



CITY OF
**PALO
ALTO**

POLICY AND SERVICES COMMITTEE

Tuesday, March 8, 2022
Regular Meeting
Council Chamber & Virtual
7:00 PM

Pursuant to [AB 361](#) Palo Alto City Council and Committee meetings will be held as “hybrid” meetings with the option to attend by teleconference/video conference or in person. To maximize public safety while still maintaining transparency and public access, members of the public can choose to participate from home or attend in person. Information on how the public may observe and participate in the meeting is located at the end of the agenda.

HOW TO PARTICIPATE

VIRTUAL PARTICIPATION

[CLICK HERE TO JOIN](https://cityofpaloalto.zoom.us/j/94618744621) (<https://cityofpaloalto.zoom.us/j/94618744621>)

Meeting ID: 946 1874 4621 Phone:1(669)900-6833

The meeting will be broadcast on Cable TV Channel 26, live on YouTube at <https://www.youtube.com/c/cityofpaloalto>, and streamed to Midpen Media Center at <https://midpenmedia.org>.

IN PERSON PARTICIPATION REQUIREMENT:

- Provide Proof of Vaccination or negative COVID-19 test (taken within 48 hours) and a photo ID
- Masks are strongly recommended
- Maintain social distancing
- If you cannot or do not wish to comply, you can still participate virtually

PUBLIC COMMENTS

Public Comments will be accepted both in person and via Zoom meeting. All requests to speak will be taken until 5 minutes after the staff’s presentation. Written public comments can be submitted in advance to city.council@cityofpaloalto.org and will be provided to the Committee and available for inspection on the City’s website. Please clearly indicate which agenda item you are referencing in your email subject line.

Call to Order

Oral Communications

Members of the public may speak to any item NOT on the agenda.

Action Items

1. Update and Potential Recommendations on Pending State and Federal Legislation. **Report added.**
2. Office of the City Auditor's Presentation of the Economic Recovery Advisory Report.
Presentations
3. Presentation of the FY22 Risk Assessment Report & Audit Plan.
Presentations
4. Presentation of the Office of the City Auditor Quarterly Status Report - October to December 2021.
Presentations

Future Meetings and Agendas

Adjournment

PUBLIC COMMENT INSTRUCTIONS

Members of the Public may provide public comments to virtual meetings via email, teleconference, or by phone.

1. **Written public comments** may be submitted by email to city.council@cityofpaloalto.org.
2. **Spoken public comments using a computer or smart phone** will be accepted through the teleconference meeting. To address the Council, click on the link below to access a Zoom-based meeting. Please read the following instructions carefully.
 - You may download the Zoom client or connect to the meeting in- browser. If using your browser, make sure you are using a current, up-to-date browser: Chrome 30+, Firefox 27+, Microsoft Edge 12+, Safari 7+. Certain functionality may be disabled in older browsers including Internet Explorer. Or download the Zoom application onto your phone from the Apple App Store or Google Play Store and enter the Meeting ID below
 - You may be asked to enter an email address and name. We request that you identify yourself by name as this will be visible online and will be used to notify you that it is your turn to speak.
 - When you wish to speak on an Agenda Item, click on "raise hand." The Clerk will activate and unmute speakers in turn. Speakers will be notified shortly before they are called to speak.
 - When called, please limit your remarks to the time limit allotted.
 - A timer will be shown on the computer to help keep track of your comments.
3. **Spoken public comments using a phone** use the telephone number listed below. When you wish to speak on an agenda item hit *9 on your phone so we know that you wish to speak. You will be asked to provide your first and last name before addressing the Council. You will be advised how long you have to speak. When called please limit your remarks to the agenda item and time limit allotted.

[Click to Join](#) **Zoom Meeting ID: 946 1874 4621 Phone: 1(669)900-6833**

AMERICANS WITH DISABILITY ACT (ADA)

Persons with disabilities who require auxiliary aids or services in using City facilities, services or programs or who would like information on the City's compliance with the Americans with Disabilities Act (ADA) of 1990, may contact (650) 329-2550 (Voice) 48 hours or more in advance.



City of Palo Alto

Policy and Services Committee Staff Report

(ID # 14117)

Meeting Date: 3/8/2022

Title: Update and Potential Recommendations on Pending State and Federal Legislation

From: City Manager

Recommendation

Staff recommends that the Policy and Services Committee (a) receive a legislative update from the City's state and federal advocates, and (b) subject to the Committee's discussion, recommend any pending bills that the full City Council may wish to take a position on outside of the existing legislative guidelines.

Background

On February 7 2022, the City Council adopted the 2022 Legislative Guidelines ([CMR 13904; Minutes](#)). The guidelines provide a baseline for the City's legislative advocates at the state and federal level to advocate on the City's behalf in relation to proposed legislation.

Discussion

The City's legislative advocates in Sacramento (Townsend Public Affairs) and legislative advocates in Washington, D.C. (Van Scoyoc Associates) will be present to discuss updates on legislation, the budget, and the coming weeks and months in Sacramento and D.C. Below is a high-level summary of activity at both the state and federal level.

State Update: **Attachment A** contains the Sacramento update from Townsend Public Affairs. The State legislative calendar is online here: <https://www.assembly.ca.gov/legislativedeadlines> or <https://www.senate.ca.gov/legdeadlines>.

Federal Update: The information below is the Washington D.C. update from Van Scoyoc Asso.

Legislative Branch Activity

FY22 Appropriations Outlook

The War in Ukraine has reinforced the need for Congress to pass the Fiscal Year (FY) 2022 appropriations bills quickly (there are 12 bills total). Congress is poised to bundle the 12 bills into a single omnibus appropriations bill, and negotiations on that bill are going smoothly. President Biden requested \$6.4 billion in military and humanitarian aid be included. There are discussions about where the funding will come from. There are also some discussions of

whether previously appropriated dollars to build the wall on the US-Mexico border can be rescinded and repurposed elsewhere.

Unless these topics are resolved quickly, it is unlikely the House and Senate can pass their massive FY 2022 appropriations bill by the March 11th deadline. That would require another short-term continuing resolution to avoid a government shutdown.

Regardless, the political desire to finish this important bill is very strong, and according to leaders of both parties, they will indeed pass the omnibus bill soon.

President Seeks to Revive ‘Build Back Better’ Bill in State of the Union Speech

In President Biden’s State of the Union speech, he laid out several domestic priorities which he hopes to be included in a future legislative package. The president hopes to rename and repackage the stalled Build Back Better legislation. In his speech he mentioned the need to address inflation by taking the following steps:

- Affordable housing investments
- Invest in weatherization and clean energy solutions
- Cap child-care costs at 7% of a family’s income
- Capping insulin costs at \$35 per month
- Allowing Medicare to negotiate drug prices with manufacturers
- Long-term care facility investments
- Pre-Kindergarten investments

Many of these components were key provisions of the Build Back Better bill which had objections from some senators (including Senator Joe Manchin (D-WV)). Following the State of the Union speech, Senator Manchin described the terms he would need to support such a plan. Senator Manchin wants to repeal some of the 2017 Trump tax cuts on top earners and corporations, with half the revenue generated being dedicated to deficit reduction, and the other half directed at key spending priorities (with a 10-year sunset). Senator Kyrsten Sinema (D-AZ) has opposed repealing the 2017 tax cuts, which makes the path forward questionable on any new Build Back Better packages.

Senate Prepares for Supreme Court Nomination

President Biden announced his nomination of Judge Ketanji Brown Jackson of the DC Circuit Court of Appeals to serve as an Associate Justice on the Supreme Court. The Senate Judiciary Committee announced it will begin Jackson’s confirmation process will begin March 21, starting with an introductory hearing, two days of questioning, and a day of witness testimony. In the coming weeks, Judge Jackson will meet with senators of both parties to address her confirmation. Any time a Supreme Court nomination occurs, all of Capitol Hill focuses on those hearings, and other work slows down. We expect this time to be no different.

Executive Branch Activity

FEMA Extends 100% Federal Funding for COVID-19 Expenses

The Federal Emergency Management Agency (FEMA) announced they are extending through July 1 the authority for the agency to fund 100% of its Public Assistance Category B payments to state and local governments without a local match. Without that announcement, such claims would have reverted to a 75% federal / 25% local split beginning April 1.

CDC Eases Mask Guidance

The Centers for Disease Control and Prevention eased mask recommendations for the vast majority of the country. Rather than use positive case data alone as the basis for its masking recommendations, the CDC is now suggesting officials also weigh metrics such as hospital capacity and coronavirus admissions.

Under the new approach, many parts of the country previously categorized as having “high” or “substantial” virus levels have been reclassified as having “low” to “medium” levels of covid-19 disease. The CDC recommends mask wearing indoors in public settings like schools only in communities with high levels of disease.

The updated CDC mask guidance can be found [here](#).

EPA Local Government Advisory Committee Adopts Infrastructure Recommendations

The Environmental Protection Agency’s (EPA) Local Government Advisory Committee (LGAC) has adopted recommendations to present to EPA Administrator Michael S. Regan on the agency’s implementation of the Bipartisan Infrastructure Law (BIL). The committee was asked for input on how to implement BIL programs in a way that both achieves the Biden Administration’s climate and environmental justice goals and also meets the needs of local governments.

Key recommendations include:

- Expanding the technical assistance available to help local governments access funding, upgrade their infrastructure, and ensure climate and equity are incorporated into their projects.
- Providing training and education at every level of government on environmental justice and encouraging the use of available tools and data to make informed, equitable decisions.
- Issuing guidance to encourage infrastructure projects that do not contribute to climate pollution.
- Encouraging state partners to engage with communities, solicit project ideas from local governments, and include them in decision-making processes.
- Adding flexibility in allowable costs to enable investments in workforce development, community outreach, and the development of regional partnerships.

More information on LGAC and the full set of recommendations can be found [here](#).

FEMA Transfers \$450 Million to Flood Risk Capital Markets

The Federal Emergency Management Agency (FEMA) announced it continues to expand its reinsurance program while also transferring an additional \$450 million to flood risk capital markets to help strengthen the National Flood Insurance Program's (NFIP) financial framework for the 2022 hurricane season.

As part of the three-year reinsurance agreement, FEMA will pay \$61.23 million in premiums for the first year of reinsurance coverage. Additionally, the agreement will cover the following losses for any single flood event:

- 2.5% of losses between \$6 and \$7 billion.
- 5% of losses between \$7 and \$9 billion.
- 32.5% of losses between \$9 and \$10 billion.

Combined with the other outstanding bonds, FEMA says it has transferred \$2.664 billion of the NFIP's flood risk to the private sector ahead of the 2022 hurricane season.

Additional Federal Bill

One item that the City Council expressed interest in during the June 22, 2021 legislative discussion that has come up within the City's SCAP discussions was possible support for the Carbon Dividend Act. To help address carbon pollution around the country, the Energy Innovation and Carbon Dividend Act would impose a fee on the carbon content of fuels that emit greenhouse gases into the atmosphere. The existing Legislative Guidelines do not clearly cover that topic presently. If the Policy and Services Committee would like to recommend the full City Council support this legislation, such a recommendation could be made through this agenda item. More information about the bill can be found online here: <https://www.congress.gov/bill/117th-congress/house-bill/2307>.

Resource Impact

No resource impacts for this particular report.

Stakeholder Engagement

Staff connects with relevant stakeholders as needed throughout the legislative session.

Attachments:

- Attachment A: 2022 State Update Memo for CPA

MEMO

To: Ed Shikada, City Manager
Chantal Gaines, Deputy City Manager

From: Christopher Townsend, President, Townsend Public Affairs, Inc.
Niccolo De Luca, Vice President
Andres Ramirez, Senior Associate
Carly Shelby, Legislative Associate

Date: February 25, 2022

Subject: State Legislative Update for January and February 2022

SUMMARY

Townsend Public Affairs, Inc. (TPA) has prepared this report for the City of Palo Alto as we start another legislative year and as a recap of the first 6 weeks of the 2022 session.

Start of the Second Year

The Legislature reconvened on Monday, January 3, which began the second year of the state's two-year session. Because it is the second year of session, the month of January featured a number of statutory deadlines for 2-year bills to continue through the legislative process. On Monday, January 31, bills introduced in the first year of session had to be passed out of their house of origin and move on to the second house. Those bills which failed to adhere to this deadline were not moving this session.

To meet the January 31 deadline for 2-year bills, the final day of January featured several "do-or-die" votes. In the Assembly, a handful of bills including AB 1400 (Kalra), which creates a state-funded single-payer health care system, and AB 854 (Lee), which requires property owners in rent-controlled jurisdictions to hold on to their buildings for at least five years before invoking the Ellis Act, failed to progress this session.

Friday, February 18 marked the 2022 Legislative Session's bill introduction deadline, meaning all new legislative vehicles will need to be introduced by this date. Although new bills have trickled in since the January 3 start of session, most legislators wait until the final deadline week to introduce the bulk of their proposals. Legislators will still have the opportunity to amend existing bill vehicles into new legislation. Assembly and Senate leaders have set a mid-March deadline for legislators to amend existing "spot" bill language into new language. Additionally, "gut and amended" bill language - which changes the cast and scope of the existing language - will also need to adhere to the mid-March deadline.

The Legislature has introduced a total of 2,115 bills for this 2022 Session. Of the 2,115 total bills introduced by the February 18th deadline, there were over 1,360 Assembly Bills and over 650 Senate Bills. Further down this memo we list some of the notable bills.



Governor Releases January Budget Framework Proposal

On January 10, Governor Newsom released his budget proposal for the 2022-2023 fiscal year, calling it his [California Blueprint](#). According to the Governor, overall spending trends in the proposed budget reflect a more “down to earth” budget framework compared to the 2021-22 FY budget, which included a larger surplus with federal COVID relief funds. Additionally, most of the proposed expenditures – 86% in total – will be made available via one-time spending formulas.

The Framework includes \$286 billion in total spending, reflecting a 9.1% increase, and \$213.1 billion in General Fund spending, which represents a 1.5% increase, from last year’s final budget. The budget framework also proposes to direct \$34.6 billion to the state’s reserves accounts, which includes approximately \$20 billion into the rainy-day fund and \$9.7 billion into the school stabilization reserve.

The Governor also announced that the January Budget proposal assumes a \$45.7 billion operating surplus, of which \$20.6 billion will be available for discretionary use. Governor Newsom iterated that these numbers are likely to change over the next few months, pending revenue information that will materialize during tax return season before the June 15th budget deadline. The breakdown of the surplus funds and earmarked expenditures are as follows:

- Total surplus: \$45.7 billion
 - \$16.1 billion in Proposition 98 obligations
 - \$3.9 billion to pay down unfunded retirement liabilities
 - \$5.1 billion for reserves
- Remaining discretionary total: \$20.6 billion

The proposed budget is largely focused on addressing what Governor Newsom referred to as “California’s five existential threats” which include addressing the COVID-19 crisis, the rising cost of living, homelessness, public safety, and making investments in climate resiliency. Several of the Governor’s specific proposals are targeted for “early action,” which mean the Governor’s goal is to get certain portions of funding out in the coming weeks, well before the final budget is adopted. The early action portions of the budget include \$1.4 billion in emergency appropriations to address the ongoing COVID-19 crisis through bolstering testing access, vaccine distribution, and supporting frontline healthcare workers.

Below is a high-level overview of proposed expenditures, organized by issue area:

- **COVID-19 Relief** (\$2.7 billion total, appropriated over 2 years)
 - \$1.2 billion: bolster testing
 - \$583 million: expand vaccine distribution
 - \$614 million: support frontline healthcare workers
 - \$200 million support state response operations
 - \$110 million: support vulnerable populations and expand contact tracing
- **Combatting the Climate Crisis**
 - Forest Health: \$1.2 billion
 - \$582 million: forest maintenance
 - \$382 million: fuel breaks
 - \$110 million: regional investments
 - Wildfires: \$648 million
 - \$400 million: CAL FIRE firefighter support



- \$248 million: new firefighter equipment
 - Drought: \$750 million
 - \$500 million: immediate drought support
 - \$250 million: drought contingency support
 - Nature Based solutions: \$2.1 billion
 - \$400 million: Coastal and ocean protection
 - \$325 million: community resiliency (catalytic projects, regional collaboration)
 - \$175 million: extreme heat (urban greening)
- **Homelessness** (\$2 billion total)
 - \$1.5 billion: solutions to get people off the streets and into shelters/treatment
 - \$500 million: encampments
 - \$10 million: Returning Home Well

- **Housing** (\$2 billion total)

Last year's housing budget and legislative priorities were focused on housing accountability and reform efforts. This year, the Administration and Legislature will focus on relationship between climate action and housing policy, meaning housing production and density that is both sustainable and reduces sprawl that could overlap with areas of the state susceptible to natural disaster.

- Sustainable Housing Developments
 - \$500 million: Infill Infrastructure Grant Program (\$225 million in 2022-23, and \$275 million in 2023-24)
 - \$300 million: Affordable Housing and Sustainable Communities (\$75 million in 2022-23, and \$225 million in 2023-24)
 - \$100 million: state excess sites development
 - \$100 million: adaptive reuse incentive grants
 - Affordable housing
 - \$200 million (\$50 million in 2022-23, and \$150 million in 2023-24): mixed-income housing development loans
 - \$200 million: portfolio reinvestment program
 - \$100 million : mobile home park rehabilitation
- **Public Safety**
 - Crime prevention
 - \$255 million: competitive grants for local law enforcement agencies over the next three years to help advance the prosecution of retail crime rings.
 - \$30 million: grants to District Attorney offices to fight theft crimes
 - \$25 million: statewide gun-buyback program
 - Emergency response
 - \$17 million: early earthquake warning system
 - \$12 million: new Southern California Emergency response center
- **Transportation**
 - Zero Emissions Vehicles: \$6.1 billion (appropriated over 5 years)
 - Transportation projects: \$9.1 billion (\$4.9 billion General Fund and \$4.2 billion Proposition 1A bond funds)
 - \$4.9 billion:
 - \$2 billion: transit and rail projects



- \$1.25 billion: local projects
 - \$750 million: bicycle/pedestrian safety/connecting communities projects
 - \$500 million: grade crossings
 - \$400 million: climate adaptation
- \$4.2 billion: high-speed rail
- **Supply Chain Resiliency** (\$2.3 billion)
 - \$1.2 billion: investments in port, freight, and goods movement infrastructure
 - \$875 million: ZEV equipment
 - \$110 million: workforce training
 - \$40 million: more licensed truckdrivers cut red tape at DMV
 - \$30 million: process improvements at port facilities
- **Education**
 - \$1 billion: universal Pre-K
 - \$639 million: first year of universal pre-k
 - \$383 million: reduced adult-to-student ratio
 - K-12
 - \$3.4 billion: summer and after school elementary programs
 - \$937 million: additional arts and music investment
 - \$596 million: universal meal program
 - Higher Education
 - New statewide degree completion goal of 70%
 - \$1.6 billion: Community Colleges
 - \$463 million: COLA (5.33%)
 - \$388 million: deferred maintenance
 - \$200 million: part time faculty health insurance
 - \$150 million: recruitment and retention rates
 - \$100 million: student success completion grants
 - \$65 million: transfer reform efforts
 - \$537 million: California State University
 - \$600 million: UC System
- **Small Business Investments**
 - \$3 billion: paying down UI debt
 - \$1 billion: loan guarantees
 - \$500 million: small business tax relief: venues and restaurants
 - \$150 million: small business COVID-19 grant program

Following the release of the budget framework proposal, the Legislature has been holding budget informational hearings within each house's standing budget committees and sub-committees with the plan to be done with hearings by the end of February/early March. However, as of the end of January, the Department of Finance has only released a portion of the trailer bill language detailing implementation and funding formula specifics necessary for enacting the Governor's budget framework.



Governor and Legislative Leaders Announce Agreement on COVID Paid Sick Leave

As expected, the final proposal mirrored previous versions of supplemental paid sick leave. Its provisions apply to employers with more than twenty-five employees. Covered employees are entitled to paid sick leave under one or more of the following circumstances:

- The employee is subject to an isolation period related to COVID-19.
- The employee has been advised by a health care provider to isolate due to COVID-19.
- The employee is attending an appointment for themselves or a family member to receive a COVID-19 vaccine or a vaccine booster.
- The employee is experiencing symptoms or caring for a family member experiencing symptoms related to a COVID-19 vaccine or vaccine booster.
- The employee is experiencing symptoms of COVID-19.
- The employee is caring for a family member who is isolating due to COVID-19.
- The employee is caring for a child, whose school or place of care is closed or otherwise unavailable for reasons related to COVID-19 on the premises.

Full-time employees are entitled to 40 hours of paid sick leave for any of the above reasons. Part-time employees are entitled to a proportionate number of hours based on their schedule. Employees are entitled to an additional 40 hours of paid sick leave if the employee or a family member tests positive for COVID-19 and provides documentation of a positive test. The maximum amount of paid sick leave a full-time employee can take during the period from January 1, 2022, to September 30, 2022, is 80 hours. If an employee is eligible for exclusion pay under the [Cal/OSHA Emergency Temporary Standard](#), paid sick leave hours cannot be used to offset any exclusion pay obligation.

Governor Signs Early Action Budget Bills into Law

The Governor signed early action budget bills into law, all of which take effect immediately. The new measures include:

- **[SB 113](#) (Committee on Budget and Fiscal Review) *Economic relief: COVID-19 pandemic.***

This measure transfers \$150 million into the California Emergency Relief Fund to fund remaining eligible waitlisted grant applicants from last year's California Small Business COVID-19 Relief Grant Program. Additionally, the measure restores the net operating loss (NOL) deduction and lifts the cap on business incentive tax credits that were suspended and capped in the 2020-21 budget.

- **[SB 114](#) (Committee on Budget and Fiscal Review) *Employment: COVID-19: supplemental paid sick leave.***

This measure provides 80 hours of paid Covid-19 leave for covered employees working for an employer with over twenty-five employees. The previous law requiring coverage (SB 95, Statutes of 2021) expired Sept. 30, 2021. SB 114 mirrors the provisions included in the previous law, with two notable changes, which include the following additional qualifying cases for taking paid sick leave time:

- Attending an appointment to receive a COVID-19 vaccine or a vaccine booster for the employee's family member; or
 - Caring for a family member who has symptoms from a COVID-19 vaccine or a vaccine booster.
- **[SB 115](#) (Skinner) *Budget Act of 2021.***



This measure amends the language contained within the 2021 Budget Act to provide for the immediate disbursement of funds marked for early action. This includes \$1.9 billion from the General Fund to the California Emergency Relief Fund for COVID-19 mitigation, which includes increasing testing capacity, enhancing vaccination programs, and supporting frontline workers. In addition to the new funds for COVID-19 mitigation and support, the measure allows the state to backfill funds for rental assistance not covered by federal dollars.

Notable bill introductions include the following:

As noted previously in this memo, Friday, February 18 marked the 2022 Legislative Session's bill introduction deadline and the Legislature introduced a total of 2,020 bills for this 2022 Session. Below is just a handful of bills we wanted to bring to the City's attention.

- **[AB 1795 \(Fong\)](#) *Open meetings: remote participation.***

Requires state bodies to provide all persons the ability to participate both in-person and remotely in any meeting and to address the body remotely.

- **[AB 1857 \(C. Garcia\)](#) *Solid waste.***

Removes the diversion credit for municipal solid waste incinerators and redefines the practice of incineration as disposal. Requires CalRecycle to ensure that municipalities are prioritizing zero-waste strategies before constructing new incinerators (to meet 1383 diversion requirements).

- **[AB 1859 \(Levine\)](#) *Mental health services.***

Expedites outpatient care for persons committed to involuntary detention. Requires a licensed mental health professional to follow up with a previously detained person no later than 48 hours after release.

- **[AB 1883 \(Quirk Silva\)](#) *Public restrooms.***

Requires local governments to complete an inventory of public restrooms owned and maintained by the local government, either directly or by contract, which are available to the general population in its jurisdiction.

- **[AB 1909 \(Friedman\)](#) *Vehicles: bicycle omnibus bill.***

Removes the prohibition of class 3 electric bicycles on trails, bikeways, bike lanes equestrian trails, or hiking or recreational trails and removes the authority of a local jurisdiction to prohibit class 1 and class 2 electric bicycles on these facilities. Instead authorizes a local authority to prohibit the operation of a class 3 electric bicycle at a motor-assisted speed greater than twenty miles per hour.

For reference:

Class 1 = pedal assist only tops off at 20 mph and no throttle

Class 2 = throttle and maxes out at 20mph.

Class 3 = Pedal Assist only and tops off at 28mph.

- **[AB 1944 \(Lee\)](#) *Local government: open and public meetings.***

Requires all open and public meetings of a legislative body that elects to use teleconferencing to provide a video stream accessible to members of the public and an option for members of the public to address the body remotely during the public comment period through an audio-visual or call-in option. Authorizes a local legislative body to, upon majority vote, waive Brown Act requirement of publishing their private addresses and making those addresses accessible to the public.



- **[AB 1993](#) (Assembly Members Wicks, Aguiar-Curry, Low, and Weber) COVID-19 vaccination requirements**

Mandates vaccines for workplaces (for both employees and independent contractors) and requires employers to verify that their workers are immunized. New hires would need to have at least one shot by their first day — and the second within 45 days. Exemptions are made for persons ineligible to receive a COVID-19 vaccine due to a medical condition or disability or who hold a sincerely held religious belief.

- **[AB 2026](#) (Friedman) *Recycling: plastic packaging and carryout bags.***

Prohibits an online retailer that sells or ships purchased products in or into the state from using single-use plastic or polystyrene packaging that consists of shipping envelopes, cushioning, or void fill to package or transport the products, on and after January 1, 2024, for large online retailers, and on and after January 1, 2026, for small online retailers.

- **[AB 2053](#) (Lee) *The Social Housing Act.***

Creates a California Housing Authority to produce and acquire social housing developments for the purpose of eliminating the gap between housing production and regional housing needs assessment targets. Check out the bill's dedicated website [HERE](#).

- **[AB 2062](#) (Salas) *Local law enforcement hiring grants.***

Establishes a grant program to provide \$50,000,000 in grants to local law enforcement agencies to incentivize peace officers to work in local law enforcement agencies that are in underserved communities and to live in the communities that they are serving.

- **[AB 2063](#) (Berman) *Density bonuses: affordable housing impact fees.***

Prohibits affordable housing impact fees, including inclusionary zoning fees, in-lieu fees, and public benefit fees, from being imposed on a housing development's density bonus units.

- **[AB 2070](#) (Bauer-Kahan) *Electrical corporations: high fire risk areas: hot work and deenergization events: notice requirements.***

Requires an electrical corporation to notify a fire protection district at least 24 hours before performing specified actions, including the initiation of a deenergization event within the district's jurisdiction. Subjects an electrical corporation that fails to provide sufficient notice to a civil penalty of \$500.

- **[AB 2097](#) (Friedman) *Residential and commercial development: remodeling, renovations, and additions: parking requirements. (Reintroduced)***

Prohibits local agencies from imposing minimum parking requirements on residential, commercial, or other development if the development is located on a parcel that is within one-half mile of public transit. Prohibits these provisions from reducing, eliminating, or precluding the enforcement of any requirement imposed on a new multifamily or nonresidential development to provide electric vehicle supply equipment installed parking spaces or parking spaces that are accessible to persons with disabilities.

- **[AB 2249](#) (Rubio) *Open meetings: local agencies: teleconferences.***

Authorizes a local agency to use teleconferencing without complying with specified teleconferencing requirements if at least a quorum of the members of the legislative body



participates in person from a singular location clearly identified on the agenda that is open to the public and situated within the local agency's jurisdiction.

- **AB 2557 (Bonta) Peace officers: records.**

Makes records and information obtained from records maintained by an agency or body established by a city, county, city and county, local government entity, state agency, or state department for the purpose of civilian oversight of peace officers subject to disclosure pursuant to the California Public Records Act. Requires those records to be redacted only as specified.

- **SB 897 (Wieckowski) Accessory dwelling units: junior accessory dwelling units.**

Increases the maximum height limitation that may be imposed by a local agency on an accessory dwelling unit from 16 to 25 feet.

- **SB 906 (Portantino) School safety: mass casualty threats: firearm disclosure.**

Requires parents/guardians of children in k-12 to disclose to schools if they have a gun at home, how it is stored, and how accessible it is to the student.

- **SB 930 (Wiener) Housing Accountability Act.**

Authorizes HCD to resolve ambiguities in the Housing Accountability Act by issuing standards and definitions.

- **SB 953 (Min) Oil and gas leases: state waters: State Lands Commission.**

Bans all offshore drilling in CA by 2023.

- **SB 964 (Wiener) Behavioral health.**

Establishes \$37,000 in stipends to students pursuing a master's degree in social work who go on to work in behavioral health at a public agency, while creating a state fund to increase

- **SB 980 (Wiener) Alcoholic beverage licenses.**

Prohibits ABC from denying the issuance of a retail alcohol license solely on the basis that the premises are located within one hundred feet of a residence and prohibits the department from maintaining a presumption that the issuance of a retail license for a premises located within one hundred feet of a residence would interfere with the quiet enjoyment of the property.

- **SB 1067 (Portantino) Housing development projects: automobile parking requirements.**

Prohibits city a with a population greater than 200,000 from imposing any minimum automobile parking requirement on a housing development project that is located within 1/2 mile of public transit and that either (1) dedicates 75% of the total units to low- and very low income households, the elderly, or persons with disabilities or (2) the developer demonstrates to the local agency that the development would not have a negative impact on the local agency's ability to meet specified housing needs and would not have a negative impact on traffic circulation or existing residential or commercial parking within 1/2 mile of the project.

- **SB 1079 (Portantino) Vehicles: sound-activated enforcement devices.**

Authorizes local jurisdictions to use sound-activated enforcement devices to capture vehicle noise levels that exceed the legal limits and face any applicable penalties after a 30-day warning period.

