: Citywide risk assessment model





Attachment A  
CITY-WIDE RISK ASSESSMENT

REF. NUM.	DEPARTMENT	PROGRAM/CATEGORY	2005-06 PROPOSED EXPEND	S C O THREE YEAR TREND	S C O FUND TYPE	2005-10 FIVE-YEAR CAPITAL EXPEND	S C O 2005-06 PROPOSED REVENUE	S C O THREE YEAR TREND	S C O 2005-06 NO. OF STAFF	S C O BEG. FUND BALANCE	S C O AUDIT REQUEST	S C O DATE OF LAST AUDIT	S C O RAW SCORE	TOTAL SCORE								
31	ASD	BUDGET	859,503	3	-1%	3	GEN	10	0	0	0%	0	6	1	0	0	10	27	110			
47	FIRE	RECORDS AND INFORMATION MGMT	929,683	3	-13%	3	GEN	10	0	0	0%	0	7	1	0	0	10	27	110			
113	ASD	Cell phone usage	0	0	0%	0	GEN	10	0	0	0%	0	0	0	0	0	2001	10	2003-Self audit	2	22	110
66	POLICE	ANIMAL SERVICES	1,473,208	4	12%	1	GEN	10	0	916,112	3	3%	3	13	2	0	0	2003-Animal Svcs	2	25	109	
23	AUDITOR	CITY AUDITOR'S OFFICE	838,646	3	19%	2	GEN	10	0	235,000	2	191%	5	4	1	0	0	2001-Review	4	27	106	
94	MANAGER	PALO ALTO BUSINESS IMPROV DISTRICT	154,000	2	NA	3	SPEC	3	0	158,000	2	NA	3	0	0	69,000	1	0	10	24	106	
25	COUNCIL	CITY COUNCIL	163,846	2	-39%	4	GEN	10	0	0	0	0%	0	9	1	0	0	10	27	105		
141	PWD	Infrastructure contracting process	0	0	0%	0	CAP	5	0	0	0	0%	0	0	0	0	2002	10	2002-Timeliness	3	18	105
50	HR	EMPLOYMENT	518,980	3	4%	1	GEN	10	0	0	0	0%	0	4	1	0	0	10	25	104		
86	CROSS-DEPT	Special Events	234,164	2	-47%	4	SPEC	3	0	80,800	1	-19%	2	1	1	0	0	10	23	104		
27	MANAGER	ECONOMIC DEVELOPMENT	219,497	2	-18%	3	GEN	10	0	0	0	0%	0	1	1	0	0	10	26	102		
12	CITYWIDE	OTHER REVENUE	0	0	0%	0	GEN	10	0	1,721,000	4	-9%	1	0	0	0	0	10	25	101		
29	ASD	ACCOUNTING	1,961,099	4	16%	2	GEN	10	0	0	0	0%	0	18	3	0	0	2001-Payroll	4	23	99	
93	PLANNING	TRAFFIC MITIG/PARKING IN-LIEU FUNDE	0	0	0%	0	SPEC	3	0	583,000	3	NA	3	0	0	2,609,000	5	0	10	24	96	
106	PWD	CIP - MISCELLANEOUS	326,000	2	NA	3	CAP	5	2,276,000	2	0	0%	0	0	0	0	0	10	22	95		
18	CITYWIDE	RENTS AND LEASES	597,189	3	-16%	3	GEN	10	0	0	0	0%	0	0	0	0	0	1997-MacArthurPai	8	24	93	
3	CITYWIDE	TRANSIENT OCCUPANCY TAX	0	0	0%	0	GEN	10	0	6,173,000	7	11%	3	0	0	0	0	2002-TOT review	3	23	93	
32	ASD	PURCHASING	1,135,949	4	-5%	3	GEN	10	0	6,000	1	5%	3	10	2	0	0	2005-Contract cont	0	23	91	
10	CITYWIDE	REVENUE FROM OTHER AGENCIES	0	0	0%	0	GEN	10	0	204,000	2	-16%	2	0	0	0	0	10	24	90		
1	CITYWIDE	SALES TAX	0	0	0%	0	GEN	10	0	19,036,000	8	9%	3	0	0	0	0	2004-Ongoing	1	22	90	
2	CITYWIDE	PROPERTY TAX	0	0	0%	0	GEN	10	0	16,986,000	8	20%	3	0	0	0	0	2004-Ongoing	1	22	90	
4	CITYWIDE	UTILITY USERS TAX	0	0	0%	0	GEN	10	0	8,341,000	7	14%	3	0	0	0	0	2005-In process	0	20	78	
119	ASD	Duplicate payments	0	0	0%	0	GEN	10	0	0	0	0%	0	0	0	0	0	10	20	70		
137	POLICE	Strategic plan implementation	0	0	0%	0	GEN	10	0	0	0	0%	0	0	0	0	0	10	20	70		
28	MANAGER	PUBLIC COMMUNICATION	246,138	2	-21%	3	GEN	10	0	0	0	0%	0	1	1	0	0	2004-Public Comm	1	17	57	
108	ASD	Cable Joint Powers Authority	0	0	0%	0	SPEC	3	0	0	0	0%	0	0	0	752,000	3	0	2005-In process	0	6	12
138	PWD	Capital projects contingency fees	0	0	0%	0	CAP	5	0	0	0	0%	0	0	0	0	0	2005-Contract cont	0	5	10	