- **SB 1100 (Cortese) Open meetings: orderly conduct.**



Authorizes members of the legislative body conducting a meeting to remove an individual for willfully interrupting the meeting, thereby modifying the Brown Act.

- **SB 1117 (Becker) General plans: environmental justice element.**

Existing law requires local governments to adopt or review the environmental justice element, or the environmental justice goals, policies, and objectives in other elements, upon the adoption or next revision of two or more elements concurrently on or after January 1, 2018. This bill instead requires local governments to adopt or review the environmental justice element upon the adoption or next revision of one or more elements.

- **SB 1154 (Eggman) Facilities for mental health or substance use disorder crisis: database.**

Requires, by January 1, 2024, the State Department of Public Health, in consultation with the State Department of Health Care Services and the State Department of Social Services, and by conferring with specified stakeholders, to develop a real-time, internet-based database to collect, aggregate, and display information about beds in inpatient psychiatric facilities, crisis stabilization units, residential community mental health facilities, and licensed residential alcoholism or drug abuse recovery or treatment facilities in order to facilitate the identification and designation of facilities for the temporary treatment of individuals in mental health or substance use disorder crisis.

More Members Depart the Legislature or Will not Seek Reelection

January featured more legislators announcing that they would be pursuing other opportunities rather than remaining in the Legislature. Notable resignations during the month of January include:

- Former Assembly Member Lorena Gonzalez, the Chair of the Assembly Appropriations Committee, departed the Legislature on January 5 to lead the California Labor Federation after its longtime executive-secretary treasurer, Art Pulaski, steps down this summer.
- Former Assembly Member Autumn Burke departed the Legislature on February 1. She served as chair of the Assembly Committee on Revenue and Taxation. Assembly Speaker Rendon has not yet announced a new committee chair.

The Assembly now features five total empty seats pending special election outcomes. The seats slated for special election include:

- *Assembly District 17 (formerly held by David Chiu) – February 15, 2022*
- *Assembly District 49 (formerly held by Ed Chau) – February 15, 2022*
- *Assembly District 11 (formerly held by Jim Frazier) – April 5, 2022*
- *Assembly District 80 (formerly held by Lorena Gonzalez) – April 5, 2022*
- *Assembly District 62 (formerly held by Autumn Burke) – Pending scheduling*

In total, five legislators have left mid-term, six will term out in 2022, and 15 have announced they will not seek reelection. These numbers exclude the handful of races where the newly drawn districts will pit incumbents against one another, leading to more incumbents out of the Capitol next year.

Additional updates

Amended "The Taxpayer Protection and Government Accountability Act" Receives Title and Summary



The Attorney General issued [title and summary](#) for the California Business Round Table-sponsored “Taxpayer Protection and Government Accountability Act.” Initiative proponents withdrew a previous version of the initiative language to push forward the initiative’s amended language. Following the issuance of title and summary, proponents can begin signature gathering. They must submit 997,139 valid signatures to qualify for the November 2022 ballot. The Secretary of State’s recommended date to turn in signatures is April 29, 2022.

The Taxpayer Protection and Government Accountability Act would amend the California Constitution to restrict the ability of the state, local governments, other local agencies, and the electorate to approve or collect taxes, fees, and other revenues. It would require voter approval of all state taxes, would further restrict local fee authority by limiting it to the “minimum amount necessary” to provide government services, and would require voter approval for local measures such as franchise fees. Its provisions would make it easier to challenge local revenue measures by increasing the burden of proof on local agencies while disallowing an agency’s characterization of a measure from being considered in court.

Initiative opponents comprise a [coalition](#) of organizations including the League of California Cities, California Professional Firefighters, AFSCME, SEIU, and the California Alliance for Jobs.





City of Palo Alto

Policy and Services Committee Staff Report

(ID # 13909)

Meeting Date: 3/8/2022

Title: Office of the City Auditor's Presentation of the Economic Recovery Advisory Report

From: City Manager

Lead Department: City Auditor

Recommendation

The City Auditor recommends that the Policy & Services Committee take the following action:

- 1) Review the Economic Recovery Advisory report and corresponding recommendations for improvement and recommend the City Council accept the report.

Background

Baker Tilly, in its capacity serving as the Office of the City Auditor (OCA), performed a citywide risk assessment that assessed a wide range of risk areas, including strategic, financial, operational, compliance, technological, and reputation risks. The purpose of the assessment was to identify and prioritize risks to develop the annual audit plan.

During the [FY2021 risk assessment](#), the OCA identified the followings risks which led to this project:

- COVID-19 Response
- Financial Performance/Revenue Generation
- Tax Revenue & Economic Recovery

Discussion

The OCA performed a review of the City's long-term financial planning models and inputs and offer recommendations for improvement. This model is known as the Long Range Financial Forecast (LRFF). This audit activity was conducted in accordance with the [FY2021 Audit Plan approved by City Council](#).

The objectives of the audit activity were to:

- 1) Review the City's long-term financial planning models and inputs and offer recommendations for improvement.
- 2) Identify and evaluate key revenue source categories that present long term risk to the City's financial sustainability and perform scenario analysis.
- 3) Offer ad hoc advisory assistance during the FY22 budget process.

Through the audit activity, the OCA identified four (4) recommendations. The Administrative Services Department concurred with each finding and has drafted action plans for each item.

The Office of City Auditor will perform periodic follow up procedures to validate that recommendations have been addressed as indicated in management responses.

The analysis, observations, and recommendations are summarized in the attached Economic Recovery Advisory report. Please note that the OCA has attached an additional report, intended to be for informational purposes only (i.e., no recommendations), that was derived as a result of our work on this project. This supplemental report is entitled the Economic Resiliency Review.

Timeline, Resource Impact, Policy Implications

The timeline for implementation of corrective action plans is identified within the attached report. All corrective actions are scheduled to be implemented by Fall of 2022 as part of the next Long Range Financial Forecast as well as the remaining FY 2023 annual budget process to the extent appropriate.

Stakeholder Engagement

The Office of the City Auditor worked primarily with the Administrative Services Department and engaged with additional stakeholders, including the City Manager's Office and City Attorney's Office, as necessary.

Environmental Review

Environmental review is not applicable to this activity. **Attachments:**

- Office of the City Auditor - Economic Recovery Advisory - Final Draft for P&S
- Office of the City Auditor - Economic Resiliency Review - Final Draft for P&S



City of Palo Alto

Office of the City Auditor
Economic Recovery Advisory
March 15, 2022

Attachment: Office of the City Auditor - Economic Recovery Advisory - Final Draft for P&S (13909 : Presentation of the Economic Recovery

Executive Summary

Purpose of the Audit Activity

The purpose of this audit activity was to review the City of Palo Alto's ("City") long-term financial planning models and inputs, offer recommendations for improvement, identify and evaluate key revenue source categories that present long term risk to the City's financial sustainability and perform scenario analysis. The Office of the City Auditor ("OCA") also offered ad hoc advisory assistance during the FY22 budget process.

In addition to the above, the OCA included economic development subject matter experts to conduct a high-level review of economic resiliency as a resource to the City and any future City employees focused on economic development initiatives. The report highlights below summarize all that is included in the informational economic resiliency report as well as the Revenue Trends and Models Review.

Report Highlights

Revenue Trends and Models Review

- Page 8** The review of the City's forecasting models focused on three major revenue sources with inputs that may be more affected by current economic trends:
- Transient Occupancy Tax (TOT)
 - Sales Tax
 - Property Tax

The analysis of the City's revenues also focused on Documentary Transfer Tax and Utility User Tax.

This section reviews the revenue sources in light of historical performance, historical averages, and corresponding economic indicators. It also provides a description of models used, some industry best practices where applicable, and corresponding observations and recommendations.

For each major revenue source, the OCA presents the data from all correlations and analyses completed, presenting the information with all factors considered. Each section has specific notes regarding the OCA's thoughts on trends, but the OCA also found that the City's current LRFF aligns with the OCA's considerations.

The OCA also analyzed data and assumptions used for models, evaluated economic factors impacting each revenue source, and determine whether the current financial forecast model uses the most relevant economic factors for predictive purposes. While the OCA provides specific recommendations and considerations, the City's models are overall aligned with best practices. The OCA does recommend that workbooks are notated with more thoroughness and that clarity is provided where assumptions are made.

**Economic Resiliency
Review**

Page 33 The Economic Resiliency Review is released as an independent informational report, but this section reviews the scope of the document, including categories of recommendations and research.

The OCA provides detailed recommendations in this separate report, include recommendations regarding business and industry attraction, retention, and diversification strategies, housing and workforce findings impacted by COVID-19 pandemic, and enhancements to livability for residents and business engagement and retention.

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Introduction

Objective

The objectives of this audit activity were to:

- 1) Review the City's long-term financial planning models and inputs and offer recommendations for improvement.
- 2) Identify and evaluate key revenue source categories that present long term risk to the City's financial sustainability and perform scenario analysis.
- 3) Offer ad hoc advisory assistance during the FY22 budget process.

Background

The OCA performed a citywide risk assessment that assessed a wide range of risk areas, including strategic, financial, operational, compliance, technological, and reputation risks. The purpose of the assessment was to identify and prioritize risks to develop the annual audit plan.

During the [FY2021 risk assessment](#), the OCA identified the followings risks which led to this project.

- COVID-19 Response
- Financial Performance/Revenue Generation
- Tax Revenue & Economic Recovery
- Current Planning Practices

Additionally, during the risk assessment, Baker Tilly included some examples of potential risks in the future related to this audit:

- Large businesses moving to other locations or decreasing the focus on in-person interactions at headquarters, lowering the daytime population and visitors
- Decreasing real estate values due to external factors decreases City revenues from property taxes
- Lost revenue for the City to fund City services with Prop 13 in place
- High taxation on residents due to increased property values, especially long term Palo Alto residents, in the absence of Prop 13

Scope

The project team analyzed each revenue source. The analysis, which focused on a subset of high risk revenue sources, includes the following:

- Historical trends
- Distribution of revenue sources by revenue type:
 - Source(s)
 - Concentration/distribution of revenue received to identify:
 - Largest payors
 - Geographic location
 - Historical relationship between economic factors and other relevant factors to revenue amounts
 - Perform a sensitivity analysis to determine the range of likely variability based on relevant drivers of sensitivity
 - Comparison of per-capita revenues by type to other similar cities

Methodology

To achieve the engagement objectives, Baker Tilly conducted an analysis that will encompass the steps listed below.

- Audit Planning & Management
 - Gather information to understand the environment under review
 - Assess the audit risk
 - Write audit planning memo and audit program

- Announce initiation of audit and conduct kick-off meeting with key stakeholders
- Information Gathering
 - Request and review background information
 - Conduct interviews with key stakeholders
 - Conduct research to identify relevant information to assess risks
- Analyze
 - Historical trends
 - Distribution of revenue sources by revenue type
 - Review analysis with City staff
 - Modify analysis incorporating City staff recommendations as appropriate
- Reporting
 - Develop findings, conclusions and recommendations
 - Validate findings with appropriate individuals
 - Draft audit report and obtain written management responses
 - Review report with member of City Council and/or the appropriate committee
 - Present the final report to City Council and/or the appropriate committee

Compliance Statement

This audit activity was conducted from September 2021 to January 2022 in accordance with generally accepted government auditing standards, except for the requirement of an external peer review^[1]. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Organizational Strengths

During this audit activity, we observed certain strengths of the City. Key strengths include:

- Detailed and thorough data collection and financial analysis
- Strategic mindset and intentionality in economic analysis and planning, including proactively reaching out to industry experts
- High level of competency among City personnel

Additionally, the OCA commends the City for its response to COVID-19. In particular, we greatly admire all efforts taken to support the health and wellbeing of Palo Alto citizens and Stanford students, as well as the support of essential workers during this time of heightened risk.

The Office of the City Auditor greatly appreciates the support of the Administrative Services Department in conducting this audit activity.

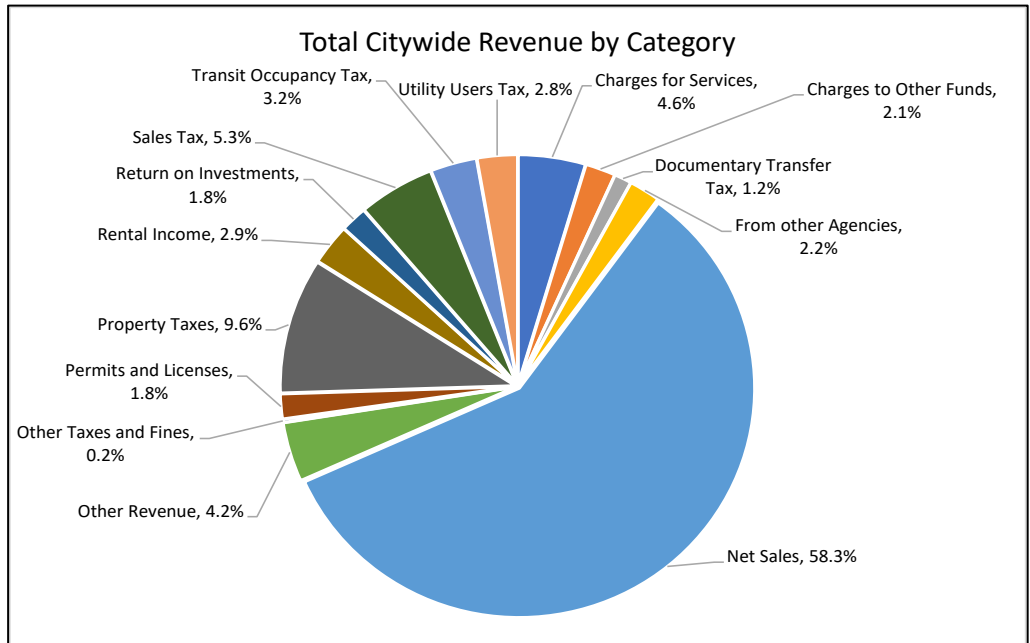
Thank you!

^[1] Government auditing standards require an external peer review at least once every three (3) years. The last peer review of the Palo Alto Office of the City Auditor was conducted in 2017. The Palo Alto City Council approved a contract from October 2020 through June 2022 with Baker Tilly US, LLP (Baker Tilly) and appointed Kyle O'Rourke, Senior Consulting Manager in Baker Tilly's Public Sector practice, as City Auditor. Given the transition in the City Audit office, a peer review was not conducted in 2020 and will be conducted in the second year of Baker Tilly's contract.

Introduction to City Financials

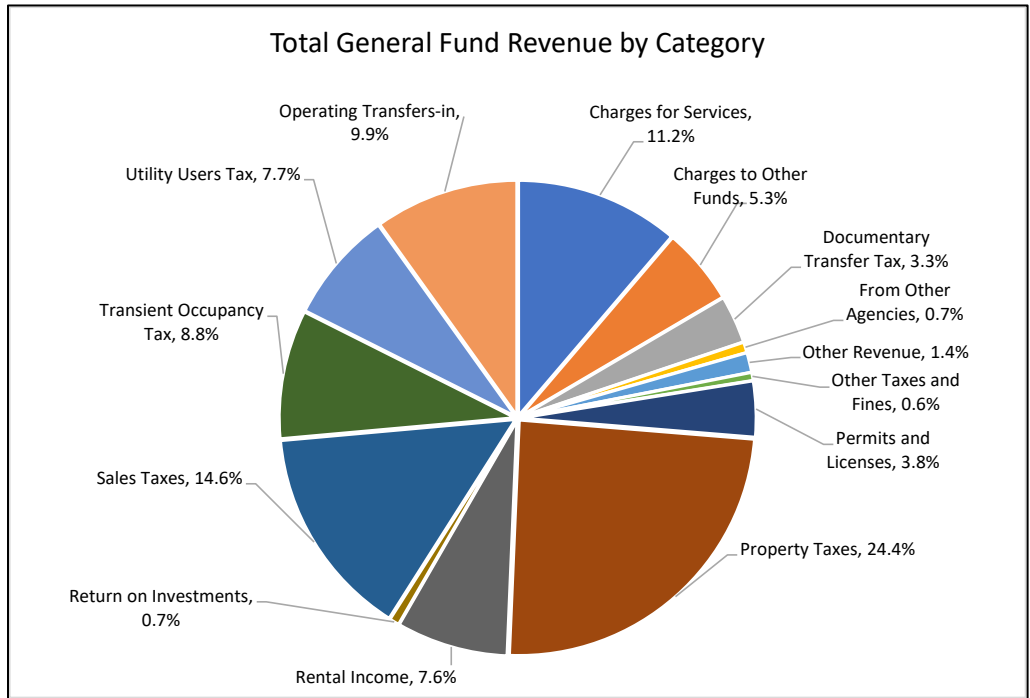
Citywide Revenue

Over the last five fiscal years (2016 – 2020) the City’s overall revenue collection has increased by \$100 million dollars. However, the COVID-19 pandemic also resulted in a \$60 million dollar decrease from FY 2019 – 2020. The City’s total revenues for FY 2020 were \$581.1 million dollars which includes both government and enterprise type funds.



General Fund Revenue

Even though the City has managed to maintain accurate projections for upcoming fiscal years, the COVID-19 pandemic has posed a challenge to forecasting model/revenue projection methods. Although the enterprise funds comprise a larger portion of the City’s total revenues, the OCA maintained focus on revenues in the general fund for this analysis which were \$209.7 million in FY 2020, making up 36% of all City revenues. The following sources were selected from the General Fund for in depth analysis by the OCA due to their size and potential influence on City operations because of their flexible uses: Property Tax, Sales Tax, Transient Occupancy Tax, Utility User Tax, and Documentary Transfer Tax.



Forecasting Accuracy

Through the last 5 years of significant growth, the City’s ability to forecast the upcoming year’s revenue collections has strayed no more than 9% from their estimates. See the chart to the right for specifics pulled from the [archived budget documents](#) on the City’s website.

Total City Revenue			
Fiscal Year	Actual Revenues	City Projections	% Difference
2016	\$479,746	\$487,295	-2%
2017	510,037	546,318	-7%
2018	585,572	590,236	-1%
2019	640,090	617,307	4%
2020	581,165	632,159	-9%

Revenue Analysis and Models Review

Overview

The City has a robust forecasting process. The Administrative Services Department ensures a smooth process for inputting all relevant information into Long Range Financial Plans (LRFF). The Administrative Services Department updates the financial forecasting model on an annual basis prior to the start of the budget process. These forecasting exercises inform the creation of the budget. The Department includes multiple scenarios to present to Council to inform decisions regarding the formation of the budget. The Administrative Services Department also reviews trends compared to the budget on a quarterly basis. These quarterly reviews are presented to Council.

The OCA conducted a Revenue Trends and Models Review to understand the current state of the City's forecasting practices. First, the OCA reviewed forecasting and financial models used by the City as well as the inputs those models utilize for their forecasts. This review was specific to Property Tax, Sales Tax, and Transient Occupancy Tax (TOT). These revenue sources alone account for almost three quarters of the total revenue base.

Following the review of the City's models, the OCA conducted a deeper review of revenue trends and data analysis for major tax revenue sources of the City, specifically Property Tax, Sales Tax, TOT, Documentary Transfer Tax, and Utility User Tax. The OCA reviewed the revenue sources for the historical performance which contribute to estimates of future performance. The section below describes the methodology and results of these reviews.

Methodology

In review of the City's models, the OCA first completed a data request to review all existing spreadsheets, documents, and reference materials used by the City in their economic forecasting processes. The OCA also conducted interviews and walkthroughs with members of Administrative Services to ensure full understanding of these documents. The OCA conducted independent best practice research and analysis for each of these revenue categories. Finally, the OCA documented the full understanding of current state of the models and inputs in the tables below, documented all best practices, and detailed any gaps for each revenue category.

In review of these revenue trends, the OCA reviewed economic and financial planning spreadsheets and documents provided by the City, including ACFRs, OpenGov and the internal documents already requested during the review of the models. The OCA also conducted independent research and analysis around state and national projections/economic indicators for each of these revenue categories. Finally, the OCA documented their understanding of each revenue source in the sections below. The sections are broken out by each revenue category and offer historical revenue analysis and future projections where possible.

Analysis

In completing this audit activity, there were a number of elements considered in the analysis. The OCA completed a thorough review of qualitative and quantitative analysis. In regards to qualitative information, the OCA completed interviews with City staff to walk through current-state practices and ensure understanding of documentation. Additionally, the OCA reviewed qualitative best practices from research and internal institutional expertise.

In regards to quantitative information, the OCA also completed a number of analyses and correlations to inform the audit. For all revenue sources, the OCA completed correlation calculations with the following factors:

- Unemployment (State and City)
- Personal Income (State and County)
- Inflation (Nation, State, Region)
- Consumer Price Index (Nation, State, Region)
- Population (County, City)
- Enrollment (Palo Alto Schools, Stanford)
- Permits for new construction (City)
- Mortgage Rates
- Prime Rates
- Federal Funds Rates

Results

The detailed results of the analysis of revenues are in the sections shown below. There is a section for each revenue source analyzed containing historical performance notes, historical averages, economic indicators with high correlation, and qualitative factors for consideration. Each section also contains graphs showing the revenue sources historical performance and projections based on historical averages and economic indicators. Please see the sections below for a detailed analysis of Property Tax, Sales Tax, Transient Occupancy Tax, Documentary Transfer Tax, and Utility User Tax. The results from the review of the City's models are also in the sections below¹. The review of the City's models are only for Property Tax, Sales Tax, and Transient Occupancy Tax.

Overall, the City's forecasting process is thoughtful and thorough. Additionally, the City has a number of highly skilled and sought-after advisors informing their forecasting decisions. The OCA's review confirmed that the City is consistent with industry best practices and uses reliable information. Additionally, the City's LRFF projections are aligned with Baker Tilly's recommendations for projections. This may point to Baker Tilly and the Administrative Services Department's collaboration during the preliminary analysis in March of 2020, both parties completing analysis that are complimentary to one another. Even with the alignment to best practices, there are always opportunities for improvement in the forecasting process. In particular, the OCA has two overarching recommendations for improvement:

1. *Naming conventions and workbook narratives.* In order to develop an accurate and thorough forecasting model, the City considers a number of data elements from various workbooks. The input from multiple parties is also involved. At the moment, the City doesn't have a consistent naming convention for workbooks, nor does it have narrative or instructions within the workbook itself to describe the flow of information. The City relies on the institutional knowledge of employees to understand how the forecasting information is pulled together. Without consistent naming conventions and information narratives, the City is at risk if key stakeholders in this process were to leave the organization. The OCA recommends developing a consistent naming convention and adding narrative in workbooks, including the purpose of the sheet, from where information is pulled, to where information is pushed, and with whom does the ownership of the spreadsheet lie.

2. *Assumptions and "guess-timates".* In some cases, the City uses assumptions and rough estimates to consider various scenarios such as percentage growth in situations when supporting data is sparse. This can be a necessary action if no better alternatives exist. However, the OCA learned anecdotally that some of these rough estimates are highly specific, oftentimes having estimated numbers to the hundredths place. If a certain series of inputs are rough estimates, these inputs should not be made to look as though they were calculated. Instead those estimates should be clearly labeled with a short description as to the thought process behind how the estimator arrived at that number. This will help to clarify which values were calculated at one point vs. which values are estimated without a specific calculation.

¹ FY20 numbers were used in analyses as FY21 numbers were unavailable for most of the audit period.

Property Taxes

Property Tax Overview

The City and the Bay Area's historically stable property values contribute to the City's revenues. While these property values are high, the City cannot collect on the full value of these properties based on Proposition 13's tax caps which imposes a maximum annual tax increase of 2% unless a change in property ownership or new construction. However, the revenue source is highly important to the City's fiscal health even with Proposition 13 in place.

Total Revenue: \$51.1M in FY20², \$56.6M in FY21³

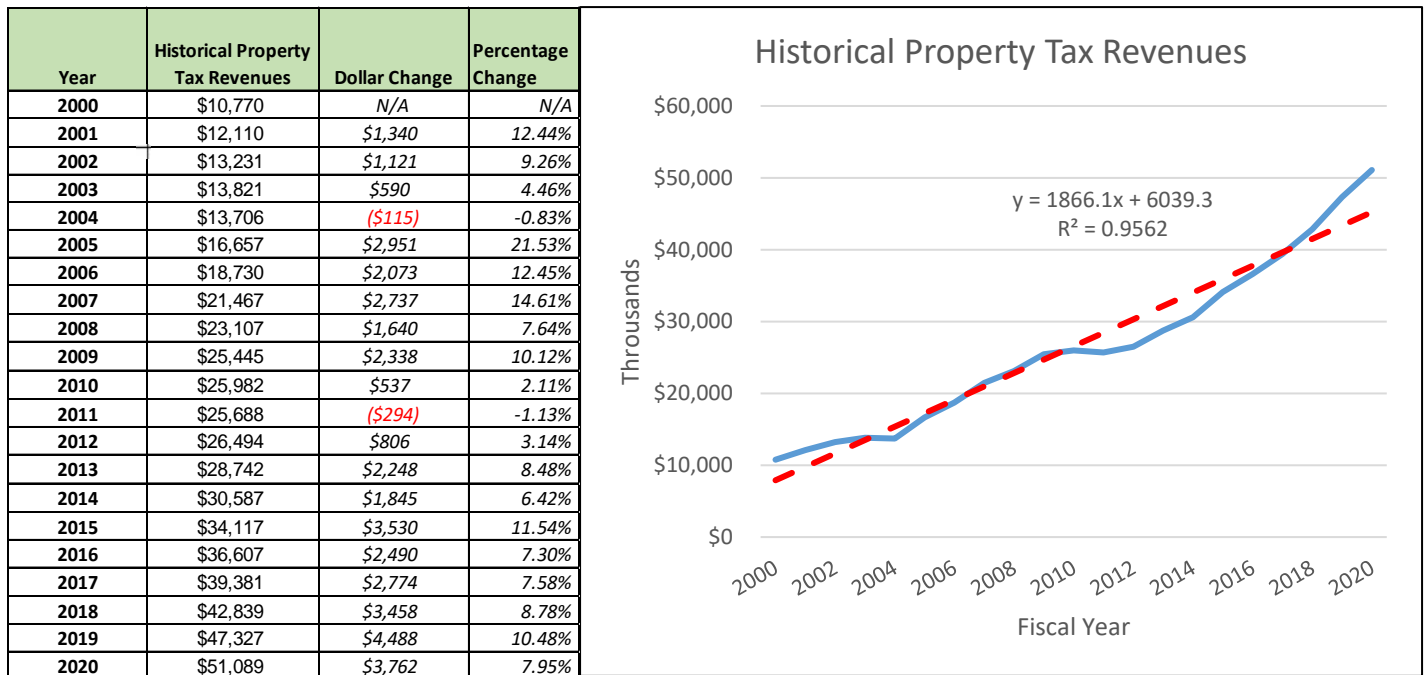
Proportion of Total Revenue: 28% in FY20, 34% in FY21

Property Tax Observations and Data Analysis

The OCA analyzed the historical performance of property tax revenue and estimating future years. The first part of the analysis consisted of reviewing historical revenue (FY 2000 – 2020) for patterns and/or anomalies and identifying their causes if possible. The second part required using historical averages and economic indicators to make future projections from FY 2021 – 2040 to help identify where revenues might trend in future years. These analytical insights were combined with less quantifiable factors to get the best possible theory of where revenues may trend in the coming years.

Historical Performance

The table and chart below display the historic property tax revenues from FY 2000 – 2020 and a trendline with the linear equation.



The information shows how property tax revenues for the City have grown rapidly over the previous 20 years. They started at roughly \$10.7M in FY 2000 and have increased to around \$51M in FY 2020. Over the years there have been large variances in year over year percentage changes ranging from -1.13% in 2011 to +21.53% in 2005.

² Palo Alto's FY20 ACFR: <https://www.cityofpaloalto.org/civicax/filebank/documents/79645>

³ Palo Alto's FY21 ACFR: <https://www.cityofpaloalto.org/files/assets/public/administrative-services/city-budgets/fy-2021-city-budget/city-of-palo-alto-acfr-fy2021-final.pdf>

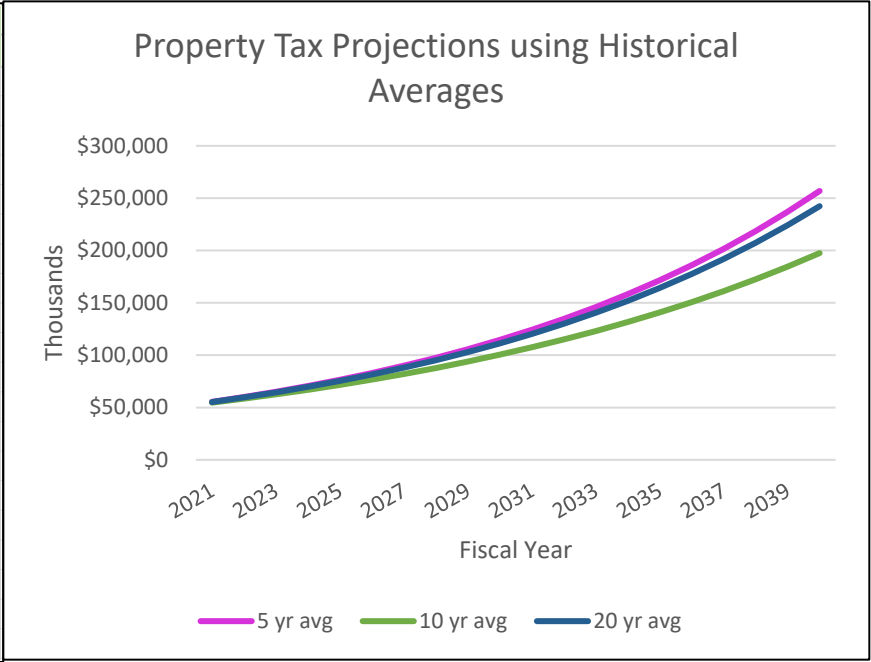
Historical Averages

The table and chart below show the property tax revenue projections for the 5-, 10-, and 20-year growth averages applied through 2040.

Growth averages:

- 5 Year: 8.41%
- 10 Year: 7.00%
- 20 Year: 8.09%

Property Tax Projections using Historical Averages			
Fiscal Year	5 yr avg	10 yr avg	20 yr avg
2021	\$55,386	\$54,663	\$55,225
2022	60,044	58,487	59,695
2023	65,094	62,578	64,527
2024	70,569	66,956	69,751
2025	76,504	71,640	75,397
2026	82,938	76,651	81,501
2027	89,914	82,014	88,098
2028	97,476	87,751	95,230
2029	105,674	93,889	102,938
2030	114,562	100,457	111,271
2031	124,197	107,485	120,279
2032	134,643	115,004	130,015
2033	145,967	123,049	140,540
2034	158,243	131,657	151,917
2035	171,553	140,867	164,214
2036	185,981	150,721	177,508
2037	201,623	161,265	191,877
2038	218,580	172,546	207,409
2039	236,964	184,617	224,199
2040	256,894	197,532	242,348



The historic averages were applied to the latest revenue collections of \$51M and projected forward for the next 20 years. The chart above shows how the collections would look if each of the averages were applied in future years.

Economic Indicators

The chart and graph below illustrate the property tax revenue projections using economic indicators to create projections. The method section below describes how the calculations were done.

Economic Indicators with High Correlation:

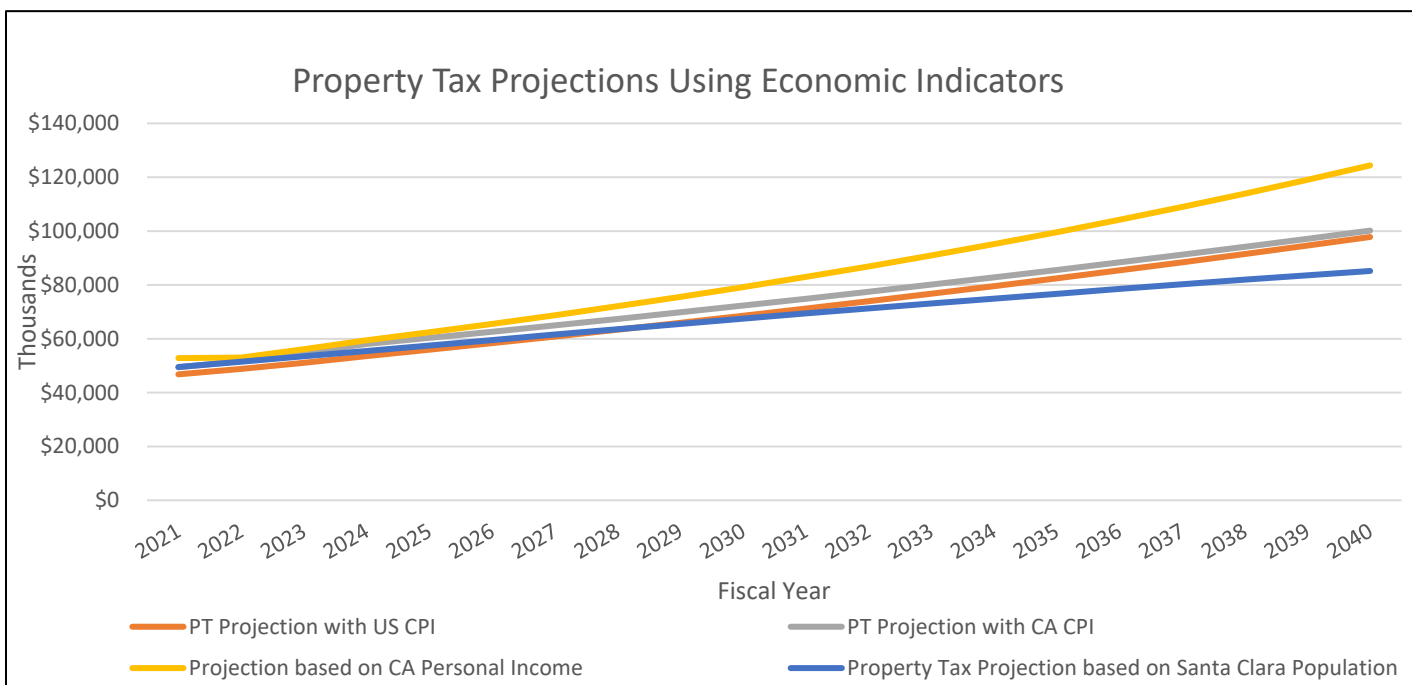
- Personal Income (99.13% for California and 98.60% for Santa Clara County)
- Consumer Price Index (CPI) (98.50% for the U.S., 96.49% for California, and 99.42% for San Francisco)
- Population (88.95% for Palo Alto and 95.77% for Santa Clara County)
- Stanford Enrollment (93.90%)

Fiscal Year	PT Projection based on US CPI	PT Projection based on CA CPI	PT Projection based on CA Personal Income	PT Projection based on Santa Clara Population
2021	\$46,789	\$49,420	\$52,825	\$49,516
2022	48,794	51,747	52,999	51,473
2023	51,067	54,716	56,128	53,515
2024	53,550	58,056	59,442	55,473
2025	55,925	60,316	62,419	57,483
2026	58,347	62,622	65,515	59,498
2027	60,818	64,973	68,734	61,560
2028	63,338	67,372	72,082	63,521
2029	65,908	69,818	75,564	65,477
2030	68,530	72,314	79,186	67,479
2031	71,205	74,859	82,952	69,400
2032	73,932	77,455	86,869	71,260
2033	76,715	80,103	90,942	73,092
2034	79,553	82,804	95,179	74,909
2035	82,448	85,560	99,585	76,702
2036	85,400	88,370	104,167	78,495
2037	88,412	91,236	108,933	80,266
2038	91,484	94,160	113,889	81,961
2039	94,617	97,142	119,043	83,566
2040	97,813	100,184	124,404	85,183

Method:

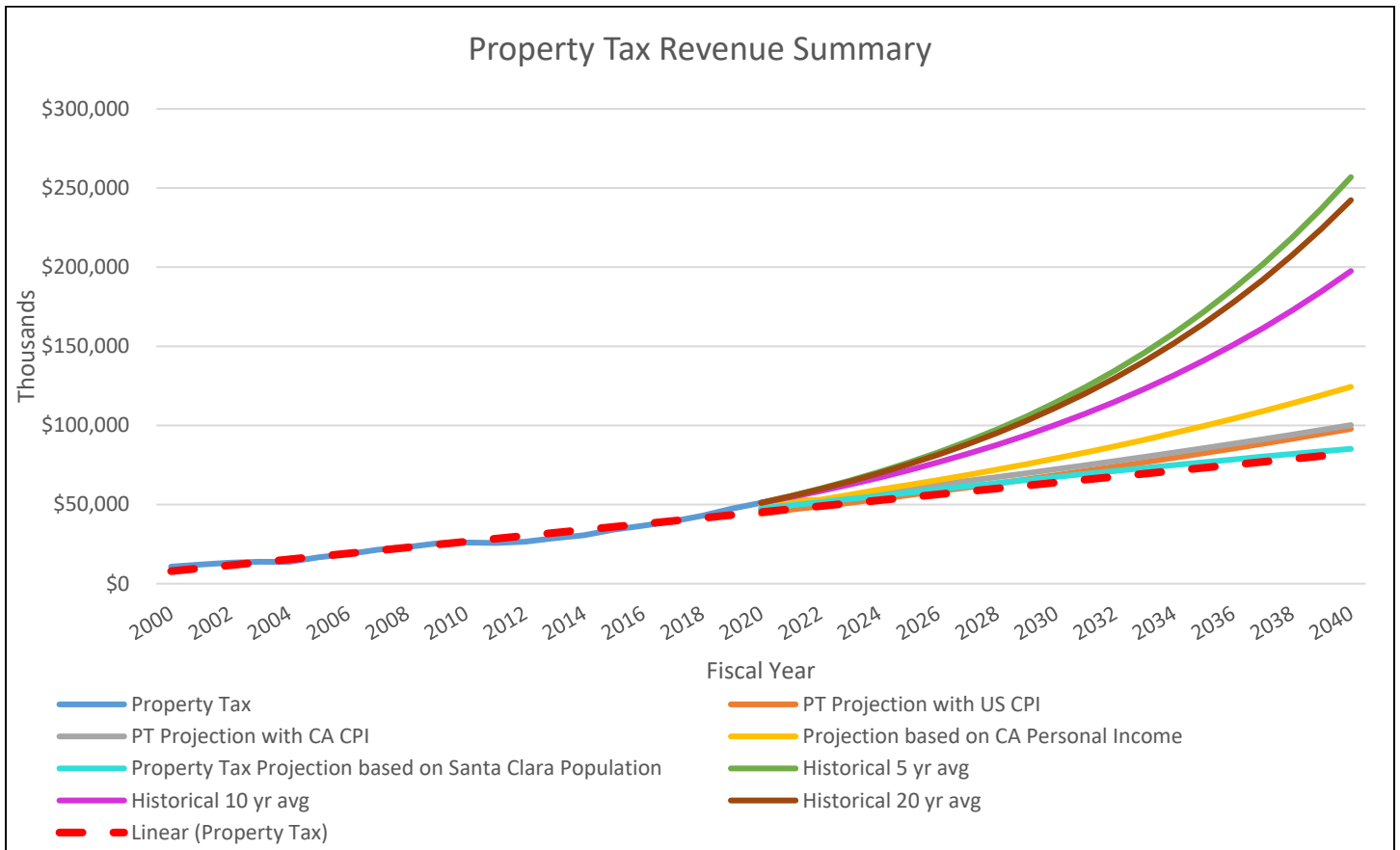
In an effort to validate the historical projections, the OCA examined economic indicators with strong correlations. If a correlation was determined to be greater than 85%, future estimates for the indicator were obtained from a reputable source and if necessary, the OCA calculated the average annual change and used that to project future years of the indicator and the revenue.

After establishing a plausible future projection with the economic indicator, the OCA completed a regression analysis between the historical tax revenue collections and historical economic indicator data. The OCA then used the regression to calculate the linear equation and project out possible property tax revenues.



Property Tax Interpretation

The graph below is a combination of the historical property taxes, projections made from historical averages, and economic indicators.



The property tax revenues for the City have performed extraordinarily well over the last 20 years. They have grown steadily with a 20 year average of 8.09% and have been fairly insulated during times of national economic decline. This phenomenon proved true again again during the COVID-19 pandemic, where property values remained high and even increased in some categories (Economic Resiliency Review). In fact there have only been two years where revenues declined, from FY 2003-2004 and FY 2010-2011.

Looking purely at the historical average projections it shows an optimistic future. On the high end, the 5 year average increases collections upwards of \$250M in FY 2040 and on the low end, the 10-year average projects collections around \$200M by then. The rate of growth property tax revenues have experienced in the City appears to be an exponential curve when projected forward. However, it is not likely revenues will continue to grow at the historical rates for another 20-years. Contributing factors being, the City has neared it's limit on population growth without an increase in density, gaining only 6,500 residents since 2000, and there are current concerns of corporate headquarters moving out of state (Hoover Institute)⁴.

⁴ Hoover Report: <https://www.hoover.org/research/why-company-headquarters-are-leaving-california-unprecedented-numbers>

Property Tax Current State Model Description

Property taxes make up the largest portion of the City's General Fund revenues and approximately 25% of total revenues (staff report⁶); fortunately, they were not as negatively impacted by the COVID-19 pandemic as sales tax and TOT. The City expects property tax revenues to grow around 10.2% from FY21 to FY22 and is projecting consistent property tax revenues for the next 3 years.

The following factors determine property tax revenue; net assessed values, transfer of ownership, new construction/declines, and Proposition 13 inflation adjustment. In determining the various scenarios for property taxes the City calculates their base projection which takes into account the major factors outlined. Once a baseline is established, the Treasury Department applies a growth factor and summarized.

Due to the unique economic situation COVID has created, the City crafted several scenarios for their revenue projections. To determine the various scenarios for Property Tax, the City determines the base projections for the revenues in the workbooks described above, and adjusts the appropriate multipliers to reflect the expected revenues in a 2-3 year recovery period, 3-5 year recovery period (base), and 5-10 year recovery period. These scenarios were presented to Council along with Sales and TOT projections.

The City uses the following inputs when forecasting Property Taxes:

- 1) Tax rolls received from the County Controller's Office
- 2) New growth and known decreases, including Proposition 13
- 3) Historical data on prior year assessed values and collections
- 4) Regional data on property sales and values (including a review of Zillow)
- 5) Property tax consultants input

Property Tax Industry Best Practices

The City's property tax projection methods align with what we see with other Baker Tilly clients. They rely heavily on historical data, current tax rolls from the County, and upcoming changes within the local market. Our review confirmed that the City is using reliable information and their practices are consistent with other communities.

Property Tax Observations and Recommendations

In our review, the OCA attempted to find correlations between assessed values and several factors such as the 30-year mortgage rates, Prime Rates, and Federal Funds rates. The strongest correlations the OCA found were between the City's total assessed values and both the Santa Clara County Per Capita Personal Income and California Total Personal Income. There is 99% correlation between total AVs and California's total personal income followed closely by a 98% correlation between the total assessed value and Santa Clara County's per capita personal income.

Based on these correlations, the OCA ran a preliminary regression analysis which showed a projected decrease in total assessed values in 2022 before rebounding back in 2023 and 2024. After running the regression analysis, we looked at the FY16 Financial Report⁵ which contained historical information back through the Great Recession, which showed total AVs remaining flat from 2009-2013. Taking all of that into account, our prediction is that AVs will remain flat for the next 3-4 years and the City's base case reflects that outcome.

The most conservative long term assumption, however, would be a projection of linear growth into future years. The conservative assumption appears to align closely to the projections shown in the Long Range Financial Forecast (LRFF) dated December 7th, 2021.

⁵ Palo Alto's FY16 ACFR: <https://www.cityofpaloalto.org/civicax/filebank/documents/54744>

Sales Tax

Sales Tax Overview

Palo Alto has a number of factors drawing visitors to the City. Similar to TOT, those in Palo Alto for business, education, or leisure contribute to the City’s revenues through the sales tax associated with their spending.

Total Revenue: \$30.6M in FY20, \$29.1M in FY21

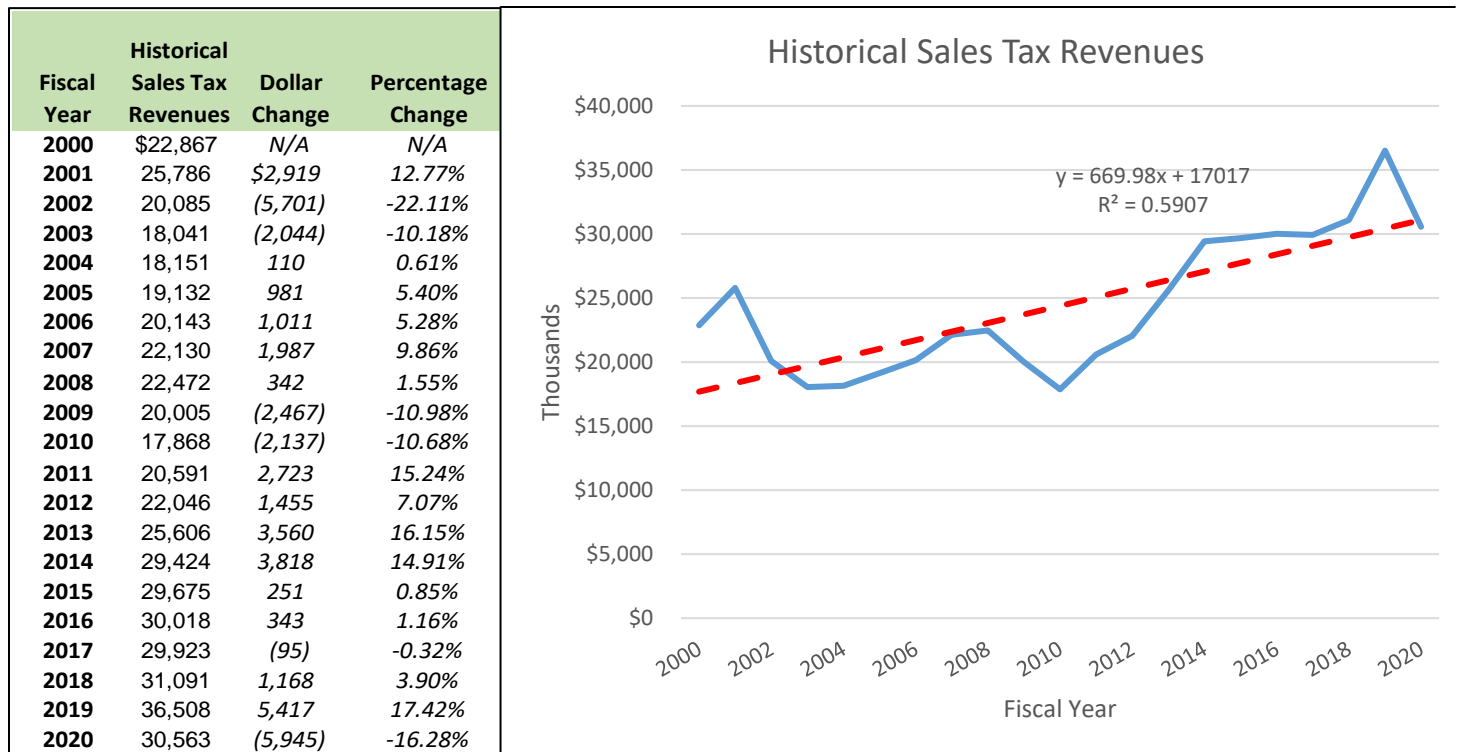
Proportion of Total Revenue: 17% in FY20, 17% in FY21

Sales Tax Observations and Data Analysis

The OCA performed an analysis of the historical performance of sales tax revenue and estimated future years. The historical analysis required examination of past performance to gain an understanding of the revenue volatility, factors creating noticeable change and reactions to economic downturns. In addition, the OCA used economic indicators to estimate revenue out through FY 2040.

Historical Performance

The table and graph below depict the historical sales tax revenues from FY 2000 – 2020 and shows a trend line with the linear equation.



Sales taxes can be a volatile revenue source and the City’s revenues are no exception. In the last twenty years there have been year over year percentage changes as low as -22.11% (FY 2001-2002) and up to +17.42% (FY 2018-2019). The revenues in FY 2000 were \$22.8M and have increased to \$30.5M in FY 2020. That is roughly \$8M in growth at a rate of 1.46% annually.

Historic Average Projections

The chart and table below depict the sales tax revenue projected out through FY 2040 using historic averages.

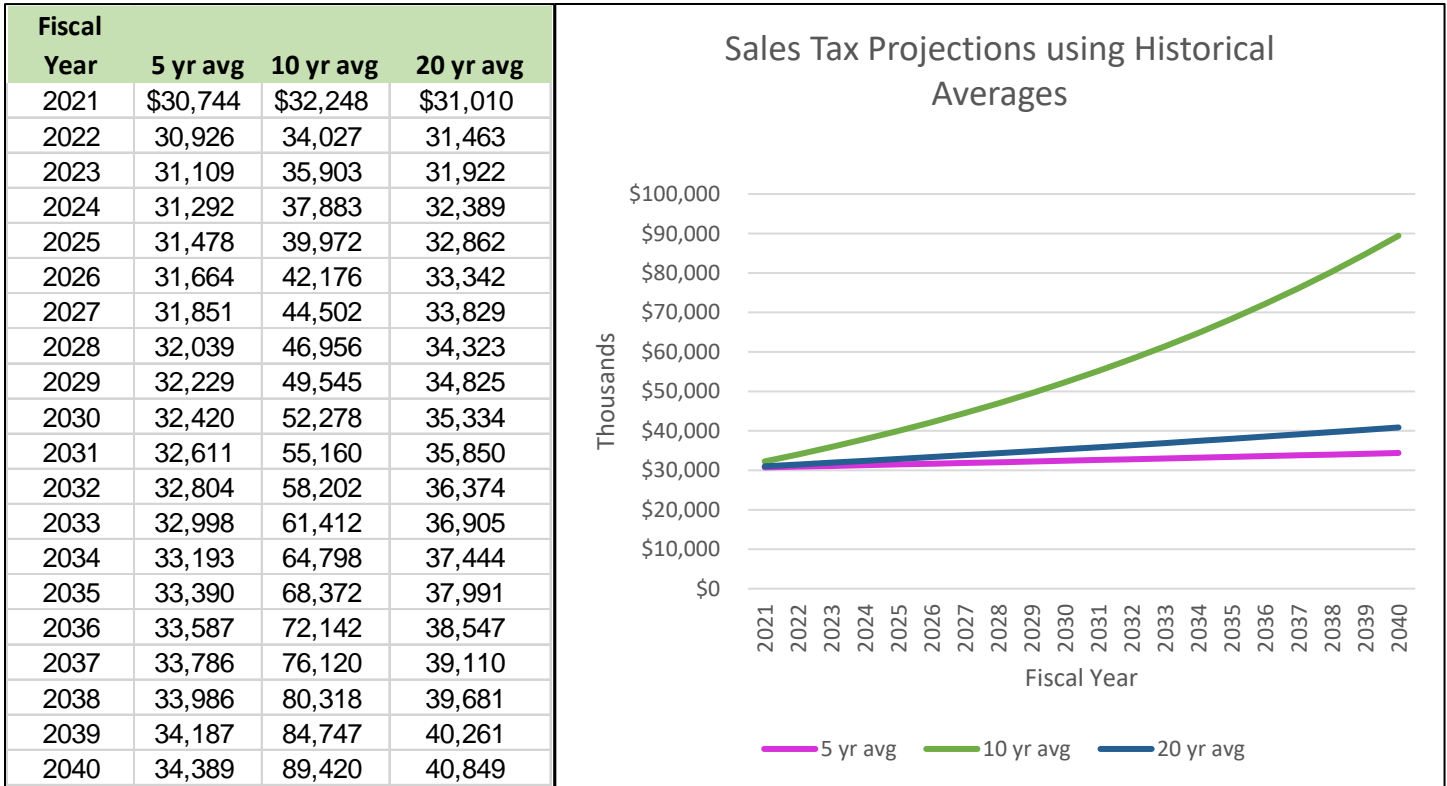
Growth averages:

4 Year: 5.32%

5 Year: 0.59% (you can see pandemic hit hard when comparing 4 yr. and 5 yr. averages)

10 Year: 5.51%

20 Year: 1.46%



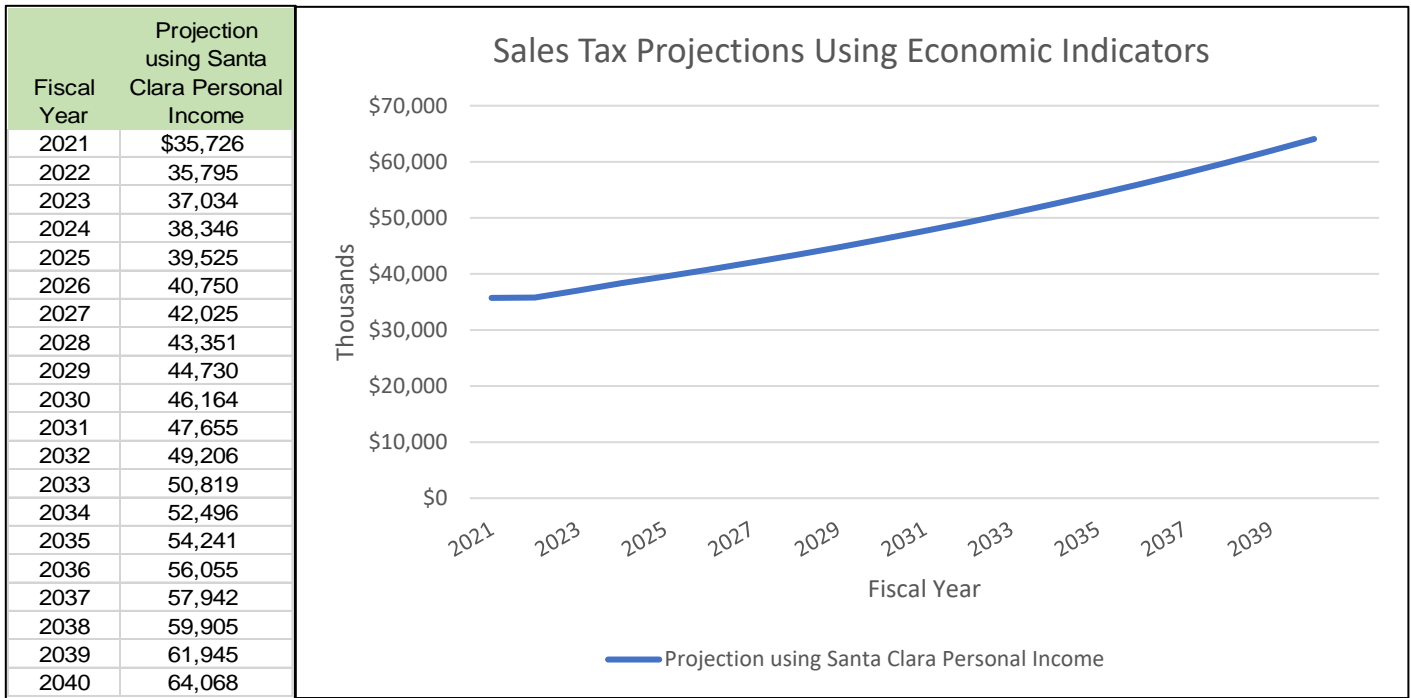
The historical averages of the revenue show that the 5-year average contains the large drop in revenues described above, making it a mere 0.59%. When applying the annual averages, the 10-year average is projecting revenues to be around \$90M in FY 2040, whereas the 5- and 20-year averages paint a picture of roughly \$40M in revenue. The 10-year average may be slightly skewed because its first year of collections is after a large dip, seemingly linked to the 2008 market crash. Therefore, the average captures this rebound and only one major year of decline due to the COVID-19 pandemic.

Economic Indicators

The table and graph below display the sales tax revenue projections using economic indicators with a high correlation. The calculations were done using the same method described in the Property Tax section.

Economic Indicators with High Correlation:

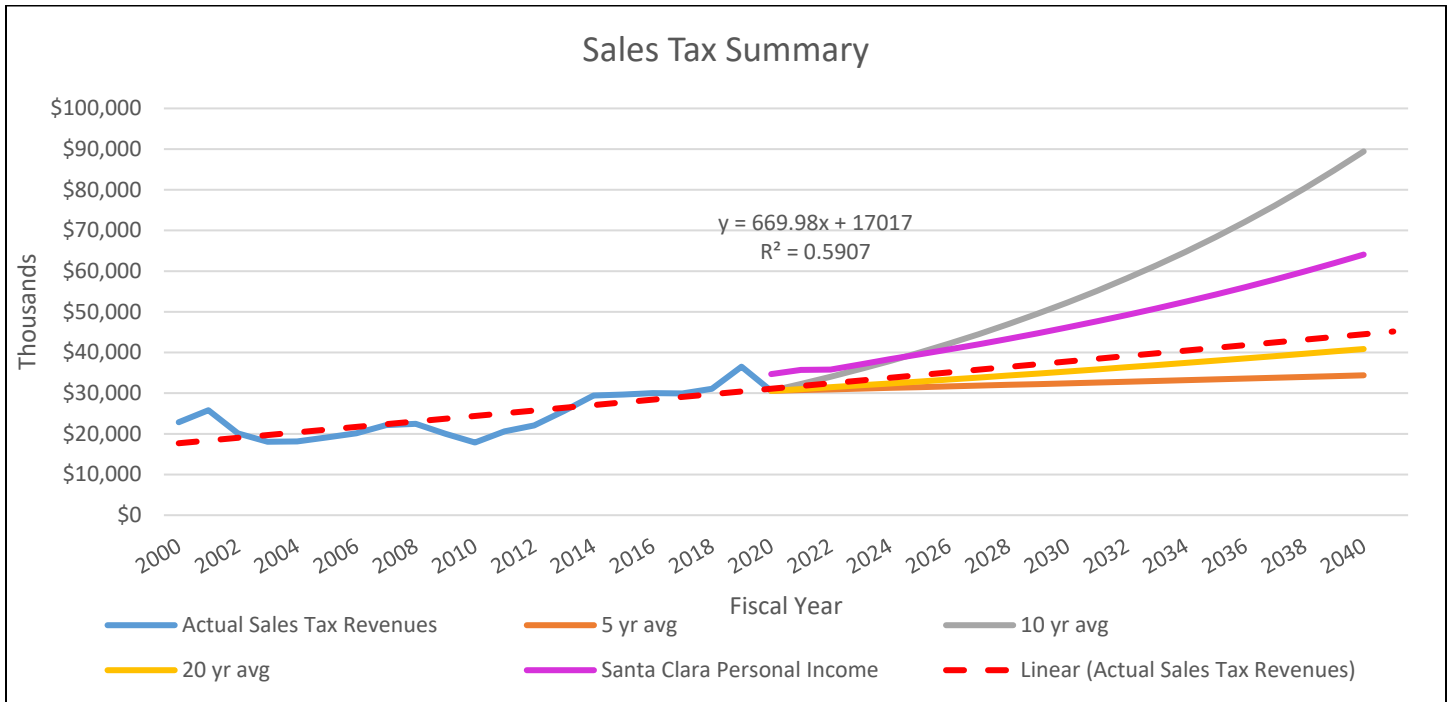
- Personal Income (Santa Clara County)
- Stanford Enrollment
- TOT Revenues (Correlation >85%)



The only projectable economic indicator with a high correlation is Personal Income for Santa Clara County. The two have an R² value roughly 93% which is enough to say there is a correlation but not enough for total confidence in their relationship moving forward. The OCA projected out the Personal Income for Santa Clara County using growth percentages for 2021-2024 obtained from CA States Personal income projections published by the California Department of Finance in the 'California Economic Forecast MR 2021-2022'. A growth factor of 4% was then applied to years 2025-2040.