\*\*\*\*\* END OF LISTING \*\*\*\*\*

SCORING TABLES

PROPOSED EXPENDITURES (\$)	
No expenditures	0
Less than 100,000	1
Less than 500,000	2
Less than 1,000,000	3
Less than 2,000,000	4
Less than 3,000,000	5
Less than 6,000,000	6
Less than 10,000,000	7
Less than 20,000,000	8
Less than 30,000,000	9
30,000,000 or more	10

NUMBER OF STAFF (FTE's)	
None	0
less than 10	1
10 or more	2
15 or more	3
20 or more	4
30 or more	5
40 or more	6
55 or more	7
75 or more	8
100 or more	9
500 or more	10

5-YEAR CAP BUDGET	
Zero/none	0
less than 1,000,000	1
less than 5,000,000	2
less than 10,000,000	3
less than 15,000,000	4
less than 20,000,000	5
less than 40,000,000	6
less than 60,000,000	7
less than 100,000,000	8
less than 150,000,000	9
150,000,000 or more	10

LAST AUDIT	
2005	0
2004	1
2003	2
2002	3
2001	4
2000	5
1999	6
1998	7
1997	8
1996	9
PRIOR	10

FUND TYPE	
General	10
Capital	5
Special/enterprise	3

AUDIT REQUEST	
Audit not requested	0
Audit requested	10

THREE YEAR EXPENDITURE TREND (% Change)	
Decrease of more than 50%	5
Decrease of 50% or less	4
Decrease of 25% or less	3
No change	0
Increase of less than 15%	1
Increase of less than 20%	2
Increase of less than 25%	6
Increase of less than 30%	7
Increase of less than 40%	8
Increase of less than 50%	9
Increase of 50% or more	10
Not available/new program	3

BEGINNING FUND BAL	
Zero	0
less than 100,000	1
less than 500,000	2
less than 1,000,000	3
less than 2,000,000	4
less than 3,000,000	5
less than 6,000,000	6
less than 10,000,000	7
less than 20,000,000	8
less than 30,000,000	9
30,000,000 or more	10

ESTIMATED REVENUES	
Zero/none	0
less than 100,000	1
less than 500,000	2
less than 1,000,000	3
less than 2,000,000	4
less than 3,000,000	5
less than 6,000,000	6
less than 10,000,000	7
less than 20,000,000	8
less than 30,000,000	9
30,000,000 or more	10

THREE YEAR REVENUE TREND	
Decrease of more than 50%	10
Decrease of 50% or less	9
Decrease of 40% or less	8
Decrease of 30% or less	7
Decrease of 25% or less	6
Decrease of 20% or less	2
Decrease of 15% or less	1
No change	0
Increase of less than 25%	3
Increase of less than 50%	4
Increase of 50% or more	5
Not available/new program	3