Sales Tax Interpretation

The graph below is a combination of the historical sales taxes, projections made from historical averages, and economic indicators.



The OCA looked at all data sources made available by the City and outside organizations to help interpret the meaning of the data trends identified above. Historical data provided by the City shows that during times of national economic recession (Dotcom bubble, 9/11, and 2008 housing crash) sales tax revenue falls off drastically with -10% to -20% reductions and takes roughly 3-5 years to recover.

The COVID-19 pandemic appears to have continued this trend as it hit sales tax hard with a revenue reduction of -16.28% when comparing FY 2019 to 2020. Much of this can be attributed to the forced business closure, work from home policies, and other new social norms the pandemic introduced. While there may be no way to tell when or what might cause an economic recession, knowing the range of revenue decrease (10%-20%) can help the City budget for worse case scenarios.

Continuing to use the context learned during data analysis, the OCA created the graph above, combining historical sales tax revenues, projections using historical averages, and economic indicators. The Santa Clara Personal Income projection shows a more aggressive growth than the 5- and 20-year averages and less growth than the 10 yr. average. As stated above, the 10-year average may be skewed due to the timing of recessions and rebounds while the 5-year average is affected by the COVID-19 Pandemic. Additionally, while the details of the information is confidential, the 10-year average includes substantial Sales Tax changes from a small number of businesses, contributing to the skewed data according to the Administrative Services Department. The City's LRFF estimates \$43 million in sales tax revenues in FY 2032, which is between the projections using Santa Clara Personal Income and the 20-year average.

Sales Tax Current State Model Description

Sales Tax receipts have taken a significant hit because of COVID-19 and the health regulations implemented as a direct result. The total year over year change from 2019 to 2020 was -16.3% and an addition decrease of -4.7% in 2021. Recent sales tax revenues point to the yearly revenue being \$1.5 million, or 5.2%, over 2021 actuals.

The City uses several major factors in their sales tax projections; actual collections received, tax consultant provides a report, previous recessions, unemployment, and local economists.

First, the City receives monthly sales tax information from the State. Their sales tax consultant also provides a report summarizing monthly revenues and providing future projections. The projections are inputted by Treasury and OMB factors in more locally focused insights to get an estimate for current year collections. Once the current year base scenario is established, a growth multiplier is added using inputs described above. Finally, the data is cleaned up and becomes the deliverable for Council.

To determine the various scenarios for sales tax, the City determines the base projections for the revenues in the workbooks described above, and adjusts the appropriate multipliers to reflect the expected revenues/operating margins in a 2-3 year recovery period, 3-5 year recovery period (base), and 5-10 year recovery period. These scenarios were presented to Council along with TOT and Property Tax projections.

Inputs considered when forecasting Sales Tax revenues include:

- 1) Consultant report - MuniServices 2020Q3
- 2) Data from the previous recession
- 3) Unemployment rates
- 4) State collections - sent monthly
- 5) Input from local economists

Sales Tax Industry Best Practices

The City's sales tax projection methods align with what we see with other Baker Tilly clients. They rely heavily on historical data, monthly sales tax revenues, and upcoming changes within the local market. Our review confirmed that the City is using reliable information and their practices are consistent with other communities.

Sales Tax Observations and Recommendations

During our review, we looked for correlations between historical sales tax revenues and the following data: Unemployment rates, Santa Clara County Per Capita Personal Income, California Total Personal Income, and historical TOT taxes. The strongest correlations came from Santa Clara County per capita income 85.3%, California total personal income 83.6%, and historical TOT revenues 82.0%. While none of these correlations are in the 90% percentile, they could give insight on future years by leveraging projections from reputable state and national entities to check for consistency with current models. Since TOT and Sales Tax have a reasonably strong correlation, when modeling future years the City may check that both revenue projections are aligned in future years.

As far as historical averages, the 1.46% 20-year average is a conservative estimate, showing \$40M in revenue by FY 2040. The Santa Clara Personal Income splits the middle between the 10-year average and the 20-year average with around 3.8% growth. The City's LRFF estimate of \$43 million in sales tax revenues in FY 2032 is plausible based on our analysis.

Transient Occupancy Tax

Transient Occupancy Tax Overview

The City has a number of travelers for local businesses/corporations, Stanford University affiliates, and leisure. These travelers contribute to a large portion of the City's revenue through the Transient Occupancy Tax (TOT).

Total Revenue: \$18.6M in FY20, \$5.2M in FY21

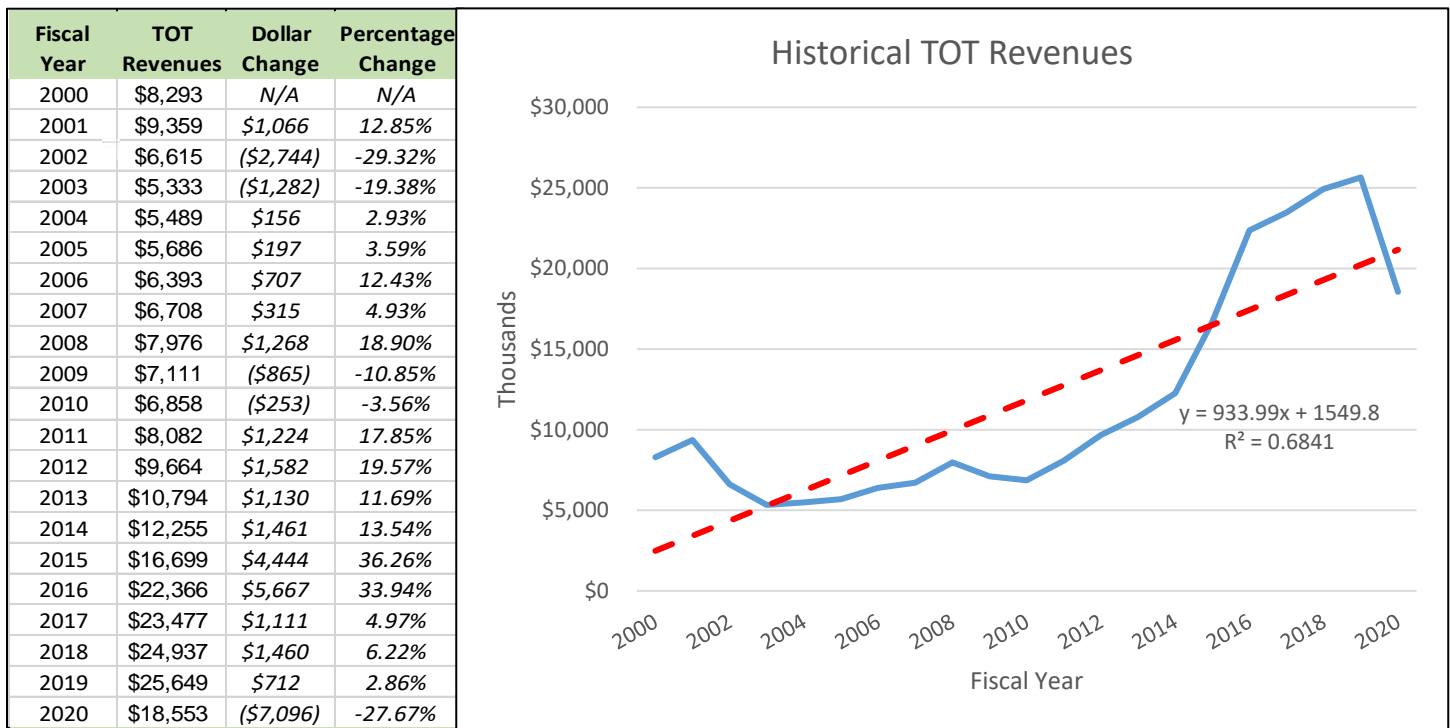
Proportion of Total Revenue: 10% in FY20, 3% in FY21

Transient Occupancy Tax Observation and Data Analysis

The OCA analyzed the historical performance of TOT revenues and estimated future years. The historical analysis required examination of past performance to identify patterns in the data as well as irregularities. The future analysis consisted of identifying highly correlated economic indicators and using them to project out revenues through fiscal year 2040. In both the historical and future analysis, qualitative factors are considered, and their potential impacts explained.

Historical Performance

The table and graph below displays the historical Transient Occupancy tax revenues from fiscal year 2000 – 2020 and includes a trend line with the linear equation.



Transient Occupancy Tax Revenues for the City have had an interesting plateau effect over the past twenty years. In 2000 the City collected \$8.2M in revenues which dropped down to \$5.3M by 2003. After that initial decline it took until 2011 for the revenues to get back around the \$8M mark. After 2011 the revenues increased dramatically with year over year increases north of 36%. This was in part because of passed ballot measures to increase the TOT rates in 2014 and 2018. The revenue collections plateaued again after 2016 where they grew around 4% per year until the pandemic took full effect creating a -27.7% reduction (2019-2020).

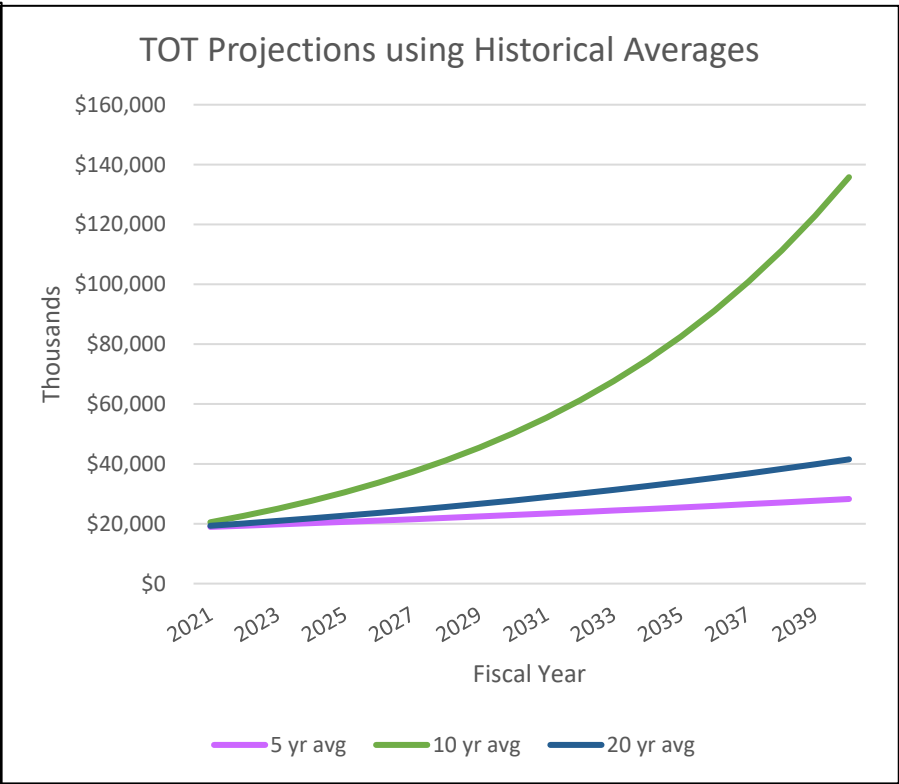
Historic Average Projections

The chart below shows that 5-, 10-, and 20-year averages applied to the TOT revenues for the next 20 years.

Growth averages:

- 5 Year: 2.13%
- 10 Year: 10.46%
- 20 Year: 2.13%

Fiscal Year	5 yr avg	10 yr avg	20 yr avg
2021	\$18,948	\$20,494	\$19,315
2022	\$19,351	\$22,639	\$20,109
2023	\$19,763	\$25,008	\$20,935
2024	\$20,183	\$27,625	\$21,795
2025	\$20,613	\$30,516	\$22,690
2026	\$21,051	\$33,709	\$23,622
2027	\$21,499	\$37,236	\$24,593
2028	\$21,957	\$41,133	\$25,603
2029	\$22,424	\$45,437	\$26,655
2030	\$22,901	\$50,192	\$27,750
2031	\$23,389	\$55,444	\$28,890
2032	\$23,886	\$61,245	\$30,077
2033	\$24,395	\$67,654	\$31,313
2034	\$24,914	\$74,734	\$32,599
2035	\$25,444	\$82,554	\$33,938
2036	\$25,985	\$91,193	\$35,333
2037	\$26,538	\$100,735	\$36,784
2038	\$27,103	\$111,277	\$38,295
2039	\$27,680	\$122,921	\$39,869
2040	\$28,269	\$135,784	\$41,507



The 10-year average is abnormally high as that is when the revenues increased dramatically. The OCA believes the 5- and 20-year averages are more reliable estimates for long term projections.

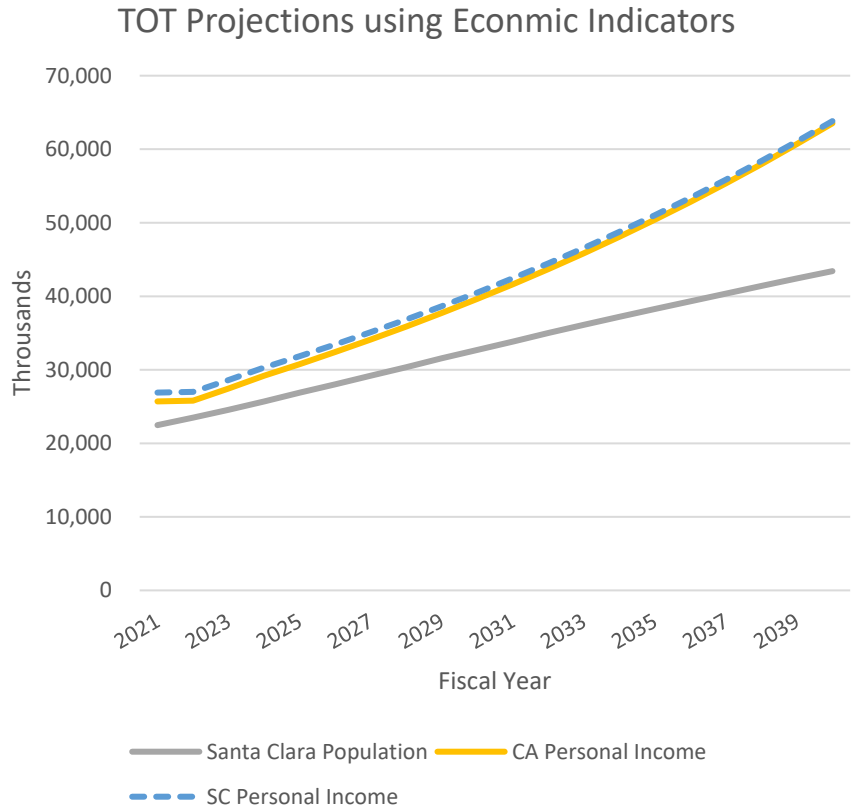
Economic Indicator Projections

The following graph depicts the TOT revenues projected through 2040 using highly correlated economic indicators.

Economic Indicators with High Correlation:

- Personal Income (California and Santa Clara County)
- Population (Palo Alto)
- Stanford Enrollment

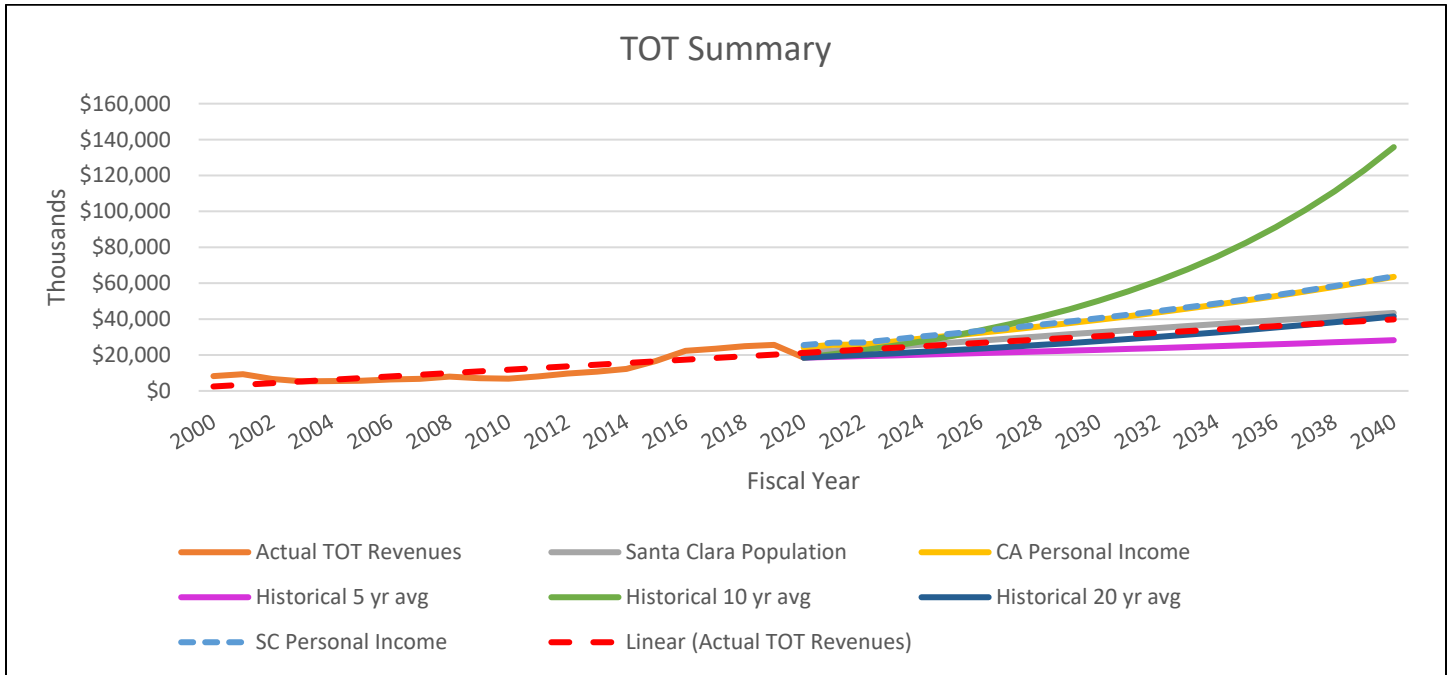
Fiscal Year	Projections		
	Santa Clara Population	CA Personal Income	SC Personal Income
2021	\$22,475	\$25,701	\$26,903
2022	\$23,501	\$25,793	\$26,992
2023	\$24,556	\$27,447	\$28,606
2024	\$25,694	\$29,198	\$30,316
2025	\$26,881	\$30,771	\$31,851
2026	\$28,019	\$32,407	\$33,448
2027	\$29,188	\$34,109	\$35,109
2028	\$30,360	\$35,878	\$36,836
2029	\$31,558	\$37,719	\$38,632
2030	\$32,699	\$39,633	\$40,500
2031	\$33,836	\$41,623	\$42,442
2032	\$35,000	\$43,693	\$44,463
2033	\$36,117	\$45,846	\$46,564
2034	\$37,198	\$48,085	\$48,749
2035	\$38,263	\$50,413	\$51,022
2036	\$39,319	\$52,835	\$53,386
2037	\$40,362	\$55,354	\$55,844
2038	\$41,405	\$57,973	\$58,400
2039	\$42,434	\$60,697	\$61,059
2040	\$43,419	\$63,530	\$63,824



There were three economic indicators used to project out TOT revenues through 2040, California Personal Income, Santa Clara County's Personal Income and Santa Clara County's Population. All three showed higher revenues than the 20-year average with the population being the closest. The most likely scenario is still revenue somewhere around the \$30-\$40M revenue mark in 2040.

Transient Occupancy Tax Interpretation

The following chart displays a combination of the historical TOT revenues and projections using historical averages as well as economic indicators.



The OCA used the data provided by the City and outside sources to get as wide of a view as possible for TOT revenues and possible influencing factors. When looking at the historical revenue graph, it is hard to miss how the COVID-19 pandemic affected the TOT revenues with a -27.7% decline from 2019-2020. When looking at other major economic downturns the revenues also dipped, Dotcom bubble showed a -22.11% decline (FY 2001-2002) and the housing market crash showed a -10.85% decline (FY 2008-2009). Although TOT revenues declined in both scenarios, revenues took 6-7 years to rebound after what is presumed to be the dotcom bubble and only took two years to rebound after 2008. Unlike the City's Sales Tax, which has historically taken 3-5 years to rebound post-recession, the TOT has had different recovery lengths making it difficult to say how TOT will bounce back after the pandemic since its effects are still lingering.

Transient Occupancy Tax Current State Model Description

The TOT was heavily impacted by the COVID-19 pandemic. The City assumes that TOT revenue will continue to suffer until the virus is under control and travel resumes. In particular, the reduction of "business and other non-leisure travel is a driving impact" (Staff Reports)⁶.

TOT revenue is comprised of four factors; the number of hotels in the City, the number of rooms at each hotel, the average occupancy of rooms, and the average room rate. Applying a 15.5% TOT to those four factors makes up the revenue the City receives from these hotels. The City is expecting TOT to be 57% below pre-pandemic levels in FY22, which is up from FY21 actuals and but still 80% below pre-pandemic levels (prior to FY21). As reported by hotels, room rates have decreased by nearly 50% and occupancy rates have decreased from 80% to 44%.

When forecasting TOT into the future, the City uses a number of factors to determine likely scenarios. First, the City assesses the current state of TOT. This includes detailed information on each hotel, including historical data and information on room rates, occupancy rates, and number of rooms. The City then includes assumptions and analyses from the Treasury department.

Treasury considers a few factors, including historical trends of TOT, regional trends of TOT, and behaviors of tax revenues after past recessions. Treasury's analysis is used to create the City Council Staff Report⁶ and Presentation⁷ with various scenarios of economic recovery.

To determine the various scenarios for TOT, the City determines the base projections for the revenues and adjusts the appropriate multipliers to reflect the expected revenues/operating margins in a 2-3 year recovery period, 3-5 year recovery period (base), and 5-10 year recovery period. These scenarios were presented to the Council along with Sales and Property Tax projections. In summary, the inputs considered when forecasting TOT are the following:

- 1) Historical data of number of hotels, number of rooms, average room rate, and average occupancy rate
- 2) Future hotels according to City Planning
- 3) Historical recovery data from the past recessions
- 4) Regional (Northern California) hotel/motel trends
- 5) Discussions with economists on potential future trends in travel

Transient Occupancy Tax Industry Best Practices

Traditionally, the City's forecasting methods are directly in-line with what we've seen with past clients. The analysis relies heavily on historical data, projected growth in rooms, and adjusting for economic conditions. Throughout our research, we also saw similar methods being used in neighboring communities such as Mountain View, San Mateo, and others. However, through our research, we've also identified additional factors that are worthy of consideration. One such factor is being used by the City of San Jose⁸. While much of San Jose's TOT forecasts are similar to the City's methods, San Jose also considers the activity and growth of local events/conventions in their TOT forecasting.

Accounting firm, Ernst and Young ("EY"), also wrote a report about forecasting hotel trends in the age of COVID⁹. Their thesis discussed the importance of the type of travel a community attracts.

For example, the pace of recovery for a highly professional community will vary from a tourist destination. EY also considers the national unemployment rate as an indicator of travel levels as well as the rise in virtual alternatives.

CBRE writes a report¹⁰ similar to EY, and both reports agree that the hotel quality matters a great deal in forecasting. In CBRE's analysis, luxury hotels are seeing less fluctuation than mid-segment or budget hotels. Finally, Moody's, the credit

⁶ 2/8/21 City Council Staff Report: <https://www.cityofpaloalto.org/civicax/filebank/documents/80088>

⁷ 2/8/21 City Council Presentation: <https://www.cityofpaloalto.org/civicax/filebank/documents/80198>

⁸ San Jose's Five Year Forecast: <https://www.sanjoseca.gov/home/showpublisheddocument?id=69842>

⁹ EY Hotel Forecasting Report: https://www.ey.com/en_us/real-estate-hospitality-construction/how-to-better-forecast-recovery-in-the-hotel-industry

¹⁰ CBRE Hotel Forecasting Report: <https://www.hotelmanagement.net/operate/cbre-adjusts-us-hotel-industry-forecast#:~:text=According%20to%20the%20recently%20released,during%20the%20year's%20second%20half.>

rating agency, produces a report on their outlook on hotels¹¹. They believe that leisure and personal travelers will be the first to return. They also believe that business travelers will lag on a macro level, but that it will depend greatly on industry. Moody's in general is more on the pessimistic side, believing that a full recovery within 3-5 years is unlikely.

In summary, additional inputs found in research not captured in the City's forecasting process are as follows:

- 1) Size and frequency of local conventions and events
- 2) National unemployment
- 3) Hotel market segments and property-specific attributes
- 4) Demographics of travelers

Transient Occupancy Tax Observations and Recommendations

In regards to forecasting of revenue trends, the OCA concluded that Santa Clara Population, 20-year average, and the linear trend line are a conservative forecast. Those projections are all grouped very closely together and have a reasonable growth pattern. The difficulty is predicting how quickly the revenue will recover to the pre-pandemic levels especially with a varied recovery pattern from historic recessions.

The LRFF dated December 7, 2021, shows a 5-6 year recovery period (FY 2019 – 2025), which is in between the recovery periods for the previous economic downturns, and estimates \$37.2 million in revenues for FY 2032. These estimates are just slightly higher than the OCA's most reasonable estimates described above, which show revenues of \$30M - \$35M for FY 2032.

The OCA also recommends considering the four factors listed above as additional forecasting inputs, namely; size and frequency of local conventions/events, national unemployment, hotel market segments and property-specific attributes, and demographics of travelers. While some of these inputs may not be possible due to lack of data or lack of applicability to the City, the OCA recommends considering these other inputs to determine if improvements to forecasting can be made. Additionally, where data is available, the City can determine correlations between various factors to determine if there is a relationship between TOT and a given input. Finally, in some cases, the City may find that these factors do not apply specifically to Palo Alto and may disregard certain factors in future forecasts. For example, while San Jose includes analysis around local conventions/events, this is also because they have a much larger convention center. If Palo Alto does not have the same ability to gather data around local conventions/events, it may not be a factor that can be included in a broader analysis.

The City should also reach out to larger hotels to understand if they forecast as well as large businesses and Stanford University to understand their expectations for conferences, business travel, student activity, etc. If a relationship with Stanford to provide such information does not exist, this would be a useful relationship to develop for future analyses that may also benefit the University.

¹¹ Moody's Hotel Industry Assessment Report: "Consumer comfort vital for travel, tourism dependent sectors' eventual recovery"

Documentary Transfer Tax

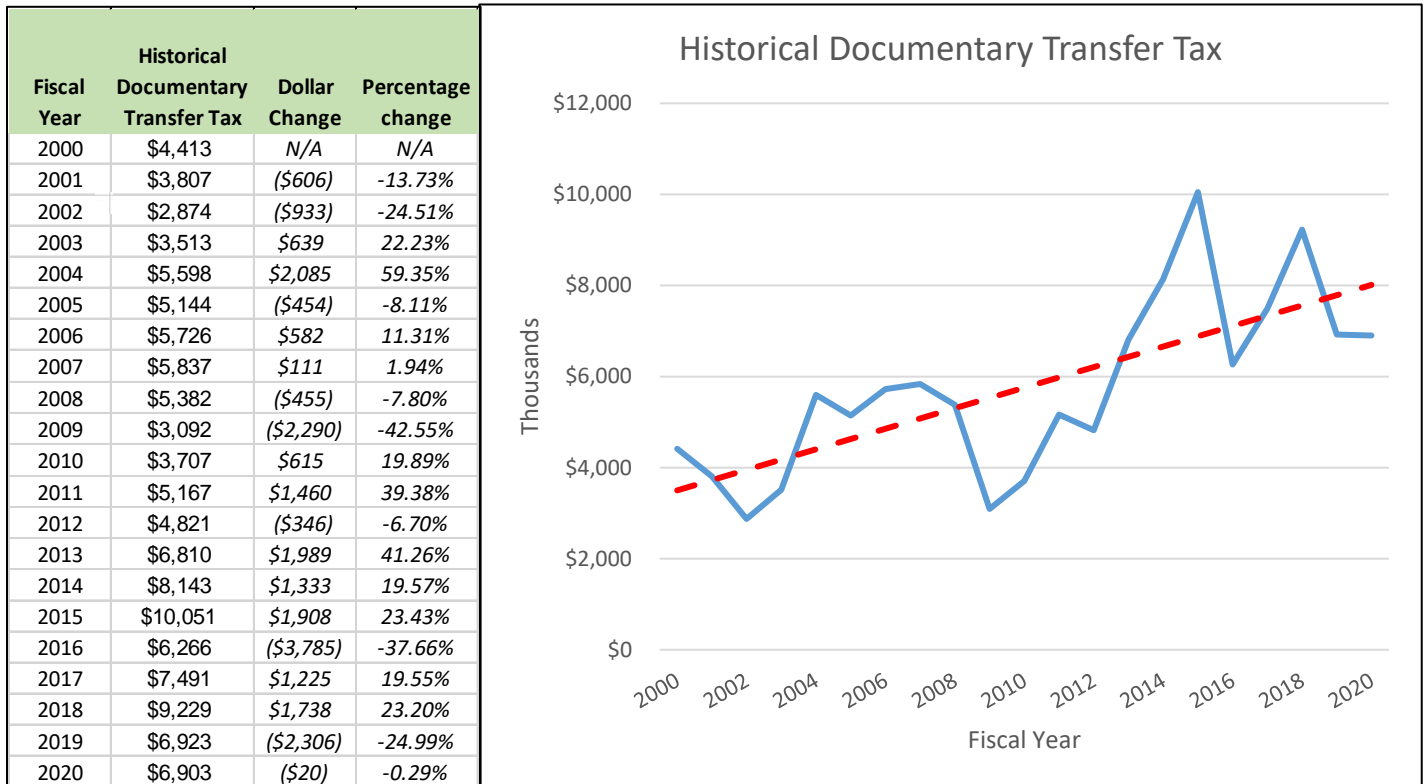
Documentary Transfer Tax Overview

The OCA analyzed the Documentary Transfer Tax (DTT) revenues and provided estimates of future performance based on historical averages. The analysis shed light on the volatility of the revenue source and proved difficult to find any correlating economic indicators that could be used to project future revenues.

Documentary Transfer Tax Observations and Data Analysis

Historical Performance

The chart below depicts the historical Documentary Transfer Tax performance from 2000 – 2020 and includes a trend line with the linear equation.



Documentary Transfer Tax revenues have been very volatile over the last 20 years. Swings ranging from -42.55% to +59.35%. However, the overall growth from 2000-2020 was only \$2.5M, which averages out to around 2.26% annually.

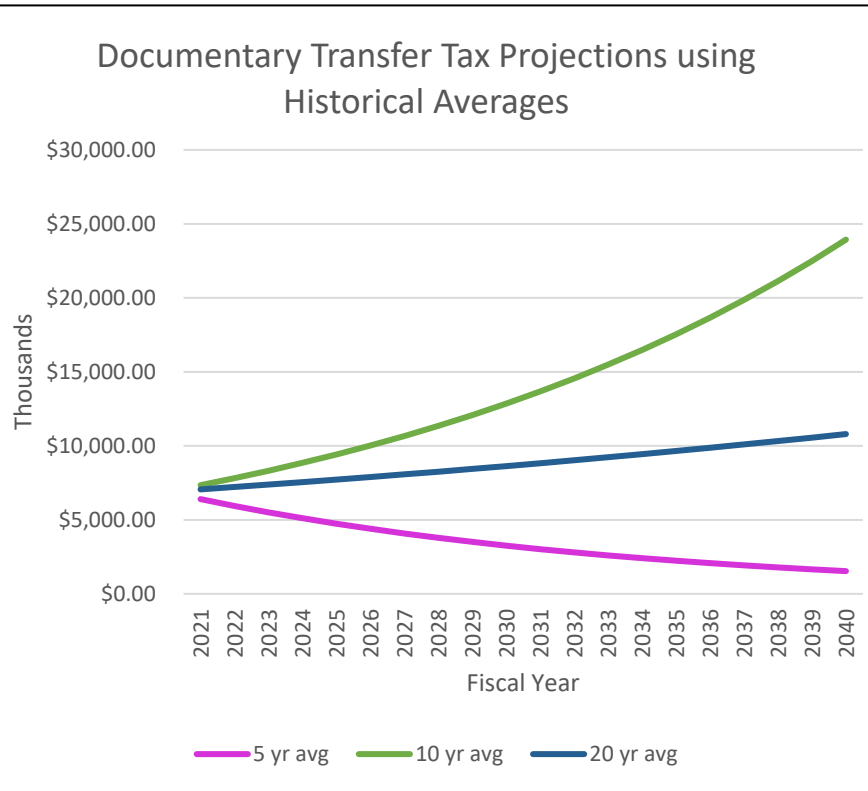
Historical Average Projections

The graph below displays the DTT revenue projections using historical averages.

Growth averages:

- 5 Year: -7.24%
- 10 Year: 6.41%
- 20 Year: 2.24%

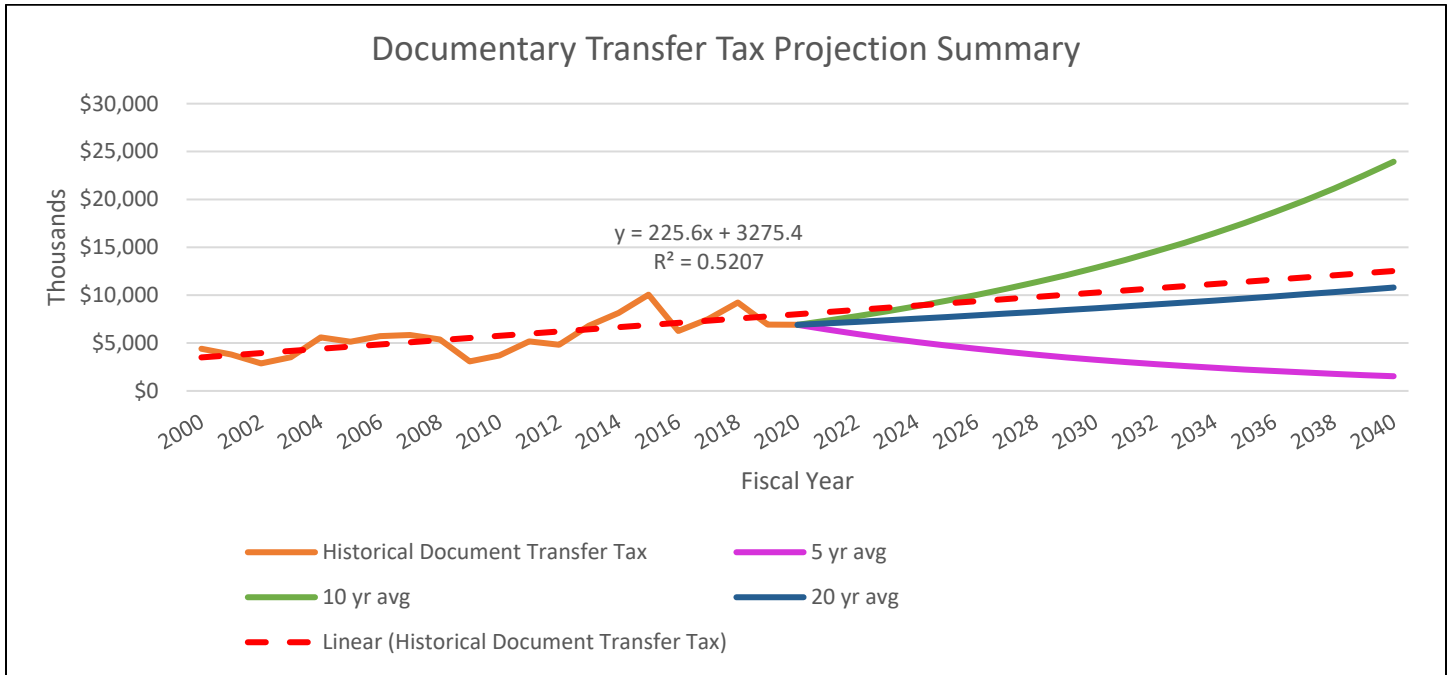
Fiscal Year	5 yr avg	10 yr avg	20 yr avg
2021	\$6,403	\$7,346	\$7,059
2022	\$5,940	\$7,817	\$7,219
2023	\$5,510	\$8,318	\$7,382
2024	\$5,111	\$8,852	\$7,549
2025	\$4,741	\$9,420	\$7,720
2026	\$4,398	\$10,024	\$7,895
2027	\$4,079	\$10,667	\$8,073
2028	\$3,784	\$11,351	\$8,256
2029	\$3,510	\$12,080	\$8,443
2030	\$3,256	\$12,854	\$8,634
2031	\$3,020	\$13,679	\$8,829
2032	\$2,802	\$14,556	\$9,029
2033	\$2,599	\$15,490	\$9,233
2034	\$2,411	\$16,484	\$9,442
2035	\$2,236	\$17,541	\$9,655
2036	\$2,074	\$18,666	\$9,874
2037	\$1,924	\$19,864	\$10,097
2038	\$1,785	\$21,138	\$10,326
2039	\$1,656	\$22,494	\$10,559
2040	\$1,536	\$23,937	\$10,798



The 5-, 10-, and 20-year averages all paint a very different picture from one another. The 10 yr. average shows growth of 6.41% while the 5-year average shows -7.24% growth and the 20-year average splits it all down the middle with 2.26% growth.

Documentary Transfer Tax Interpretation

The graph below is a combination of historic performance and all projections which were only the historic average projections.



Due to the lack of correlation with any economic indicators, the only projections the OCA were able to model were the historical averages. As stated in the observations and data analytics section, all three averages show vastly different outcomes when projected forward. In this case it was determined that using the 20-year average is the most reliable and conservative projections going forward. The LRFF Documentary Transfer Tax projections align with this assumption.

Utility User Tax

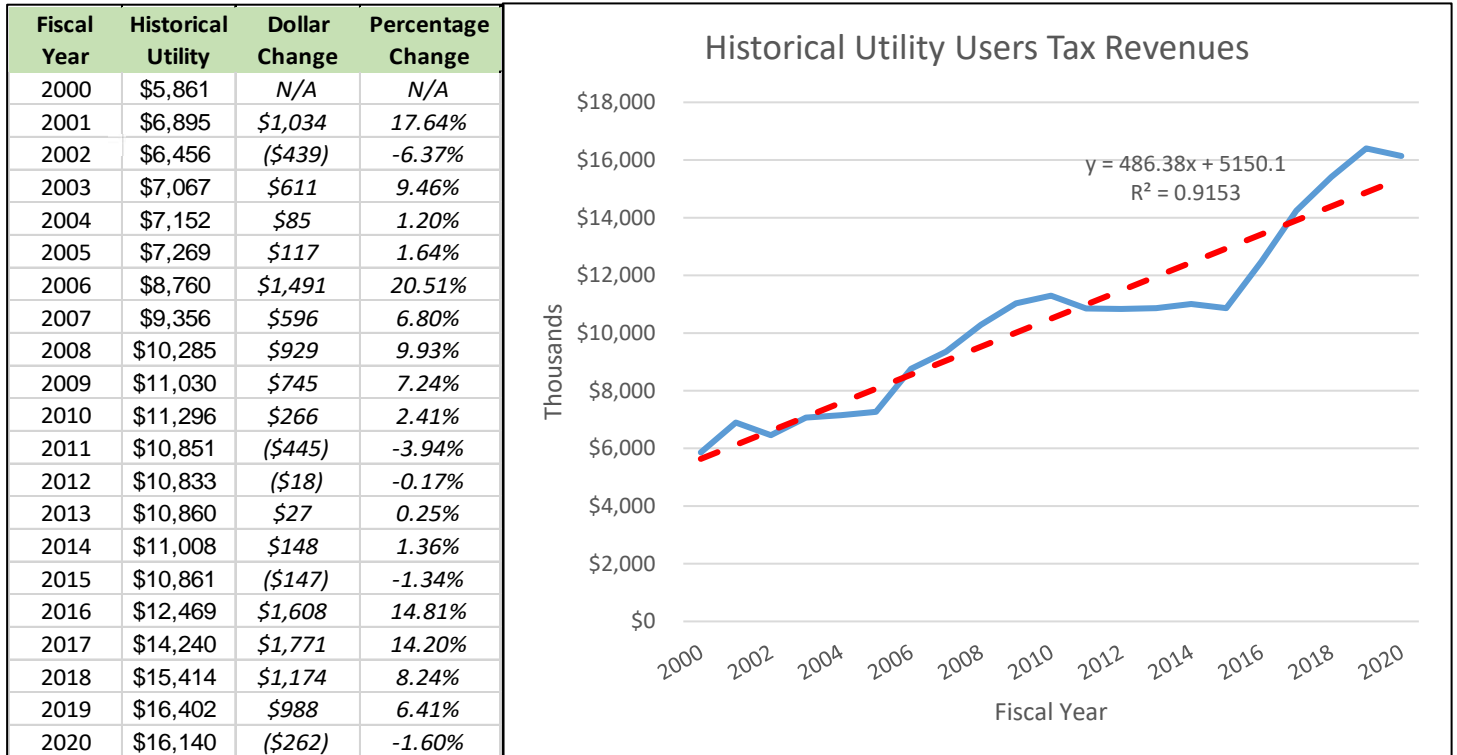
Utility Users Tax Overview

An analysis was performed by the OCA for the historical utility user tax revenues and future years were projected. The analysis provided insight into the steady increase in revenues over the past 20 years and future projections were calculated using historical averages and several economic indicators. These projections along with nationwide utility estimates were used to provide a best estimate of UUT's future performance.

Utility Users Tax Observations and Data Analysis

Historical Performance

The chart below shows the historical revenues for Utility User Tax from 2000 – 2020.



Utility user tax revenues have had a steady increase over the last 20 years. It has grown just over \$10M since the year 2000 which averages out to be 5.2% annually. There are a few years where revenues had jumped, but overall, it has not been rapid growth.

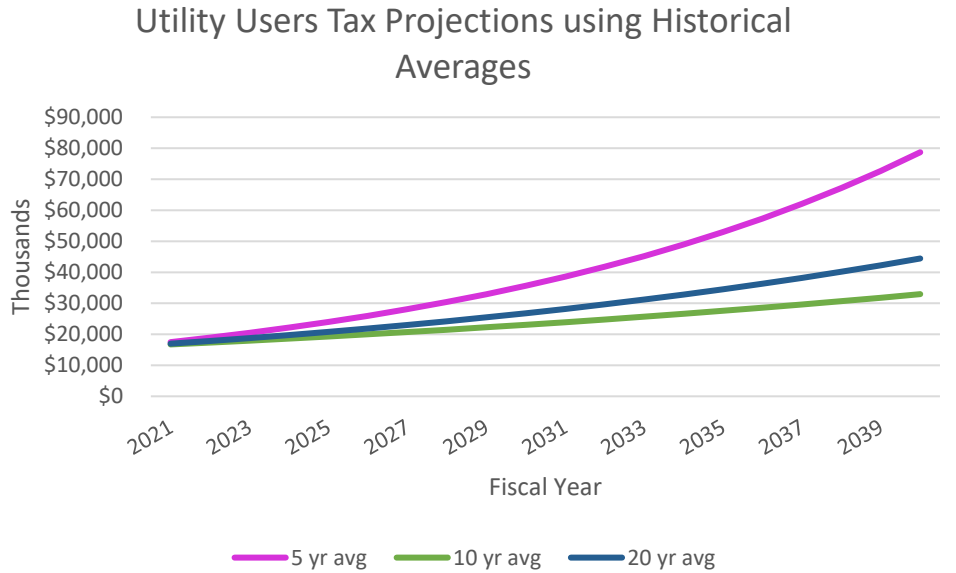
Historical Growth Averages

The graph below displays the UUT's revenue projections using the growth averages shown below.

Growth averages:

- 5 Year: 8.24%
- 10 Year: 3.63%
- 20 Year: 5.20%

Fiscal Year	5 yr avg	10 yr avg	20 yr avg
2021	\$17,471	\$16,726	\$16,979
2022	\$18,911	\$17,334	\$17,861
2023	\$20,470	\$17,964	\$18,789
2024	\$22,158	\$18,616	\$19,765
2025	\$23,985	\$19,293	\$20,792
2026	\$25,962	\$19,994	\$21,872
2027	\$28,103	\$20,720	\$23,008
2028	\$30,420	\$21,473	\$24,203
2029	\$32,928	\$22,253	\$25,461
2030	\$35,643	\$23,061	\$26,784
2031	\$38,581	\$23,899	\$28,175
2032	\$41,762	\$24,767	\$29,639
2033	\$45,205	\$25,667	\$31,179
2034	\$48,933	\$26,600	\$32,799
2035	\$52,967	\$27,566	\$34,503
2036	\$57,334	\$28,567	\$36,295
2037	\$62,061	\$29,605	\$38,181
2038	\$67,178	\$30,681	\$40,164
2039	\$72,716	\$31,795	\$42,251
2040	\$78,712	\$32,950	\$44,446



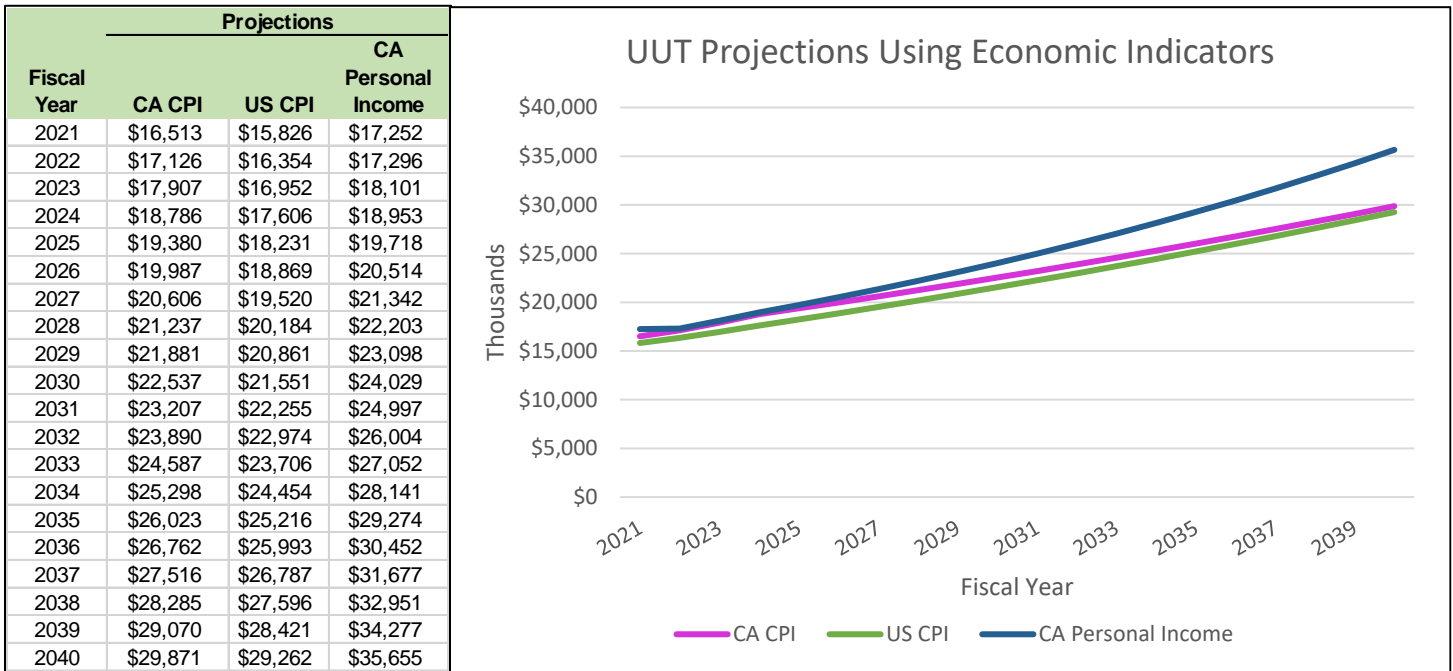
The historical data was used to compute growth averages over the last 5, 10, and 20 years. Those averages were applied to the 2020 revenues and carried forward until 2040.

Economic Indicator Projections

The chart below depicts the UUT projections using highly correlated economic indicators.

Economic Indicators with High Correlation:

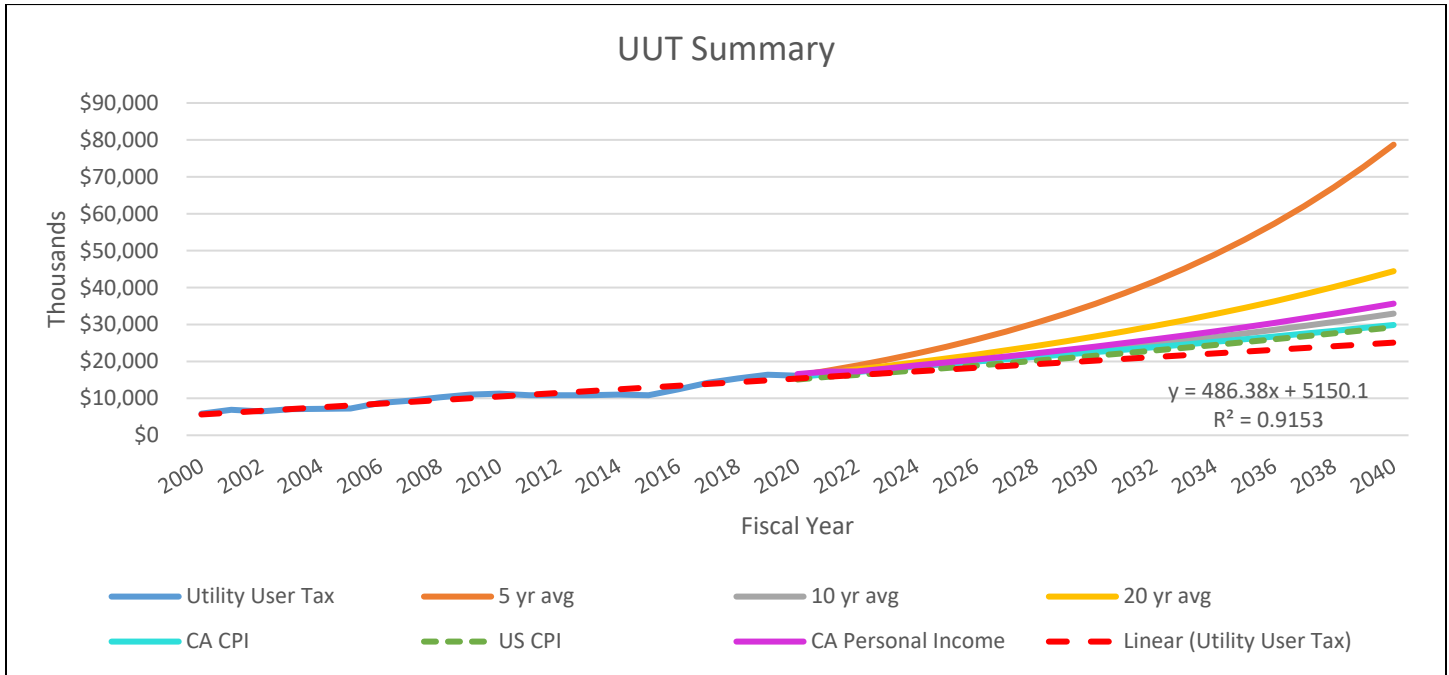
- Personal Income (California and Santa Clara County)
- Consumer Price Index (U.S., California, and San Francisco)
- Population (Palo Alto and Santa Clara County)
- Stanford Enrollment



The OCA found several economic indicators that had strong correlations to the historical UUT revenues. The indicators we were able to project forward include California CPI, US CPI, and California Personal Income

Utility Users Tax Interpretation

The chart below shows a combination of the historical UUT and the projections using historical averages and correlated economic indicators.



The OCA found some conflict between the historical averages, economic indicators, Utility Financial Forecasts and outside resources. Our internal data would suggest that the 10-year and 20-year average projections give a solid indication of where revenues might go as they are very close together. In addition, all three economic indicators created projections that were very close to the 10-year average. Based on this alone it could be suggested that revenues ending up in the \$30-\$35M by 2040 is plausible. The 10-year average and economic indicators also align with the Utility Users Tax projections for FY 2032 shown in the LRFF.

The OCA found information in the City Utility Department’s FY 2022 Preliminary Financial Forecasts¹¹ and FY 2021 Financial Plans¹² complimentary to the historical average projections. The plans show load forecasts with decreasing consumption for electric, water, and gas utilities as well as slight rate increases to offset some of the declining consumption leading to percentage increases close to the 10- and 20-year historical averages.

However, the OCA found some conflicting information from the Annual Energy Outlook 2021 published by the U.S. Energy Information Administration. This showed that the average annual electricity usage is anticipated to increase across the US by slightly less than 1% through 2050. That is more conservative than all of the historical factors and would have revenues only reaching around \$20M by 2040.

Due to conflicting opinions and data the City’s best option may be to continue leveraging their utility departments knowledge and forecasts to keep a close watch on their energy usage in the coming years and see if it aligns closer to the very minimal growth or remains closer to the historical averages.

¹¹ FY 2022 Preliminary Financial Forecasts: <https://www.cityofpaloalto.org/files/assets/public/agendas-minutes-reports/reports/city-manager-reports-cmrs/2021/id-11864.pdf>

¹² FY 2021 Financial Plans:

Electric: <https://www.cityofpaloalto.org/files/assets/public/agendas-minutes-reports/reports/city-manager-reports-cmrs/attachments/attachment-b-fy2021-electric-utility-financial-plan.pdf>

Gas: <https://www.cityofpaloalto.org/files/assets/public/agendas-minutes-reports/reports/city-manager-reports-cmrs/attachments/attachment-e-2021-gas-plan.pdf>

Water: <https://www.cityofpaloalto.org/files/assets/public/agendas-minutes-reports/reports/city-manager-reports-cmrs/attachments/attachment-i-fy-2021-water-financial-plan.pdf>

Economic Resiliency Review

Overview

The OCA conducted an review of the City's economic resiliency in parallel with the Revenue Trends and Models Review. The OCA included Economic Development subject matter specialists (SMSs) to complete an informational report of the Cities current state of economic resiliency. The City is currently in search for new position(s) focused on economic development. To aid in these efforts, the OCA will provide this Economic Resiliency Review in the form of a separate report.

Methodology

To complete a review of the City's economic resiliency, the Economic Development SMSs conducted two main tasks. The first task was focused on data analysis of key economic indicators while the second task was the resiliency analysis itself.

In regards to the data analysis, the City has had a recent focus on economic development, given the impacts from the Covid-19 pandemic, such as the reduction in retail sales tax, recent business turnover, and site redevelopment opportunities. The OCA conducted an analysis to assess the City's economic resiliency current state and uncover opportunities for adjustment or improvement.

Results

The Economic Development SMSs produced a memo specific for informational purposes. This memo was provided as guidance as the City searches for internal economic development personnel. The memo includes three high-level strategic recommendations supported by the economic resiliency analysis. Recommendations focus on the following areas:

- Business/industry diversification strategies
- Housing and workforce findings impacted by Covid-19 pandemic
- Enhancements to livability for resident and business engagement and retention, which could include high quality service delivery, recommendations on placemaking or other strategies to build community, and/or business programming

Appendices

Appendix A: Management Response – Revenue Trends and Model Review

Recommendation	Responsible Department(s)	Agree, Partially Agree, or Do Not Agree and Target Date and Corrective Action Plan
<p>Finding: Workbook Organization and Clarity</p>		
<p>In order to develop an accurate and thorough forecasting model, the City considers a number of data elements from various workbooks. The input from multiple parties is also involved. At the moment, the City doesn't have a consistent naming convention for workbooks, nor does it have narrative or instructions within the workbook itself to describe the flow of information. The City relies on the institutional knowledge of employees to understand how the forecasting information is pulled together. Without consistent naming conventions and information narratives, the City is at risk if key stakeholders in this process were to leave the organization. The OCA recommends developing a consistent naming convention and adding narrative in workbooks, including the purpose of the sheet, from where information is pulled, to where information is pushed, and with whom does the ownership of the spreadsheet lie.</p>	<p>Administrative Services</p>	<p>Concurrence: Partially Agree Target Date: Fall 2022 Action Plan: The City partially agrees with the recommendation and recognizes the potential for "key personnel" risk. There are four main workbooks that are used to monitor and forecast General Fund major tax revenue that each pull data from multiple sources. Staff believe the file names of the workbooks are appropriately named; however, staff agrees with the recommendation that the source of information can be improved to ensure sufficient informational narratives that assist in identifying data used from a detail level to summarized level for forecasting activities. The addition of information narratives would help improve the ability for other staff to both navigate the supporting workbooks as well as summarizing the forecasts for public narratives such as the Long Range Financial Forecast or budget documents. Staff believe the ownership of these workbooks is clear, the City's Manager of Treasury, Debt, and Investments is responsible for these forecast activities; support from a team of staff including senior managers and divisions in the department such as the Office of Management and Budget collaborate on the public reporting and financial planning.</p>
<p>In some cases, the City uses assumptions and rough estimates to consider various scenarios such as percentage growth in situations when supporting data is sparse. This can be a necessary action if no better alternatives exist. However, the OCA learned anecdotally that some of these rough estimates are highly specific, oftentimes having estimated numbers to the hundredths place. If a certain series of inputs are rough estimates, these inputs should not be made to look as though they were calculated. Instead those estimates should be clearly labeled with a short description as to the thought process behind how the estimator arrived at that number. This will help to clarify which values were calculated at one point vs. which values are estimated without a specific calculation.</p>	<p>Administrative Services</p>	<p>Concurrence: Agree Target Date: Fall 2022 Action Plan: Staff agrees that labeling estimates with short descriptions and selecting consistent rounding (i.e. hundredths place) will improve documentation of forecast assumptions and will implement this as part of the remaining FY 2023 annual budget process and as part of the FY 2024-2033 Long Range Financial Forecast.</p>

Finding: Model Improvements		
<p>The OCA recommends considering the following four factors as additional forecasting inputs for TOT;</p> <ul style="list-style-type: none"> - size and frequency of local conventions/events, - national unemployment, - hotel market segments and property-specific attributes, and - demographics of travelers. <p>While some of these inputs may not be possible due to lack of data or lack of applicability to the City, the OCA recommends considering these other inputs to determine if improvements to forecasting can be made. Where data is available for these factors, the City can use correlations factors to determine the strength of the relationship between TOT and a given input.</p>	Administrative Services	<p>Concurrence: Partially Agree</p> <p>Target Date: Fall 2022</p> <p>Action Plan:</p> <p>Administrative Services staff agree that these variables are informative inputs to forecasting when data is readily available for these factors. Staff review some of these factors including national unemployment, historical trends driving events and travelers on a macro level when developing the City’s financial reporting documents with projections including but not limited to the Long Range Financial Forecast and annual budget process. Incorporating these additional factors at a more precise individual revenue level, as noted in the recommendation, is not feasible as the data is not readily available or applicable for Palo Alto at this time. For example, since Palo Alto does not have assets such as a destination convention center like neighboring jurisdictions San Jose and Santa Clara, the size and frequency of local conventions/events is not as closely impactful in Palo Alto.</p> <p>Staff does have and references historical data such as demographics of travelers studied as part of the 2015 economic analysis completed as part of the development of the current Comprehensive Plan. Factors such as these are typically provided by organizations such as a convention and visitors bureau which the City is currently not a participant in. Staff will continue to review available data as part of the annual Long Range Financial Forecast.</p>
<p>The City should reach out to larger hotels to understand if they forecast as well as large businesses and Stanford University to understand their expectations for conferences, business travel, student activity, etc. If a relationship with Stanford to provide such information does not exist, this would be a useful relationship to develop for future analyses that may also benefit the University.</p>	Administrative Services	<p>Concurrence: Partially Agree</p> <p>Target Date: Fall 2022</p> <p>Action Plan:</p> <p>The City does review expected special events based on historical trends as part of the annual forecast, however, staff agree that seeking feedback from the local community would provide additional insights specific to Palo Alto if such organizations are able and willing to provide and disclose such information to the City. Historically staff have received anecdotal feedback on an ad hoc basis. In the coming Long Range Financial Forecast, staff will reach out to applicable organizations for this feedback and include feedback to the extent it is received.</p>



Attachment: Office of the City Auditor - Economic Resiliency Review - Final Draft for P&S (13909 : Presentation of the Economic Recovery



City of Palo Alto

Office of the City Auditor
Economic Resiliency Review
March 15, 2022

Executive Summary

Purpose of the Economic Resiliency Review

The Economic Resiliency Review was a component of a broader Economic Recovery Advisory audit activity. The purpose of the Economic Recovery Advisory audit activity was to review the City of Palo Alto's ("City") long-term financial planning models and inputs, offer recommendations for improvement, identify and evaluate key revenue source categories that present long term risk to the City's financial sustainability and perform scenario analysis. The Office of the City Auditor ("OCA") also offered ad hoc advisory assistance during the FY22 budget process.

In this particular report, the OCA included economic development subject matter specialists to conduct an Economic Resiliency Review as a resource to the City and any future City employees focused on economic development initiatives. This report supplements the Revenue Trends and Models Review included in the broader Economic Recovery Advisory report.

Results

The Economic Development SMSs produced this separate report specific to the Economic Resiliency Analysis. This report was provided as guidance as the City searches for internal economic development personnel. The report includes three high-level strategic considerations supported by the economic resiliency analysis. Recommendations focus on the following areas:

- Business/industry attraction, retention, and diversification strategies
- Housing and workforce findings impacted by Covid-19 pandemic
- Enhancements to livability for resident and business engagement and retention, which could include high quality service delivery, recommendations on placemaking or other strategies to build community, and/or business programming

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Introduction

Objective

The objectives of the Economic Recovery Advisory audit activity was to:

- 1) Review the City's long-term financial planning models and inputs and offer recommendations for improvement.
- 2) Identify and evaluate key revenue source categories that present long term risk to the City's financial sustainability and perform scenario analysis.
- 3) Offer ad hoc advisory assistance during the FY22 budget process.

The Economic Resiliency Review is a component of these broader objectives.

Background

The OCA performed a citywide risk assessment that assessed a wide range of risk areas, including strategic, financial, operational, compliance, technological, and reputation risks. The purpose of the assessment was to identify and prioritize risks to develop the annual audit plan.

During the [FY2021 risk assessment](#), the OCA identified the followings risks which led to this project.

- COVID-19 Response
- Financial Performance/Revenue Generation
- Tax Revenue & Economic Recovery
- Current Planning Practices

Additionally, during the risk assessment, Baker Tilly included some examples of potential risks in the future related to this audit:

- Large businesses moving to other locations or decreasing the focus on in-person interactions at headquarters, lowering the daytime population and visitors
- Decreasing real estate values due to external factors decreases City revenues from property taxes
- Lost revenue for the City to fund City services with Prop 13 in place
- High taxation on residents due to increased property values, especially long term Palo Alto residents, in the absence of Prop 13

Scope

To complete a review of the City's economic resiliency, the Economic Development SMSs conducted two main tasks. The first task was focused on data analysis of key economic indicators while the second task was the resiliency analysis itself.

Methodology

The City has recently focused on economic development, given the impacts from the Covid-19 pandemic, such as the reduction in retail sales tax revenue, recent business turnover¹, and resulting site and/or storefront revitalization opportunities. As there is some available data from previous studies, the Economic Development SMSs conducted a mix of data review and alignment from existing studies and additional analysis, including:

- Economic Growth & Employment
- Demographics
- Business/Industry

¹ Discussed in Palo Alto Online, "Layoffs. Red tape. Anxiety. Small businesses fight to survive pandemic" 4/17/2020; <https://www.paloaltoonline.com/news/2020/04/17/as-costs-mount-small-businesses-fight-to-survive>. Accessed 01/05/22

- Visual review and locational analysis using maps and other tools

The Economic Resiliency Analysis involved calculating risk to a community's key economic assets and developing a strategy to buffer risk to minimize or avoid shocks to the economy. The OCA conducted an analysis to assess the City's economic resiliency current state and uncover opportunities for adjustment or improvement, including:

- Economic incentives scan
- Regional economic trend scan, including employment and industry location quotient
- Economic resiliency readiness check, including evaluation of steady state and responsiveness factors

Compliance Statement

This audit activity was conducted in accordance with the Annual Audit Plan. The audit activity was not performed in compliance with the generally accepted government auditing standards (GAGAS). The audit activity was not performed in compliance with GAGAS for two primary reasons:

- The individuals conducting the activity did not meet the CPE requirements. As subject matter experts in construction risk, the team members are not required to obtain government audit CPE. Rather, multiple team members are required to be technically competent construction risk professionals and obtain CPE in construction risk topics.
 - Mitigating factor – City Auditor Kyle O'Rourke and Manager Chiemi Perry both adhere to CPE requirements
- The City of Palo Alto Office of the City Auditor has not undergone an External Peer Review in the required 3 year cycle as required by Standards.
 - Note – the Office of the City Auditor will undergo a peer review at the conclusion of FY22.

We planned and performed the activity to obtain sufficient, appropriate evidence to provide a reasonable basis for our recommendations based on our objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit the objectives.

Organizational Strengths

During this review, we observed certain strengths of the City regarding economic resiliency. Key strengths include:

- A high-level of responsiveness and a problem-solving approach to business needs during the Covid-19 pandemic
- A strong baseline for the city's residential property tax base and supporting demographics to continue to support future growth
- A healthy mix of business sizes, industry specialization, and geographic location of retail and business centers across the city to support the city's economic resiliency profile

The Office of the City Auditor greatly appreciates the support of the Administrative Services Department in conducting this audit activity.

Thank you!

Economic Resiliency Review

Introduction

The purpose of the economic resiliency review is to provide a high-level background of baseline conditions and core indicators that the City could consider as an economic resiliency threshold. This review is primarily drawn from secondary research, data, and reports. Unfortunately, there is a lag of data available to truly elucidate the disruption of the Covid-19 pandemic to the core conditions of the local and regional economy.

The intent of this review is to summarize past baseline conditions to prepare the City and its economic development partners to move forward with a new set of challenges and conditions given the ongoing pandemic and long-term changes to remote work and an online retail economy. With that in mind, the City considers itself as embedded within the business community, aligned with other groups that provide support and resources to local businesses, such as the Palo Alto Chamber of Commerce, the downtown business district, the California Avenue business district, property owners and brokers, the Stanford Research Park, and Stanford University. As such, the City should rely on its many partners in economic development to act on strategies, policies, and programming to support economic growth.

Summary Presentation of Demographic Data & Business Baseline

To develop a working understanding of the economic baseline, the economic development SMSs reviewed key indicator demographics, including population data, income, educational attainment, housing market data, business, and employment information. These demographic indicators determined a strong profile of economic resiliency.

Population, Income, and Educational Attainment

The City's population was 68,572 as of the 2020² census data. Between the 2010 and 2020 censuses, the population grew by a steady but modest pace of 6.47% that was above the state average of 6.13%, but below the national average of 7.35% and below the 8.67% increase experienced in Santa Clara County as a whole³. The population is significantly less diverse than Santa Clara County and California. 54.9% identified as "white alone, not Hispanic or Latino" while that number was 30.6% in Santa Clara County and 36.5% statewide⁴. The City's younger age brackets are comparable to county and state averages; however, the city has a higher proportion of its population that is 65 years or older at 19.4% while the county and state percentages are 13.9% and 14.8% respectively⁵.

Palo Alto has very strong personal and family income when compared to the county and state averages. Median household income was \$158,271 while Santa Clara County was \$124,055 and California was \$75,235. Per capita income was even more significant at \$92,590 with the county and state averages being \$56,248 and \$36,955 respectively. Poverty prevalence was significantly lower as well, with the percent of persons in poverty at 6.10% compared to 7.52% in Santa Clara County and 11.8% in California⁶.

The city has extremely high education attainment rates. 97.4% of persons age 25 year or older are high school graduates or higher, and 82.8% have a bachelor's degree or higher⁷. The city's extremely high rate of college degrees is of note, being more than double the state average. By comparison, Santa Clara County's rates are 88.4% and 52.4% respectively, and California's rates are 83.3% and 33.9% respectively.

² US Census Bureau, Quick Facts; Palo Alto, CA; 2020 Census

³ US Census Bureau, 2020 Census.

⁴ Ibid

⁵ Ibid

⁶ Ibid

⁷ US Census Bureau, QuickFacts; Palo Alto, CA; 2015-2019 data

Housing Market and Property Tax Revenue

The city has a very strong housing market with much higher property values than county and state averages. According to the US Census Bureau, the median value of owner-occupied housing units was \$2,000,000+ in Palo Alto, \$984,000 in Santa Clara County, and \$505,000 in California⁸.

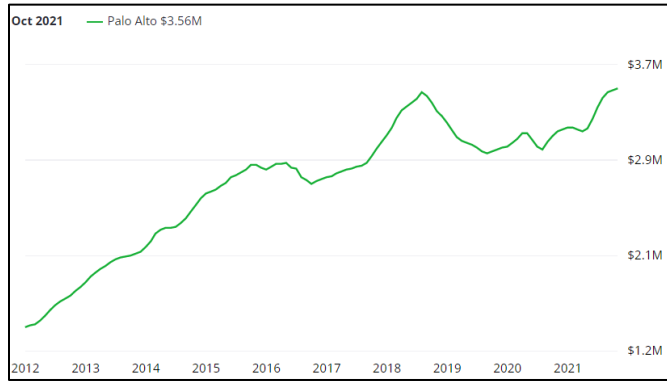


Figure 1: Zillow Home Value Index, Palo Alto, 2012-2021

According to the more recent Zillow Home Value Index⁹, the typical home value in The City was \$3,560,805 as of their October 2021 data. This value is seasonally adjusted and reflects the typical value for homes in the 35th to 65th percentile range and represents an 11.6% increase over the previous year. The market has rebounded from the 2008 Financial Crisis and following recession, with Zillow’s Home Value Index showing a value of \$1,500,000 in Dec 2011. Over the last five years, growth has continued but the pace has moderated somewhat.

According to Redfin’s November 2021 data, the housing market is considered very competitive, with a Redfin Compete Score of 87 out of 100. The median sale price was \$3,525,000, representing a 21.5% increase year-over-year. The average home is on the market for 11 days and sells for 8% above list price, with some homes selling for 17% above list price. Approximately 64.6% of homes sold above list price, a 31.7% increase year-over-year.

With the rapid increase in housing prices during the post-recession recovery period, housing costs have increased considerably to nearly three times the national average for owners and more than double the national average for

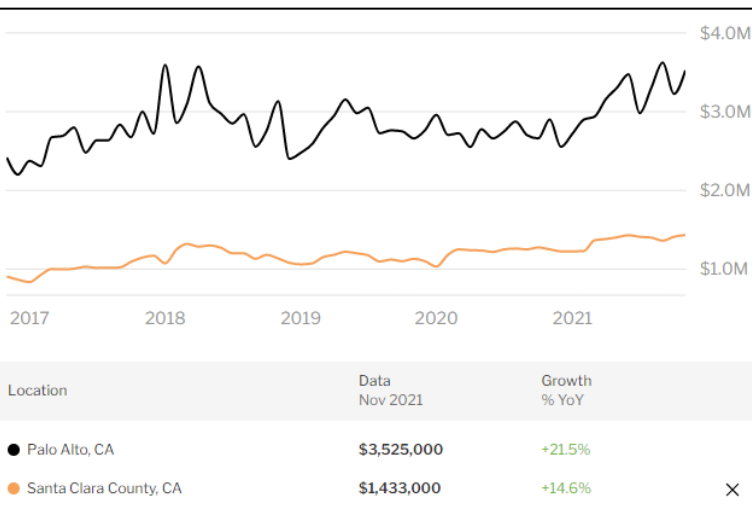


Figure 2: Redfin Median Sale Price, Palo Alto and Santa Clara County, 2016-2021

renters. According to data from the US Census Bureau¹⁰, median monthly owner costs with a mortgage were \$4,000+, significantly higher than the \$3,381 in Santa Clara County and \$2,357 in California. Median gross rent (2015-2019) in Palo Alto was similarly high when compared with the county and state averages of \$2,268 and \$1,503 respectively.

As the residential property market has experienced increased activity in recent years, the City’s property values have seen increases across all categories of real estate. The Palo Alto Property Tax Summary for 2019-2020 reflects pre-pandemic numbers. According to the summary, the year-over-year increase in property values for all real estate categories was \$3.055 billion, an increase of 7.8%. Residential values experienced a 6.3% increase and accounted for 56% of all growth for

the period. Commercial properties had an increase of 9.7% which accounted for approximately 24.8% of all growth for the period. Industrial properties saw the greatest increase at 28.4% after having declined by 10% in the previous year. The significant jump in industrial values was primarily related to improvements to certain larger parcels. Fifty vacant parcels were developed and transferred to other uses.

⁸ Ibid

⁹ Zillow Home Value Index; Palo Alto, CA, October 2021 Report

¹⁰ US Census Bureau, QuickFacts; Palo Alto, CA; 2015-2019 data

While there was uncertainty surrounding real estate and the overall economy at the outset of the pandemic, the trend towards higher property values and increased real estate transactions has continued. Any negative impact to commercial or industrial properties is likely to be offset by the strong growth in residential property sales during the pandemic which was buoyed by historically low interest rates. Even with the Federal Reserve considering multiple interest rate increases in 2022¹¹, interest rates are anticipated to remain comparatively low relative to historic trends, which should sustain the residential real estate market and related property tax revenues.

While residential property values are a benefit in terms of property tax revenue, they can pose a barrier to local employment growth. When comparing Palo Alto's housing data to Santa Clara County and the state, high housing prices combined with limited land available for new housing, could be a driver of the unusually high commute patterns identified in the labor force summary below. (US Census 2019, Commute Patterns). Employers in Palo Alto import 93% of their employment base from outside of the city. If the standard rule follows that mortgage/rent payments should not exceed more than 30% of a household budget, a theoretical person purchasing a house at the current median home value of \$2,000,000 (US Census) to \$3,500,000 (based on recent sales data) with a median income of \$158,271 would spend a much higher percentage of their income on housing-related costs. While the housing market, income levels, and household budget allocations are more complex than this example, economic development strategies to support businesses and the workforce may be needed to mitigate some of the issues related to housing costs.

However, since commute data is not available from 2020- to current, which includes the pandemic, it is unknown to what the extent the trend toward remote work will impact the residential and commercial real estate market and property tax revenue. With remote work becoming more prevalent as a result of the pandemic, particularly as it relates to business class/white-collar jobs, there may be a trend for workers to relocate to more suburban areas with lower costs of living, larger residential properties, and access to outdoor space. Additionally, many employers are downsizing office size and shifting to more remote and shared-work spaces. It is not known if this trend is temporary or permanent and how it may impact the city in the long term. However, based on current real estate market data, it does not appear to be negatively impacting residential prices.

Business Size Profile

The city's employment base is characterized by several factors that are noticeably different from California as a whole. A high percentage of overall employment is from larger companies. The percentage of employers with 500+ employees is four times the state average. Similarly, the percentage of employers with between 250 to 499 employees is double the state average. At the other end of the spectrum, companies in the size class of 1 to 4 employees make up a higher percentage of businesses in Palo Alto, with a rate of 41.4% when compared to the state average of 34.7%.

Palo Alto Employers	Employee
Stanford Healthcare	5,50
Lucile Packard Children's Hospital	5,70
Stanford University	4,50
Veteran's Affairs Palo Alto Healthcare System	3,90
VMWare, Inc.	3,50
SAP Labs Inc.	3,50
Space Systems/Loral*	2,80
Hewlett-Packard Company	2,50
Palo Alto Medical Foundation	2,20
Varian Medical Systems	1,40

Figure 3: Palo Alto Top Largest Employers, Good City Company

Figure 3 above shows the largest employers in the city. While there is a heavy concentration of firms in the information industry sector, healthcare and social services account for half of the top employers, and three out of the top four on the list are in the healthcare and social services industry. There is a significant economic impact of Stanford University School of Medicine and its related medical research and technology, and Stanford Health Care (among the top hospitals in the nation) that add to the health care economy core strength. Stanford University (4,500 employees) is a strong asset

¹¹ Timiraos, N. (2022, January 5). Fed minutes point to possible rate increase in March. The Wall Street Journal. Retrieved January 7, 2022, from <https://www.wsj.com/articles/fed-minutes-reflect-growing-unease-over-high-inflation-11641409628>

and economic driver on multiple levels, as a top tier education and research institution, as well as driver of new residents and visitors to the community.

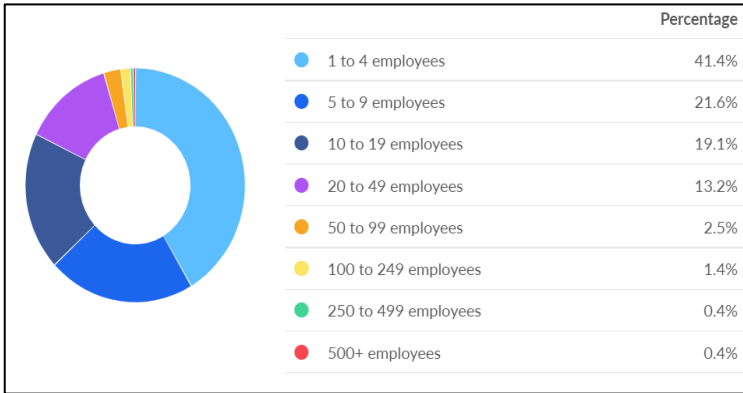


Figure 4: Palo Alto Business Percentage, Emsi/DatabaseUSA.com

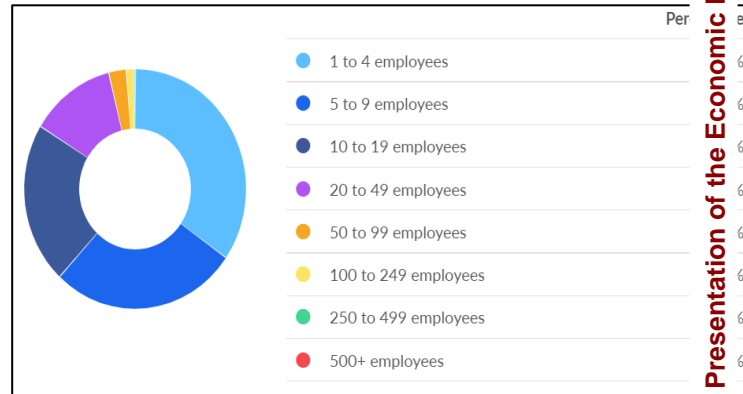


Figure 5 California Business Percentage, Emsi/DatabaseUSA.com

Employment and Industry Mix

We looked at industry employment based on percentage change from 2015 to 2020 and industry employment by location quotient to determine both the growth in employment and the concentration of employment as it compares to the national average.

In the top growing industries, the largest change in industry employment was in the Information sector with a 5-year increase of 32%, or 6,697 new jobs. Government saw a 5-year increase of 12% or 910 jobs. Health Care and Technical Assistance saw a 5-year increase of 11% increase or 2,575 jobs. And Professional and Scientific, and Technical Services saw a 5-year increase of 10% or 1,726 jobs.

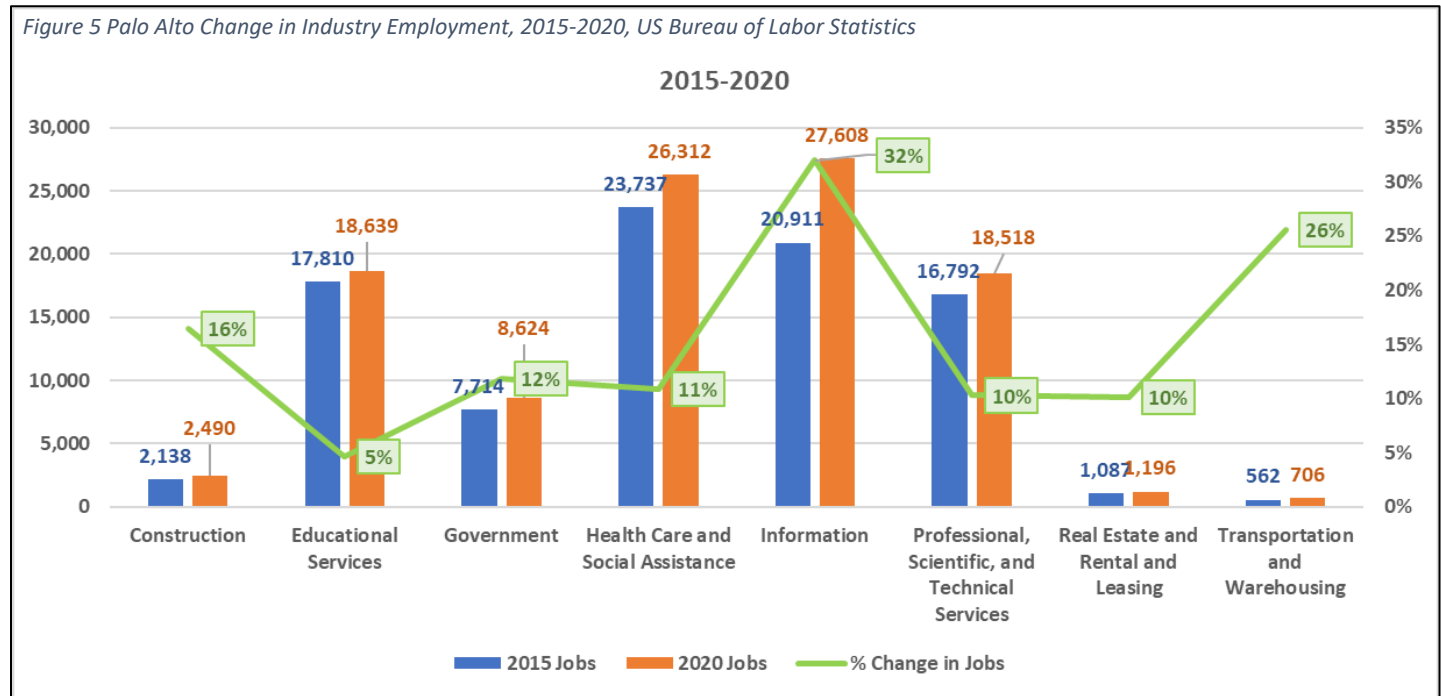


Figure 5 Palo Alto Change in Industry Employment, 2015-2020, US Bureau of Labor Statistics

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Next, we looked at location quotient (LQ), which is a ratio that measures a region's industrial specialization relative to the US. An LQ greater than 1 indicates an industry with a greater share of local area employment than the national base. Palo Alto has several industries, such as information; health care and social assistance; educational services; and professional, scientific, and technical services, which have a LQ over 1. The Information industry with a NAICS code of 51, includes jobs in software development, data communications, data processing, and other jobs related to publishing of information and data.



Figure 6 Palo Alto 2020 Industry Location Quotient, 2-digit NAICS, US Bureau of Labor Statistics

Location quotients help to understand regional economic strengths and opportunities. They are also useful in forecasting regional economic trends based on trends for specific market sectors. It is no surprise that the city has significant employment in the Information industry with a location quotient of 11.42. This high location quotient tells us there is a significant information technology ecosystem that can be leveraged to support other industry linkages as well as attract sub industry sector businesses. This robust ecosystem drives the local economy with extensive reach both domestically and internationally.

Analyzing location quotients at the more granular 6-digit NAICS versus a 2-digit NAICS allows for more precise reporting of the employment and overall growth of a region's industry sectors. More precise industry data allows workforce training providers to design programs to better fit the existing and future skill needs of those industries, and for communities to leverage this projected growth. To get a closer look at the city's industry mix, we looked at the 6-digit industry NAICS location quotient by employment. Internet Publishing and Broadcasting and Web Search Portal had a location quotient of 86.72, while Blank Magnetic and Optical Recording Media Manufacturing had a location quotient of 56.52 and Radio and Television Broadcasting and Wireless Communications Equipment Manufacturing¹² had a location quotient of 35.36. All these LQ specializations reveal strengths with the technology industry.

¹² NAICS 334220 includes manufacturing radio and television broadcast and wireless communications equipment. Examples of products made by these establishments are transmitting and receiving antennas, cable television equipment, GPS equipment, pagers, cellular phones, mobile communications equipment, and radio and television studio and broadcasting equipment.

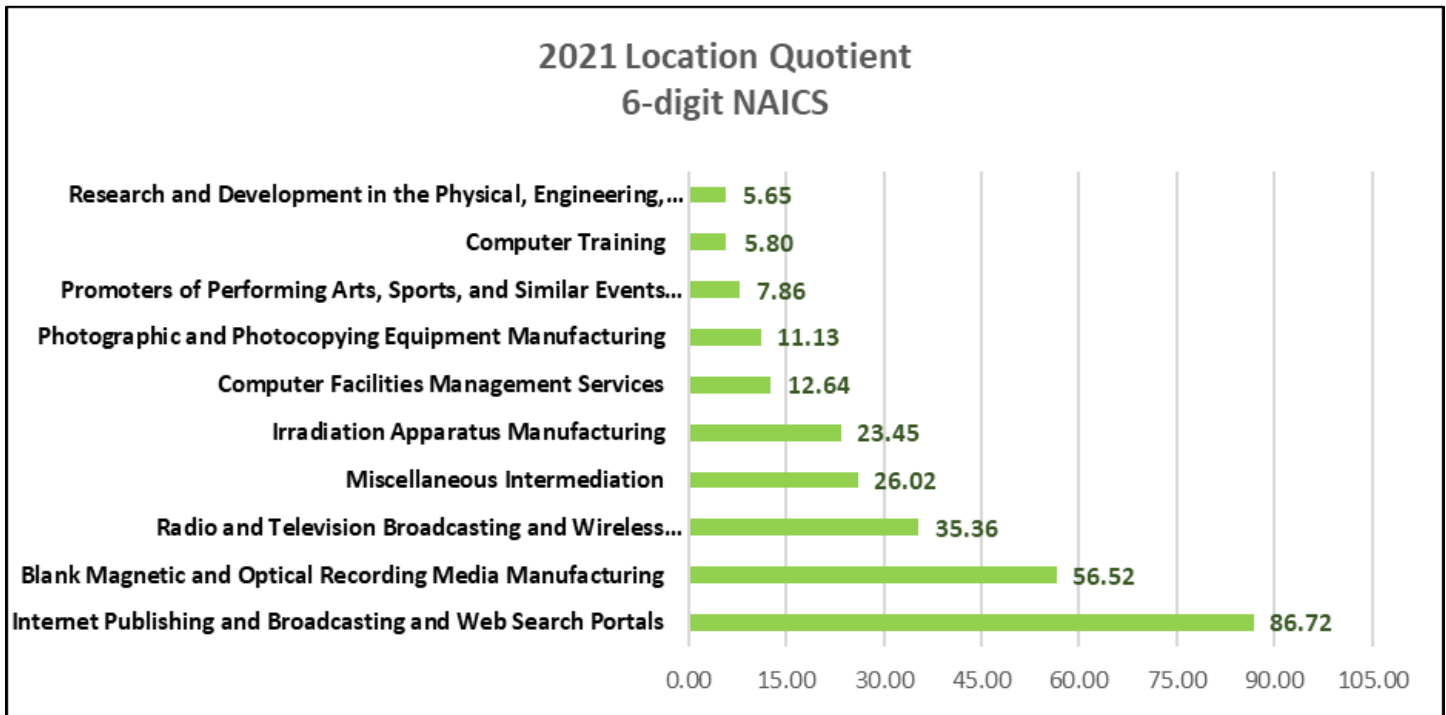


Figure 7 Palo Alto 2020 Industry Location Quotient, 6-digit NAICS, US Bureau of Labor Statistics

However, often a significant industry concentration needs to be addressed in terms of economic diversification. A diversified economy is more able to withstand downturns in their primary economic driving activity leading to a more resilient economy. Industry diversification also provides for skill set diversification which can allow employees to transfer more quickly into other occupations and employers to customize job training programs should there be downturns in the primary industry.

Labor Force and Commuting Patterns

To further understand the geographic labor shed of the area, Baker Tilly analyzed the workforce’s place of work when compared to the place of residence. Based on 2019 data from the Bureau of Labor Statistics, the City’s total primary private employment was 109,220, with a net inflow of 82,304 jobs. Of the 109,220 total primary private jobs in 2019, only 24.6% of workers, or 26,916, were living in the City of Palo Alto. Whereas 102,544 people were employed in the Palo Alto area but living outside the area. Of the 26,916 workers living in the city, only 6,676 are employed and living in the Palo Alto. This data suggests a significant in-migration of workers who could live in here if other factors, such as available housing types, cost of living, commute time, work flexibility, or other factors were different. A further analysis of this large in-migration of workers is warranted to determine if providing a shorter commute or an opportunity to live within the area in which they are employed could create a positive impact for attraction and retention of a highly skilled and sought-after workforce.

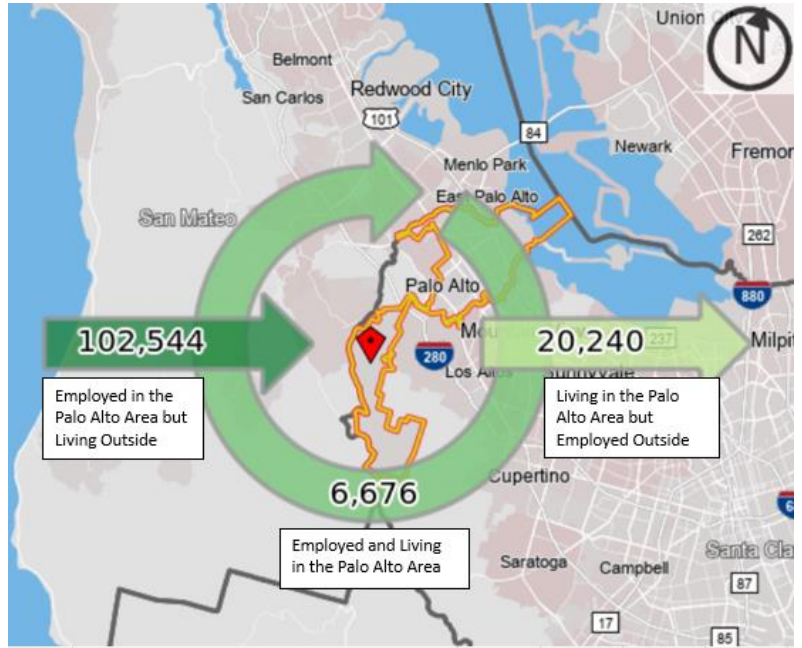


Figure 8 Commuting Patterns, US Census, OntheMap, 2019

Inflow/Outflow Job Counts (Private Primary Jobs)		
	2019	
	Count	Share
Employed in the Palo Alto Area	109,220	100.00%
Employed in the Palo Alto Area but Living Outside	102,544	93.90%
Employed and Living in the Palo Alto Area	6,676	6.10%

Figure 10 Inflow/Outflow Job Counts, US Census, OntheMap, 2019

Palo Alto (Private Primary Jobs)		
	2019	
	Count	Share
Employed in the Palo Alto area	109,220	100.0%
Living in the Palo Alto Area	26,916	24.6%
Net Job Inflow (+) or Outflow (-)	82,304	-

Figure 9 Employed and Living in Palo Alto, US Census, OntheMap, 2019

Retail – Shopping Centers and Key Corridors

The OCA’s economic recovery report projects future growth in and sales tax over time. The City’s largest sales tax contributors are a diverse group of businesses that conduct automobile sales, medical sales, tech companies and data management, and destination retail. Geographically, the largest sales tax contributors are located on automobile-oriented corridors, at the Stanford Shopping Center, or along small business-scale or “walkable” retail corridors, such as California Avenue and University Avenue. While California Avenue and University Avenue are well-known and contribute to a sense of place in the city, the largest sales tax performers are located in auto-oriented retail destinations.

Numerous challenges have emerged on small retail corridors during the Covid-19 pandemic, including temporary closures of California Avenue to support outdoor dining. Anecdotally, this appears to have helped some businesses and hurt some businesses. A broader analysis and redevelopment strategy of the California Avenue corridor could be conducted to position it for the future economy and an endemic status of Covid-19, where remote work continues to impact localized retail corridors.

Palo Alto, CA. Major Sales Tax Performers, 2020	
Business*	Type**
Anderson Honda	Auto
Lucile Packard Children's Hospital	Medical
Tencent	Tech/Data Management
Apple Stores	Destination Retail
Macy's Department Store	Destination Retail
Tesla	Auto
Audi Palo Alto Magnussen's	Auto
Toyota of Palo Alto	Auto
Telsa Lease Trust	Auto Lease
Bloomingdales	Destination Retail
Hp Enterprise Services	Tech/Data Management
Shell Service Stations	Gas
McLaren San Francisco	Auto
Tiffany & Company	Destination Retail
Bon Appetit Management Co	Catering
Neiman Marcus Department Store	Destination Retail
Urban Outfitters	Destination Retail
Hermes	Destination Retail
Nest Labs	Tech/Data Management
Varian Medical Systems	Medical
Houzz Shop	Destination Retail
Nordstrom Department Stores	Destination Retail
Volvo Cars Palo Alto	Auto
Integrative Archive Systems	Tech/Data Management
Stanford Outpatient Clinic Pharmacy	Medical

*Source for Business: Good City Company Presentation to Council, 6/1/21

**Source for Type: Baker Tilly

Economic Resiliency Analysis

The economic resiliency analysis involves calculating risk to a community’s key economic assets and developing a strategy to buffer risk to minimize or avoid shocks to the economy. Baker Tilly analyzed the current state of economic resiliency through a high-level review of development incentives, economic trends, and business engagement during the COVID-19 pandemic to uncover opportunities for adjustment or improvement.

Economic Trends

Several of the city’s strong business and professional occupations held steady or experienced growth over the past five years, such as Business/Financial Operations, Management, and Health Care Practitioners/Technical, Educational, and Sales. The city’s top growing occupations can be found primarily in the health-related industry and Arts/Media fields. The Arts/Design/ Entertainment/Sports and Media occupations grew by 43% from 2015 – 2020. In the same period, the combined growth in occupations related to the health care industry grew by roughly 20%

The top occupations based on location quotients are computer and mathematical at 3.56, legal at 2.95, art/design/entertainment/sports and media at 1.92, and healthcare practitioners and technical at 1.87. These quotients indicate a higher concentration of employment in these occupations in the Palo Alto area than the national average.

As we are shifting from an occupation-based workforce to a skills-based workforce, knowing the concentration of skills within these occupations is important to attract new businesses. Employers are often looking for skills versus occupations as they can retrain/upskill if the employee has the basic industry skill sets. A valuable exercise would be to determine the skills sets within these industry occupations to market the region’s workforce and to sustain existing business growth.

Business Engagement During Covid-19

The City was very involved in business recovery and engagement strategies during the Covid-19 pandemic, particularly as it impacted retail and restaurants on key corridors, such as California Avenue and University Avenue. The city developed an action team of decision makers and department heads, with hands-on involvement from the City Manager to address and solve problems brought up by local businesses. The city developed weekly business check-in meetings

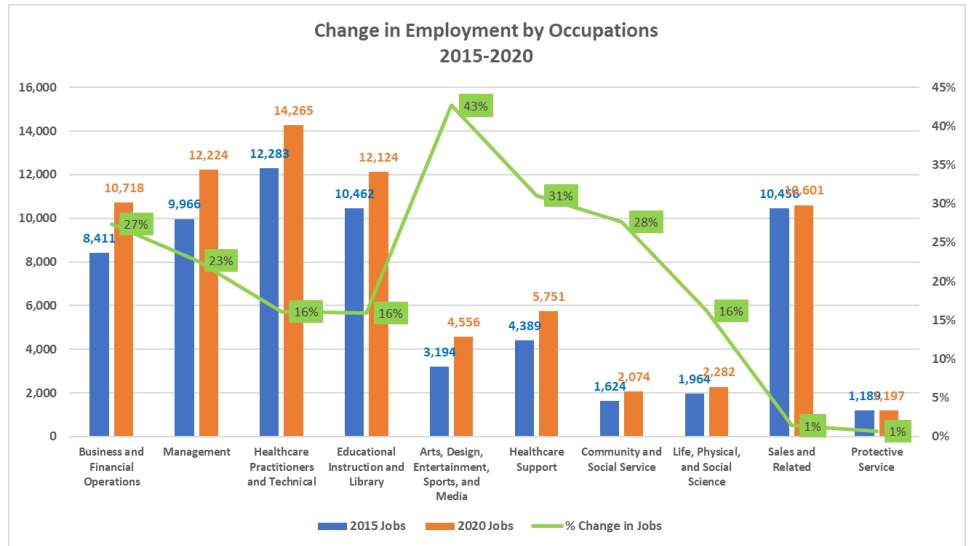


Figure 11 Change in Employment by Occupations, US Bureau of Labor Statistics, 2015-2020

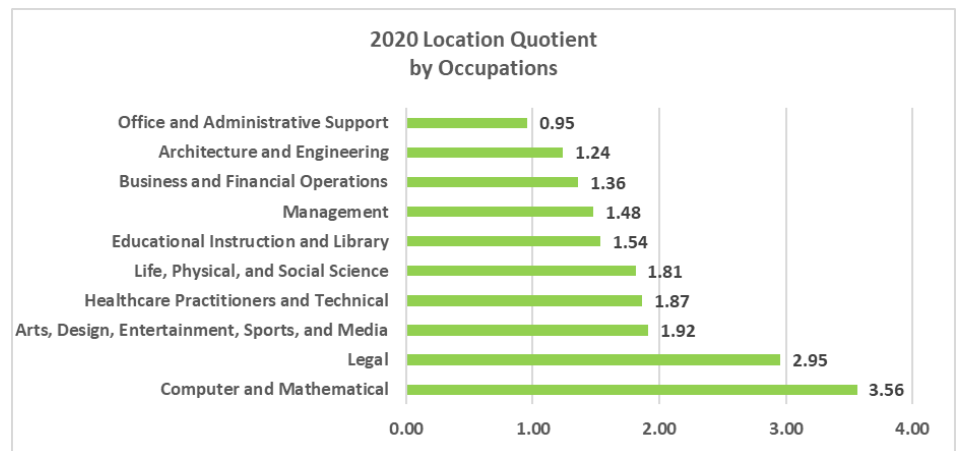


Figure 12 Location Quotient by Occupations, US Bureau of Labor Statistics, 2020

and the *Uplift Local* program to quickly utilize outdoor spaces to help expand business activities outdoors for restaurants and fitness businesses.

The Stanford Research Park is a powerhouse economic asset to the City and is an economic driver of jobs, salaries, spending power, business growth, industry diversification, and property tax receipts. While there was some collaboration during the COVID-19 pandemic with strategic support of the small businesses on California Avenue corridor, a more proactive engagement strategy of business retention and attraction could be considered from the city perspective, targeted to the larger industrial and tech businesses located there.

The City views itself as embedded within the business community when it comes to economic development, aligned with other groups that provide support and resources to local businesses, such as the Palo Alto Chamber of Commerce, the downtown business district, the California Avenue business district, property owners and brokers, the Stanford Research Park, and Stanford University. The new economic development staff person is one of many participants within the business development and economic development space, and can only act on the specific decisions, programs, or action steps that can be executed by city staff.

Considerations

Business and Industry Attraction, Retention, and Diversification Strategies

The City and its economic development partners could explore the following considerations for business and industry attraction, retention, and diversification to enhance long-term economic resiliency. Retail and small business corridors warrant different considerations than considerations for larger businesses.

Retail and Small Business Corridor Considerations

While destination retail in the city is doing well, small business corridors, such as California Avenue and University Avenue, have been more vulnerable to impacts of the COVID-19 pandemic and the changing retail environment. The following considerations would support a more proactive approach by economic development partners to attraction and retention of small businesses in walkable, “Main Street” corridors.

- A mix of coveted small-scale retail stores and California-based boutique brands can be found here, as well as independently owned restaurants, wine bars, and other small business venues. A strategic approach to corridor planning with intentional placemaking¹³ tactics could be utilized to address the multi-faceted set of issues on key retail corridors.
- If it benefits the community’s identity and “placemaking” efforts, the City could consider if a more proactive approach to support business retention and attraction on walkable, small business-focused corridors is a priority. Ideas include simplifying the renovation and redevelopment process and fee structure, potential rent subsidies for small businesses, and/or workforce support programs. If an incentive program is considered, the City may require some evaluation criteria, such business plan information, revenue projections, market analysis, customer potential, etc. to qualify for investment.
- Another approach to the California Avenue corridor could be to undertake a broader business and retail analysis and develop a more divergent, future-focused redevelopment vision and plan. A new approach could position the corridor for the future economy and an endemic status of Covid-19, where remote work continues to impact localized retail corridors.
- The restrictions on big-box stores or retail chains could be reviewed to see if the current policy still meets the City’s goals in the current retail environment.
- Economic development partners focused on corridor business attraction could collaborate on retail attraction strategies with the owner/operator of Stanford Shopping Center. There may be an opportunity to capture an overflow of retail prospects to locate on University Avenue or California Avenue.
- As the population ages, changing demographics that lean towards an online-focused, more diverse population may not have the same brand allegiance to destination retail and/or may have different retail shopping habits. Consider developing strategies that account for changing retail preferences and trends to ensure the future success of destination retail.

Note: In contrast to the above, the City could choose a less proactive approach, including letting market forces guide what happens in the University Avenue and California Avenue corridors. There may be consequences for the small-scale, walkable businesses on these corridors and a lag in redevelopment efforts as market forces dictate future opportunities.

¹³ “Placemaking” is used here to reference a process of creating quality places (unique, visually attractive, interesting, often including public art and entertainment) to attract people and activities.

Larger Business Diversification Considerations

The following considerations summarize the findings on larger business diversification. While the City is doing well in employment in total jobs and jobs within growth industries, continued business retention is an ongoing consideration, especially with the rapidly changing business climate.

- The city's industry mix is concentrated primarily in two industries, information and health care. Even though these are growth industries, industry diversification can provide economic stabilization and help mitigate the risk associated with the downturn in a concentrated industry.
- The percentage of employers with 500+ employees is four times the state average. This provides a workforce that would attract other larger corporations. However, consideration of providing targeted support and incentives to mid-size, small business and entrepreneurs would help diversify workforce and overall industry mix.
- The top occupations based on location quotients by 2-digit NAICS are computer and mathematical at 3.56, legal at 2.95, art/design/entertainment/sports and media at 1.92, and healthcare practitioners and technical at 1.87. The location quotient by 6-digit industry NAICS are Internet Publishing and Broadcasting and Web Search Portal at 86.72, Blank Magnetic and Optical Recording Media Manufacturing at 56.52 and Radio and Television Broadcasting and Wireless at 35.36. These occupations support a highly educated and skilled workforce, which can be used to support an effort to attract mid-sized businesses and aid in industry diversification.

Housing and workforce findings impacted by Covid-19 pandemic

Here are some brief short-term considerations in the areas of housing and workforce, as it relates to issues that emerged and actions taken by the City during the Covid-19 pandemic.

- The housing market was stable and continued to grow throughout the pandemic. This helped buffer the City's revenue streams when retail sales tax, hotel stays, and other growth areas slumped.
- The continued growth of housing costs may need to be considered and further analyzed from a business retention and workforce recruitment standpoint.
- Many businesses on the University Avenue and California Avenue retail corridors that depend on office workers and commuters as customers struggled during the pandemic. Additionally, many businesses reported challenges with workforce attraction and retention in city surveys. As the pandemic continues to disrupt daily life and long-term remote work continues, a loss of foot traffic and daytime customers continues to negatively impact Palo Alto's retail and restaurants on key corridors. A broader strategy of coordination with partners to activate corridor businesses and business support strategies could be explored by the City. A more rigorous analysis using primary research of businesses on these corridors could be conducted to understand the long-term impacts of remote work and new strategies to engage existing residents and businesses to rebuild the customer base.
- As multi-family redevelopment sites become available, the City could consider additional financial and placemaking benefit opportunities in supporting this development. For example, locating multi-family development near transit networks, existing parking structures, or walkable retail corridors to increase foot traffic to existing small businesses that struggled during the pandemic.
- The city was highly engaged with local businesses and did a good job with troubleshooting during the pandemic. Some issues, such as parking and workforce attraction issues, emerged less as a crisis point as a result of the pandemic and more as a systematic issue to address with a long-term operational approach. Therefore, consideration of a strategic approach using urban planning and economic development expertise to address some of these issues may be needed.

Enhancements to livability for resident and business engagement and retention

Palo Alto is a desirable community to live and to work in, which is supported by the strong economic indicators discussed in this report. However, even a successful community needs to look to the future, and to continue to enhance its position for businesses and residents. Some additional considerations to enhance livability to support positive resident and business engagement and retention include:

- Create experiences in downtown spaces and retail locations to attract resident attention and support, increase visitors, and prolong time spent in the walkable “Main Street” corridors, such as California Avenue and University Avenue.
- Enhance opportunities for more and different events in coordination with Stanford, since Stanford enrollment and visitor events have a positive impact on retail sales and hotel stays, as well as adding vibrancy and interest for college students and residents.
- Protect and market natural assets and areas since open space and natural assets are at a premium in the Bay Area and Southern Peninsula.
- Continue dialogue and ongoing engagement with current residents to guide delivery of relevant, high-quality city services.



City of Palo Alto

Policy and Services Committee Staff Report

(ID # 13911)

Meeting Date: 3/8/2022

Title: Presentation of the FY22 Risk Assessment Report & Audit Plan

From: City Manager

Lead Department: City Auditor

Recommendation

The City Auditor recommends that the Policy and Services Committee take the following actions and forward the corresponding reports to the City Council for consent:

- 1) Review the Fiscal Year 2022/23 Risk Assessment Report and Recommend City Council Approval
- 2) Review the Fiscal Year 2022/23 Audit Plan Report and Recommend City Council Approval
- 3) Review the following Task Orders identified in the Audit Plan Report and Recommend City Council Approval
 - Remote and Flexible Work Study
 - Cybersecurity Assessment
 - Wastewater Treatment Plant Agreement Audit

Executive Summary

Baker Tilly conducted a comprehensive Risk Assessment in FY21, which was used as the basis the FY22/23 Risk Assessment. In order to make updates to the assessment, Baker Tilly spoke with City Council members and executive leadership across 14 departments within the City. In addition, executive leaders were asked to complete a survey that evaluated the potential opportunities and threats to their departments and the City as a whole. Baker Tilly analyzed the results of the survey and conducted additional interviews, as necessary.

The Risk Assessment identifies 15 risks rated as high to the organization among 154 total risks listed. The FY22/23 Audit Plan was prepared based on the results of the risk assessment, conversations with leadership, and other matters.

Background

In its capacity serving as the City Auditor function, and in accordance with [Baker Tilly's agreement with the City](#) (Task #2 of the agreement), Baker Tilly performed a citywide risk assessment. The purpose of the assessment was to identify and prioritize risks in order to develop the annual audit plan (Task #1). During the risk assessment, Baker Tilly assessed a wide range of risk areas, including strategic, financial, operational, compliance, technological, and reputation risks. The comprehensive risk matrix is included as an appendix to the report. Baker Tilly will provide a presentation to the Committee to discuss the results of the Risk Assessment and is asking that the Committee recommend approval of the report by City Council.

The Palo Alto Municipal Code ([Section 2.08.130](#)) requires the City Auditor prepare and submit an annual audit plan to the City Council for review and approval. Baker Tilly performed the initial risk assessment after having started to serve as the Office of the City Auditor in October 2020 and submitted in early 2021 the FY21-FY22 annual audit plan identifying audit activities across an 18-month horizon (through FY22). The OCA updated the initial risk assessment in January 2022, one year after our initial risk assessment. This audit plan covers the remainder of FY22 as well as FY23 and was prepared based on the results of the updated risk assessment described above.

Baker Tilly plans to present the audit plan and is asking that the Committee recommend approval of the audit plan report by City Council. Upon approval of the audit plan, the Task Orders will be approved by the Policy & Services Committee Chair.

Discussion

The attached reports summarize the analysis of the risk assessment and the outline of potential future audit activities derived from the report.

Timeline, Resource Impact, Policy Implications (If Applicable)

Timeline for risk assessment and audit plan is for FY22-23. The audit plan assumes that the Office of the City Auditor will be allocated a similar budget in FY23 as in FY22. The budget will be approved at a future point, and may necessitate review of the Audit Plan. The City Auditor will bring any necessary changes to the Committee and to City Council.

Stakeholder Engagement

The Office of the City Auditor worked with Executive Leaders from 14 Departments across the City and engaged the City Council.

Environmental Review

Environmental review is not applicable to this activity. **Attachments:**

- OCA - Risk Assessment Report FY22-23 (Final Draft for P&S)
- OCA - FY22-23 Audit Plan (Final Draft for P&S)



City of Palo Alto

Office of the City Auditor

FY22 Annual Risk Assessment

February 15, 2022

Attachment: OCA - Risk Assessment Report FY22-23 (Final Draft for P&S) [Revision 1] (13911 : Presentation of the Office of the City Auditor's

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Introduction

According to City Ordinance of the City of Palo Alto (the City), the mission of the Office of City Auditor (OCA) is to promote honest, efficient, effective, economical, and fully accountable and transparent city government. To fulfill this mission, the OCA conducts performance audits and performs financial/operational analyses of city departments, programs, services, or activities as approved by the City Council. ([Section 2.08.130](#)). In its capacity serving as the City Auditor function, and in accordance with [Baker Tilly's agreement with the City](#) (Task #1 of the agreement), Baker Tilly conducted the FY22 citywide risk assessment in order to develop the FY22/FY23 annual audit plan (Task #2).

The [California Government Code Section 1236](#) requires all cities that conduct audit activities to conduct their work under the general and specified standards prescribed by the Institute of Internal Auditors (IIA) or the Government Auditing Standards (GAO) issued by the Comptroller General of the United States, as appropriate. According to the IIA Standard 2010, the head of internal audit function “must establish a risk-based plan to determine the priorities of the internal audit activity, consistent with the organization’s goals” and consider the input of senior management and a governing board.

The purpose of the risk assessment is to develop an internal audit plan that assigns internal audit resources to the activities that add the most value to the City. The risk assessment process involves identifying, measuring, and prioritizing risks associated with the audit universe (list of specific departments, functions, processes, programs, etc. that can be subject to an audit). Risk is defined as “the possibility of an event or condition occurring that will have an impact on the ability of an organization to achieve its objectives.”¹

Our risk assessment involved collaboration with City Council and executive leadership from 14 main departments across the organization. This report summarizes our risk assessment methodology, analysis, and results. The FY22/FY23 annual audit plan is based on the results of this risk assessment.

Through the risk assessment, we observed certain strengths of the City. Key strengths include:

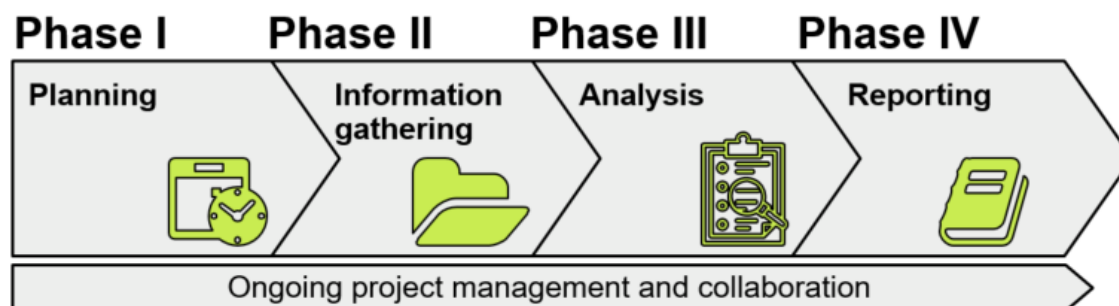
- Commitment to public service
- High value on efficient and effective government
- Focus on long term strategy
- Dedicated and highly professional management and staff
- Demonstrated history of innovation and commitment to sustainability

Additionally, OCA commends the City for its continued response to COVID-19. In particular, we greatly admire all efforts taken to support the health and wellbeing of Palo Alto citizens and Stanford students, as well as the support of essential workers during this time of heightened risk.

¹ Rick A. Wright Jr., CIA, “The Internal Auditor’s Guide to Risk Assessment” The Institute of Internal Auditors Research Foundation (IIARF), 2018

Risk Assessment Approach

Baker Tilly's risk assessment approach consisted of the following phases:



FY22 Risk Assessment Phase	
Planning	<ul style="list-style-type: none"> – Discussed a survey using an online survey tool with the City and the Baker Tilly internal resources. – Prepared risk assessment survey questions and the online survey tool.
Information Gathering	<ul style="list-style-type: none"> – Reviewed key documentation such as the capital plan, annual budget, organizational charts, financial statements, and internal audit reports. – Sent a link to the online survey to ELT members, asking them to complete the survey and forward it to their staff members as appropriate. Survey responses were downloaded in Excel spreadsheet. – Updated the risks in the existing risk matrix based on interviews with City Council members and the ELT members, survey responses, and review of critical documents.
Analysis	<ul style="list-style-type: none"> – Analyzed the survey responses. – Scored the risks in the risk matrix based on the likelihood and the impact of potential adverse events. – Identified potential internal audit activities with high risk scores.
Reporting	<ul style="list-style-type: none"> – Summarized the approach and results of the risk assessment.

Baker Tilly conducted an initial comprehensive risk assessment in FY2021 by interviewing all Council members and Executive Leadership Team (ELT) members to create a risk matrix. For the FY2022 risk assessment, we interviewed all available Council members, surveyed all ELT members and some additional members of management, and conducted interviews with key ELT members representing areas of perceived high risk in the current landscape (e.g., Information Technology, Human Resources).

Our initial FY2021 risk assessment primarily measured inherent risk (the risk without mitigating controls/factors). We continue to learn the City's risk responses, processes, controls, and/or other factors in place to mitigate identified risks through internal audit activities. We considered the information gathered to identify risks and determine the likelihood and impact of risks identified.

The risk matrix in [Appendix B](#) includes our risk rating scale and lists all of the identified risks and associated likelihood and impact of potential adverse events.

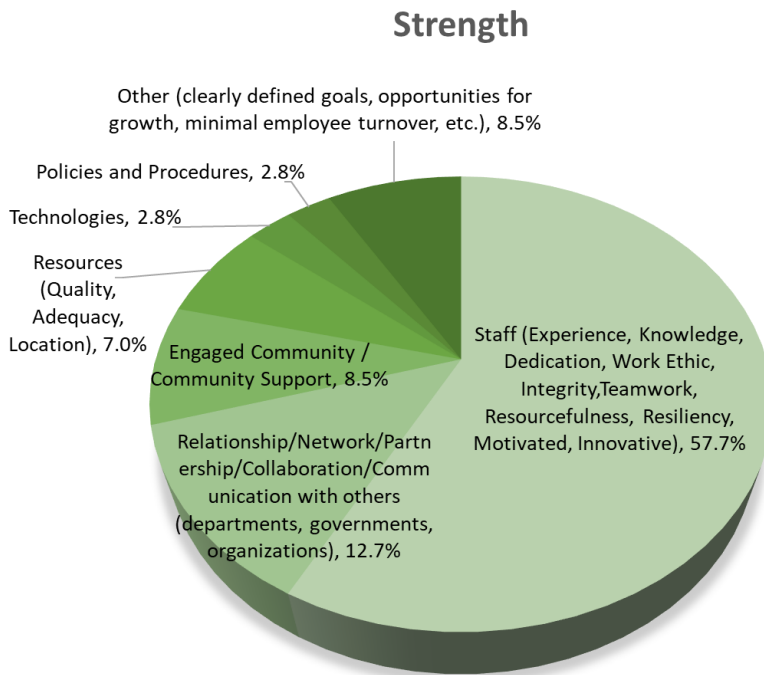
Survey Results

Baker Tilly team conducted an online risk assessment survey to gather management’s insights for all City departments and received 24 responses. The survey questions are listed in [Appendix A](#).

Management’s View of Strengths and Weaknesses/Threats

Each manager was asked to identify up to three strengths of his/her team/department or the City. The following summary shows that the employees are the strength of the City and that the relationships and collaboration with different departments and organizations are an integral part of the City’s operation.

Managers were also asked to identify up to three weaknesses as well as threats for their teams/departments or the City. The results show that the City currently faces various issues related to human capital management. Additionally, economy, rising costs, aging population, and a supply chain issue were listed as some of the threats (unfavorable external factors).



Weakness / Threat



Key Risk Areas Rated by Management

We asked the managers who participated in the survey to rate 38 risk factors across five risk categories, using a scale of 1 (Very Low) to 5 (Very High), to assess their teams/departments. As shown in the table below, five out of top ten risk factors rated high by the City's management belong to the Environmental risk category. Each risk category is summarized below, and the detailed descriptions of risk factors are included in the survey in [Appendix A](#).

Rank	Risk Category: Risk Factor	Average Rating
1	Environmental: Economy	4.04
2	Environmental: Citizen Demands	3.71
3	Organization: Succession Planning	3.63
4	Environmental: Regulatory	3.46
5	Environmental: Reputation	3.42
6	Strategy: Planning and Budgeting	3.38
7	Organization: Human Capital Management	3.33
7	Organization: Governance	3.33
9	Environmental: Legal	3.25
10	Strategy: Strategic Change	3.17

Environmental (Factors external to the organization)

Five out of six risk factors in this category are included in the top ten high-risk factors. External factors, such as the economy and citizen demands, are identified as the highest areas of Environmental risk category. Compliance with laws and standards and the opinions and perceptions of the public and customers towards the City (Regulatory) are also rated higher than other risk factors. Legal risk is the potential for an unforeseen event to cause litigation for the City or its elected leaders, directors, and officers.

Risk Factor	Average Rating
Economy	4.0
Citizen Demands	3.7
Regulatory	3.5
Reputation	3.4
Legal	3.3
Technologies	2.5
Environmental	3.4

Strategy (Planning and decision-making)

Risk Factor	Average Rating
Planning and Budgeting	3.4
Strategic Change	3.2
Resource Allocation	3.1
Compliance Management	3.1
Financial	2.8
Investments	2.8
Inter-government Relations	2.6
Strategy	3.0

The top two risk factors of this risk category concern financial management necessary to achieving the City's goals (Planning and Budgeting) and the City's ability to modify its processes in order to either align with its current strategy or to achieve a different strategic goal (Strategic Change). The Compliance Management risk factor refers to the continuous monitoring of the organization's ability to operate within regulatory requirements and community standards

Organization (Attributes of departments)

Three risk factors in the Organization category are included in the top ten risk factors. The Succession Planning risk factor is rated as the third highest risk factor. It is the planning and processes to ensure that there are highly qualified people in key leadership positions today and in the future. The related risk factor rated as the seventh highest is Human Capital Management that is the set of practices an organization uses for recruiting, managing, developing, and optimizing their human capital. Governance is also rated as the seventh highest overall and relates to the activities providing direction and oversight for the organization.

Risk Factor	Average Rating
Succession Planning	3.6
Governance	3.3
Human Capital Management	3.3
Communication	2.9
Leadership and Authority	2.9
Safety	2.7
Organizational Structure	2.7
Empowerment and Values	2.6
Ethics and Code of Conduct	2.5
Organization	2.9

Process and Operations (Functional effectiveness and policies and procedures)

Risk Factor	Average Rating
Human Resources	3.1
Procurement/Sourcing	3.0
Change Management	3.0
Efficiency	2.9
Information Systems	2.8
Vendor Management	2.8
Fraud	2.5
Contracts	2.5
Accounting	2.3
Payroll	2.2
Process and Operations	2.7

The Process and Operations risk factor was not represented on the top ten risks rated by the City's management. However, the top three risk factors of this category are the 13th through 15th risk factors among all 38 risk factors. Human Resources concerns the knowledge, skills and experiences, and resources among personnel, which allow for the execution of the organization's business plan and achievement of its critical success factors. Procurement/Sourcing pertains to the ability to acquire the necessary goods and services for operation and the process of vetting, selecting and managing supplier, vendors and contractors.

Information (Data governance)

This Information risk category had the lowest average rating among the five categories. The risk factor rated highest by City management in this category is the availability of relevant critical information when needed in order to maintain the organization's critical operations and processes, including when a disaster or unplanned disruption occurs. The Security (any event that could result in the compromise of organizational data) is rated as the second highest risk.

Risk Factor	Average Rating
Information: Availability	2.8
Information: Security	2.7
Information: Retention	2.7
Information (Data Governance): Data Integrity	2.6
Information: Privacy	2.5
Information: Access	2.3
Information	2.6

Significant Changes in FY21

We asked the managers who participated in the survey to describe the significant changes for their teams or departments during the past 12 months. The responses seem to be consistent with the effect of a significant reduction of staff in FY21 as described in the FY22 Adopted Operating Budget as well as the national labor market facing all industries.

Significant Changes During Last 12 Months	% of Respondents
Change in Workload	64%
Workforce Reduction	44%
New Workflows or Business Processes	40%
Change in Compliance Requirements (Due to Changes in Policies/Contracts/Laws/Regulations)	32%
New/additional Staff	32%
Change in Organizational Structure	32%
Other (No Significant Change, Staff Turnover, Mandatory Overtime)	24%
Changes in Processes/Controls/ Information Technology Systems	24%
New Software	20%
Increased Undesirable Performance or Instances (such as Injuries/Complaints/Customer Dissatisfaction)	16%
Change in Culture	16%
Change in Goals/Objectives/ Performance Measures	12%
New Vendors and Contractors	12%
Change in Any Risks Previously Identified for Your Team/Department	4%

Barriers to Meeting Goals and Objectives in FY22

We asked the managers who participated the survey to describe the possible reasons that prevent their teams or departments from meeting their goals and objectives in FY22. These responses are consistent with the weaknesses and significant changes mentioned by them in this survey.

Barriers to Meeting Goals and Objectives in FY22	% of Respondents
Staffing Constraints	88%
Financial Constraints	48%
Limited Skills/Knowledge/Experience/Training	32%
Constraints due to COVID-19	24%
Community Pressure	24%
Inefficiency in Process and/or Communication	20%
Technology Issue	20%
Other (Changing Priorities/Goals/Assignments Bottlenecks)	16%
State/Federal Regulations	12%
Lack of or Ineffective Internal Controls	4%

Risk Assessment Results

We developed the risk matrix in FY21 during our first risk assessment for the City. For the FY22 risk assessment, we updated the matrix by identifying the changes that have occurred (e.g. City's goals, organizational structure, etc.) over the past 12 months, obtaining input from City Council members and the City's management, and by continuing to learn more about the City's programs, initiatives, and processes. We added additional information to the existing risks, added or removed risks, and adjusted the rating, as necessary. The updated risk matrix is included in [Appendix B](#). The following chart shows the distribution of overall risk scoring in our risk matrix. We do not necessarily seek a normal distribution but do consider distribution to evaluate the effectiveness of our scoring methodology, which has been right-sized to the City.



Listed below are the risks with a score over 36 (out of 50) in the risk matrix, excluding six risks that were audited in FY21 – FY22 or are currently being audited. The list includes 15 areas rated as high risks (with a score between 40 and 50) and 20 areas rated as high-moderate risks (with a score 36 and 38). In determining the audit activities to be performed in FY22 and in FY23, we further review these risks and functional areas and consider risk-based priorities as well as other factors such as requirements by law or regulation, timing of activities, special projects, and requests from City Council and management.

Functional Area	Title	Likelihood (1-5)	Impact (1-5)	Score
City Wide	COVID-19 Response	5	5	50
Org Wide	Employee Retention & Succession Planning	5	4	46
Planning and Development Services	Long Range Planning	5	4	46
Information Technology	Disaster Recovery Preparedness and Testing	3	5	44
Information Technology	Host Intrusion and Malware Defense	3	5	44
Information Technology	Problem Management and Incident Response	3	5	44
Transportation	Contract Management	3	5	44
Org Wide	Workforce	4	4	42
Org Wide	Citywide Risk Management	4	4	42
Administrative Services	Procurement	4	4	42
Fire	Emergency Medical Service	4	4	42
Human Resources	High Cost Claims	4	4	42
Human Resources	Workload	4	4	42
Information Technology	Mobile Device Management	5	3	40
Information Technology	Strategy and Governance	5	3	40
Public Works	Secondary Treatment Upgrades	2	5	38
Public Works	ADA Compliance Upgrade	2	5	38
Administrative Services	Investments, Debt, and Cash Management	2	5	38
Information Technology	Information Security	2	5	38
Information Technology	Operations and Monitoring	2	5	38
Information Technology	Physical and Environmental Controls	2	5	38
Information Technology	Ransomware	2	5	38
Police	Use of Force and Officer Conduct	2	5	38
Org Wide	Governance	3	4	36
Org Wide	Organizational Culture	3	4	36
Administrative Services	ERP System Upgrade	3	4	36
City Wide	Sustainability and Climate Action Plan	3	4	36
Administrative Services	Accounts Receivable	3	4	36
Fire	Fire Suppression	3	4	36
Fire	Fire Prevention - Palo Alto Foothills & Wildland Fire Risk	3	4	36
Public Works	Public Services - Fleet	3	4	36
Public Works	Wastewater Treatment Plant Operations	3	4	36
Public Works	Public Services -Facilities	3	4	36
Utilities	AMI (Advanced Metering Infrastructure) Project	3	4	36
Utilities	Rates and Rate Adjustments	3	4	36

Appendices

Appendix A: Survey Questions

The Office of City Auditor is conducting the FY22 Risk Assessment to identify and prioritize risks in order to update the annual audit plan. As part of our FY22 Risk Assessment, we are conducting a survey. This survey is used primarily to collect information related to changes in operations, emerging issues and risks the City faces, and to gather your perspective on key risks faced by your department. Your candid responses would be greatly appreciated to assess the risks that prevent the City of Palo Alto from achieving its mission, goals, and objectives.

Note: Although we may reach out to some of you to discuss specific topics further, your identity will not be part of our risk assessment report.

1. Please provide your name, title, Department, and e-mail address:

- Name
- Title
- Department
 - City Council
 - City Attorney
 - City Manager's Office – Other than Transportation
 - City Manager's Office – Transportation
 - Administrative Services
 - City Clerk's Office
 - Community Services
 - Emergency Services
 - Fire
 - Human Resources
 - Information Technology
 - Library
 - Planning
 - Police
 - Public works
 - Utilities
- E-mail address

2. Are you a head of your department?

- Yes
- No – Please briefly describe the specific function or process for which you are responsible.

3. Describe any significant changes for your team or department during last 12 months.

- New software
- New workflows or business processes
- Changes in processes, controls. Or information technology systems
- Change in organizational structure
- Change in culture
- Workforce reduction
- New/additional staff
- New vendors and contractors

- Change in workload
- Change in compliance requirements (due to changes in policies, contracts, laws, or regulations)
- Change in goals, objectives, or performance measures
- Increased undesirable performance or instances (such as injuries, complaints, customer dissatisfaction, etc.)
- Change in any risks previously identified for your team/department
- N/A
- Other (please specify)

4. Are there adequate policies and procedures to perform your job responsibilities?

- Yes
- No – Please describe how the responsibilities and requirements are communicated in a clear and consistent manner.

5. Describe what can possibly prevent your team/department from meeting its goals and objectives in FY22.

- Financial constraints
- Staffing constraints
- Limited skills, knowledge, experience, training
- Technology issue
- Inefficiency in process and/or communication
- Ambiguity in roles and responsibilities
- Lack of or ineffective internal controls
- Community pressure
- State/Federal regulations
- Constraints due to COVID-19
- N/A
- Other (please specify)

6. Describe the complexity of the processes in your team or department:

Complexity is a measure of the difficulty in performing a process or function. As a process or function becomes more complex, the greater the opportunity for errors.

- Very high complexity
- High complexity
- Medium complexity
- Low complexity
- Very low complexity

Please provide any comment related to complexity, if necessary.

To help us identify potential risks, please list your team/department's Strengths, Weaknesses, Opportunities, and Threats (SWOT) for achieving its missions, goals, and objectives. Typically, strengths and weaknesses are internal aspects of team/department/organization, while opportunities and threats are found externally.

7. Describe up to three STRENGTHS of your team or department:

Strengths refer to the resources or capabilities that help the team/department accomplish its mission and serve the public. These can be things like competitive advantages, available resources, engaged community, strong balance sheet, utilized technology and so on.

8. Describe up to three WEAKNESSES of your team or department:

Weaknesses refer to the areas where the team/department needs to improve to accomplish its mission. These can include things like deficiencies in resources and capabilities, inefficient use of available technologies, barriers or inability to collaborate among different departments, lack of effective communication, mission or direction, high levels of debt, financial or human resources constraints and so on.

9. Describe up to three OPPORTUNITIES for your team or department:

Opportunities are any area where the team/department can grow. They are often related to the organization's strengths. Outside factors that affect the organization in a favorable way can include things like; offering more products or services to citizens, lower costs through new technology and so on.

10. Describe up to three THREATS for your team or department:

Threats include the level of competition, the overall economy and any other external issue that can harm the team/department. Common threats include things like rising costs for housing/living, increasing competition, tight labor supply, billing rates and so on.

11. Environmental (factors external to the organization): For each risk category described below please assess the potential risk level to your department based on a scale of 1 (Very Low) to 5 (Very High).

- **Reputation** - The opinions and perceptions of the public and customers toward the organization.
- **Regulatory** - Laws and standards, which the organization must comply with in its operations.
- **Citizen Demands** - The effect that current citizens demands have on the decisions made by management for aligning tactical plans with the business strategy and the allocation of resources.
- **Economy** - The effect that current external conditions have on the decisions made by management for aligning tactical plans with the business strategy and the allocation of resources.
- **Legal** - The potential for an unforeseen event to cause civil or criminal litigation for the organization or its elected leaders, directors, officers, and employees.
- **Emerging Technologies** - The evolution of technology both within and outside of the organization's industry.

12. Strategy (planning and decision-making): For each risk category described below please assess the potential risk level to your department based on a scale of 1 (Very Low) to 5 (Very High).

- **Strategic Change** - The ability of the organization to modify its processes in order to either align with its current strategy and business model or to achieve a different strategic goal.
- **Investments** - The portfolio of both intangible and tangible investments held by the organization, and the implications of these assets on the resources, financial viability, and operations of the organization. The effect on liquidity the ability of current assets to meet current liabilities when due.
- **Planning and Budgeting** - Details of the organization's goals and the financial management necessary to achieving those goals.
- **Financial** - The goals of the organization in terms of the structure of its assets and liabilities, including the financing capability based on its credit worthiness, the ability to receive credit and the use of credit lines to achieve its business objectives.
- **Inter-government Relations** - The relationship of the organization with other government agencies that have regulatory and oversight responsibilities and shared services or citizens.
- **Compliance Management** - The continuous monitoring of the organization's ability to operate within regulatory requirements and community standards.
- **Resource Allocation** – The process for assigning and managing assets that support the organizations strategic goals

13. Organization (attributes of departments): For each risk category described below please assess the potential risk level to your department based on a scale of 1 (Very Low) to 5 (Very High).

- **Governance** - The role, composition, and major activities of the governing body of the organization in providing direction and oversight for the organization.
- **Empowerment and Values** - The ability of senior members of the organization to effectively delegate power or authority to other members of the organization.
- **Communication** - The methods of communication commonly used in the organization and the effectiveness of this communication on the operations of the organization.
- **Ethics and Code of Conduct** - The set of rules outlining the ethical practices expected of management and employees of the organization.
- **Leadership and Authority** - The members of the organization who hold power and their ability to exercise this power effectively.
- **Organizational Structure** - The configuration of units and work flows to align the behavior of the units to the higher-level goals of the organization.
- **Succession Planning** - The planning and processes to ensure that there are highly qualified people in key leadership positions today and in the future.
- **Human Capital Management** - The set of practices an organization uses for recruiting, managing, developing, and optimizing employees, including performance management (The process of creating expectations for performance, monitoring progress, and measuring the results) and training (The ability for employees to gain and develop necessary tools to ensure effective operations).
- **Safety** - The organization strives to provide a safe working environment by effectively mitigating the risks to the safety of its employees.

14. Process and Operations (functional effectiveness and policies and procedures): For each risk category described below please assess the potential risk level to your department based on a scale of 1 (Very Low) to 5 (Very High).

- **Contracts** - Contracts are adequately structured to address and mitigate risks.
- **Efficiency** - Processes are up-to-date and efficient, resulting in efficient operations and output.
- **Accounting** - The timely and accurate tracking of the financial position of the organization.
- **Payroll** - The policies, processes, and systems in place to ensure that employee compensation is reliable, timely, and accurate.
- **Fraud** - The organization uses internal controls to prevent and/or detect fraud.
- **Procurement/Sourcing** – The ability to acquire the necessary goods and services for operation and the process of vetting, selecting and managing supplier, vendors and contractors.
- **Human Resources** - The knowledge, skills and experiences, and resources among personnel, which allow for the execution of the organization’s business plan and achievement of its critical success factors.
- **Information Systems** - The facilities, systems, and connectivity in place to support data processing.
- **Vendor Management** - The need for the organization to continuously monitor the quality and reliability of vendors it uses in the course of its business.
- **Change Management** - Management adapts appropriately to the evolution of the processes and operations of the organization.

15. Information (data governance): For each risk category described below please assess the potential risk level to your department based on a scale of 1 (Very Low) to 5 (Very High).

- **Data Integrity** - Data used for making management decisions, recording information, and reporting financial activity is accurate, complete, and reliable.
- **Access** - The right to view or manipulate data is carefully granted and monitored to prevent the mishandling of data.
- **Retention** - The policies used by the organization to determine document retention in terms of the form of documents, how these documents are stored, and for how long these should be maintained.
- **Availability** - Relevant critical information is available when needed in order to maintain the organization’s critical operations and processes, including when a disaster or unplanned disruption occurs.
- **Privacy** - Organization policies are in place to ensure the correct treatment of sensitive information held by the organization.
- **Security** – Any event that could result in the compromise of organizational data. (I.e. unauthorized use, loss, damage, disclosure or modification of organizational data).

16. Do you feel that adequate internal controls are in place and performed effectively to mitigate the risks your team or department is exposed to?

Internal controls can be segregation of duties, proper approvals, application controls that prevent errors, proper training, timely communication, reconciliation of data/information, review and resolution of exception reports, and so on.

- Yes – Processes and procedure are in place and performed effectively
- Yes – Processes and procedures are in place but NOT always performed effectively
- No – Processes and procedures are not in place to mitigate risks

Please provide any comment related to complexity, if necessary.

17. What would be the potential impact of significant risks not being addressed in your team or department?

- Reputation of the team/department or the City will be damaged
- The team/department or the City will be in noncompliance with contracts, laws or regulations
- The operations or procedures will be inefficient, which may result in more costs and/or decreased level of services
- The team/department will not meet its objectives, goals, and mission
- The consequences may be result in injuries or deaths
- The City may lose assets (cash, properties, equipment, etc.)
- The information provided to the public will be incomplete, inaccurate, and/or untimely.
- No or little impact
- Other (please specify)

18. Please share your thoughts on any risks you think your team/department or City of Palo Alto faces:

For example, risks you identified for other teams or department; risks of frauds (corruption, misappropriation of assets, financial statement fraud); and so on.

19. Please list any potential audit activities you recommend based on the risks you identified.

Appendix B: Risk Matrix

For purposes of scoring risks based on likelihood and impact, Baker Tilly categorized risks in the following manner:

- **Environment, Strategy, and Governance** – Generally speaking, these risks affect the entire organization rather than a specific department or function.
- **Major Projects and Initiatives** – These are risks related to on-going projects and initiatives; generally speaking, the duration of the project lasts only as long as the project itself (i.e., they are not inherent to the organization).
- **Function Specific Risks** – These risks are inherent to a function with no timetable for completion.

Likelihood of an Adverse Event

Likelihood Definitions		
Likelihood	Scale	General
Very Likely	5	Weekly (50+ occurrences annually)
Likely	4	Monthly (10-50 occurrences annually)
Somewhat Likely	3	Annually (>10 occurrences annually)
Unlikely	2	Once every 2 years
Rare	1	Less than once every 2 years

Impact of an Adverse Event

The table below shows the scoring methodology for major initiatives and projects:

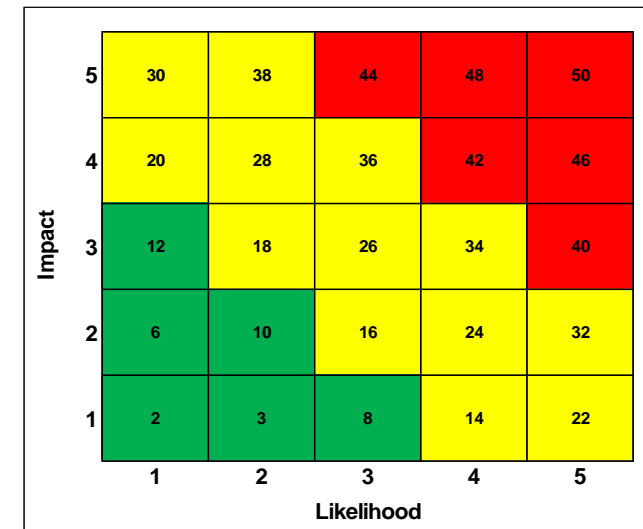
Impact - Major Initiatives		
Impact	Scale	Financial
High	5	\$50M+
Elevated	4	\$25M - \$49.99M
Moderate	3	\$10M - \$24.99M
Minor	2	\$5M - \$9.99M
Insignificant	1	<\$5M

The table below shows the scoring methodology for function specific risks as well as general organization wide risks:

Impact Definitions - General			
Impact	Scale	Financial	General
High	5	Event causes a \$100k or greater impact to revenue, expense, or net revenue	Very significant and long term impact to revenue, profit, brand/company image, and/or people
Elevated	4	Event causes a \$50k - \$100k impact to revenue, expense, or net revenue	Significant and sustained impact to revenue, profit, brand/company image, and/or people
Moderate	3	Event causes a \$25k - \$50k impact to revenue, expense, or net revenue	Moderate and short-term impact to revenue, profit, brand/company image, and/or people
Minor	2	Event causes a \$5k - \$25k impact to revenue, expense, or net revenue	Moderately low impact to revenue, profit, and/or brand/company image which can be overcome w/in 1 year
Insignificant	1	Event causes less than \$5k impact to revenue, expense, or net revenue	Low impact to revenue, profit, and/or brand/company image which can be overcome within one quarter of occurrence

Overall Risk Scoring

Following the scoring of likelihood and impact, each risk is assigned an overall score based on the methodology outlined in *The Internal Auditor's Guide to Risk Assessment* by Rick Wright Jr. Red represents high risk, yellow represents moderate, and green represents low.



Note: Examples of Potential Risks

Included in the Risk Detail column of the Risk Matrix in the following pages are examples of potential risks. These are examples of risks inherent in the activities before any controls are applied to reduce risks. The inherent risks are identified to understand what could go wrong without mitigating factors or controls.

Risk Matrix - Environment, Strategy, and Governance Risks (Risks 1-13)

The following table summarizes risks related to **Environment, Strategy, and Governance**.

Note: Examples of Potential Risks included in the Risk Detail column of the Risk Matrix on the following pages are examples of potential risks inherent to the function. These are examples of risks in the activities before any controls are applied to reduce risks. The inherent risks are identified to understand what could go wrong without mitigating factors or controls. These are not intended to communicate actual issues or challenges.

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
1	Org Wide	Ethics	Title 2 - Administrative Code, Part 7 Ethics in Contracting Title 2 - Administrative Code, Chapter 2.09 Conflict of Interest for Designated Positions	Ethics is mentioned directly in the City Code as it pertains to purchasing/contracting. The City Code intends to prevent conflicts of interest in the purchasing process and requires employees from withdrawing from participation in a purchasing or contracting activity where a real or perceived conflict exists. Additionally, the City has adopted a Conflict of Interest Code in accordance with the CA Political Reform Act. The City of Palo Alto has a Fraud, Waste, and Abuse Hotline in place and corresponding administrative policy. The objective of the Hotline is to encourage anonymous reporting of potential instances of fraud, waste, and abuse. The Hotline is monitored by a committee consisting of the 3 members - the City Manager, City Auditor, and City Attorney. Examples of Potential Risks (Note): >Instance of fraud, waste, or abuse involving a City employee or contractor engaged by the City >Conflict of interest in the purchasing process whereby a City employee improperly influences a City purchasing decision	1	5	30	Financial Legal & Compliance Reputation
2	Org Wide	Governance	Charter of the City of Palo Alto, Article III. Council Charter of the City of Palo Alto, Article III. Council, Section 9	FY22 Risk Updates: In the risk assessment survey, Governance was rated as the seventh highest risk by management. Some of the risk assessment interviewees have a concern about governance, and some have a concern about risk management. FY21 Risks: The City of Palo Alto is governed first and foremost by its citizens. The citizens of Palo Alto elect seven members of City Council, who in turn elect the Mayor and Vice Mayor. The City Council is the governing body of the City and is responsible for all legislation. The Council also sets the strategic direction and priorities of the City. It approves the budget, adopts ordinances and resolutions, and functions as a board of appeals. The City Council also appoints the City Manager, City Attorney, City Clerk, and City Auditor. The City Council has committees including the Policy & Services Committee and the Finance Committee. The City Council also appoints members to Boards and Commissions including the Human Relations Commission, the Utilities Advisory Commission, and the Public Art Commission. The Executive Leadership Team is the administrative function of the City and is made up of leaders from different departments across the City. The Executive Leadership Team is led by the City Manager. Examples of Potential Risks (Note): >Acting outside the bounds of delegated authority >Misuse and abuse of authority for personal gain >Conflicts of interest in appointees by City Council >Non-compliance with the City Charter	3	4	36	Strategic Operational Legal & Compliance Reputation Political & Economic
3	Org Wide	Labor Environment		City of Palo Alto employees are represented by seven unions and collective bargaining agreements. Palo Alto must maintain ongoing negotiations, handle disputes, and mitigate conflicts from becoming larger, more costly issues. Labor contracts include: >International Association of Fire Fighters (IAFF) >Management and Professional Personnel and Council Appointees (MGMT) >Fire Chief's Association (FCA) >Palo Alto Peace Officers' Association (PAPOA) >Palo Alto Police Management Association (PAPMA) >Service Employees International Union (SEIU) >Utilities Management and Professional Association of Palo Alto (UMPAPA) The City also adheres to other compensation plans including: >Limited Hourly Employees Compensation Plan Examples of Potential Risks (Note): >Non-Compliance with California Labor Code >Long-term financial pressures, including unfunded pension liabilities >Agreement oversight and administrative burden >Service disruptions due to extended contract negotiations	3	3	26	Operational Financial Legal & Compliance Reputation Political & Economic

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Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
4	Org Wide	Financial Planning and Budgeting	Title 2 - Administrative Code, Chapter 2.28 Fiscal Procedures	<p>The adopted budget is released annually in August. The preparation of the budget begins in September of the prior year. The Office of Management and Budget (OMB) in the Administrative Services Department develops the operating and capital budgets. The OMB works with senior management and the City Manager to develop budgets accordingly. Per the Capital Budget for FY21, there are six sources that inform the budget:</p> <ul style="list-style-type: none"> >The City Council's top priorities and other City Council directives, such as the 2014 Infrastructure Plan >Organizational financial status and budgetary guidelines >Service level and infrastructure prioritization, as identified by the City Manager >Community input (e.g. Infrastructure Blue Ribbon Commission) >The City's policies regarding land use and community design, transportation, housing, natural environment, business, and economics, as outlined in the Comprehensive Plan. <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Disagreement among City leadership and/or City Council regarding budgetary priorities >Non-compliance with City Code >Long-term financial pressures, including unfunded pension liabilities 	2	4	28	Strategic Operational Financial
5	Org Wide	Public-Private Partnerships		<p>Palo Alto partners with private organizations and non-profits. In particular, the City has established partnerships with non-profits in the administration of senior services, the animal shelter, urban forestry, local history museum, suicide prevention activities, the Zoo, and others.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Reputational damage done to the City based on actions of a partner >Financial impact of any inefficiencies >Agreement oversight and administrative burden 	3	4	36	Strategic Operational Financial Reputation
6	Org Wide	Compliance and Regulatory Environment		<p>FY22 Risk Update: In the risk assessment survey, Regulatory was rated as the fourth highest risk by management.</p> <p>FY21 Risks: Palo Alto has numerous laws and regulations, ordinances, and policies and procedures that the organization and its employee must abide by. These laws are promulgated at the Federal, State, and Local level.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Failure to track and update relevant regulations may lead to external audit findings, fines, and other punitive measures by federal and state agencies >Changing regulations may add complexity to operations and strategic planning >Non-compliance leading to enforcement action 	3	3	26	Legal & Compliance Political & Economic
7	Org Wide	Employee Retention & Succession Planning	Title 2 - Administrative Code, Chapter 2.36 Personnel Procedures	<p>FY22 Risk Updates: Recruitment and retention challenges and lack of succession plan were identified as weaknesses by many managers who took our risk assessment survey. Palo Alto living situation (Long commute, Cost of living) was listed as threat. Some of the risk assessment interviewees are concerned about succession planning</p> <p>FY21 Risks: Many factors impact employee recruitment and retention within the City.</p> <p>The Public Employee Pension Reform Act of 2013 (PEPRA) ultimately made public employment less attractive in the State. The new benefits structure lowered retirement benefits to State employees.</p> <p>Palo Alto and the surrounding area has a high cost of living. For many employees, it is difficult to afford to live in or near Palo Alto, and any employees commute great distances to work for the City. For certain positions, it is difficult to recruit candidates, as there are other employment options in more affordable communities. This is especially difficult for those employees with skills in high demand, such as linemen and other employees in the trades.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Lack of succession planning or cross training may result in knowledge loss after employee separations >High levels of turnover may result in expensive hiring/training >Inability to recruit for key positions >Inability to hire qualified candidates due to greater competition from other companies/communities 	5	4	46	Strategic Operational Financial

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
8	Org Wide	Stanford University		<p>Palo Alto provides Stanford University with a variety of services, including, but not limited too; police, fire, ambulance, disaster preparedness, land use, and utilities.</p> <p>Stanford directly and indirectly serves as a revenue source for the City. Stanford University is the largest source of property taxes within the City, with \$5.5M in taxable assets for the City.</p> <p>The City and Stanford also partner on various community issues, relationships and projects. Stanford Medical and Stanford University are the first and third largest employer in Palo Alto, respectively. Palo Alto is responsible for providing services to students, faculty, staff and visitors of the University every day, as well as providing increased services for special events held by or at Stanford University every year.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Reliance on revenues generation directly and indirectly tied to Stanford University > Shared blame or reputational impact for instances that occur on or by Stanford persons or property, and City services are involved 	1	4	20	Financial Reputation Political & Economic
9	Org Wide	Organizational Culture		<p>FY22 Risk Updates: Burnout / Low Moral, Multiple competing priorities, Lack of Diversity, and Lack of Communication (Among departments) were identified as weaknesses by many managers who took our risk assessment survey.</p> <p>FY21 Risks: General risk description: Culture is the system of values, beliefs and behaviors that shape how things get done within an organization. Culture risk results form potential misalignments between the values and beliefs of an organization and day to day operations.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Acceptance of deviations from policies and procedures >Culture of long hours leading to employee dissatisfaction >Lack of ethical tone at the top 	3	4	36	Operational Reputation Political & Economic
10	Org Wide	Workforce		<p>FY22 Risk Update: - FY22 Adopted Operating Budget reflects a net reduction of 86 full-time staff (equivalent of 78.85 FTE) and 102 part-time staff (equivalent of 24.73 FTE) - Workload and Limited Resources were identified as weaknesses by many managers who took our risk assessment survey.</p> <p>FY21 Risks: There are vacancies throughout the organization at all levels. Vacancies have increased workload of current employees, who must cover the same amount of work with fewer FTE's. Nationwide staffing and workforce shortages, combined with the generational highest resignations have also contributed to the City's difficulties finding potential employees.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Inability to be proactive in handling situations and concerns for the City > Burnout and resentment of staff > Exhaustion and increased safety concerns for field employees 	4	4	42	Operational
11	Org Wide	State Legislative Issues		<p>FY22 Risk Update: One of the risk assessment interviewees is concerned about unfunded state mandates. There is uncertainty with those mandates.</p> <p>FY21 Risks: State priorities and legislative action impact have increased in recent years, as the State priorities and mandates, particularly related to housing, land usage and development have become more robust. The City has to balance local priorities with legal regulations and usage from the State.</p> <p>Policies around the use of land, housing developments, low-income housing and green initiatives require additional legal action and planning considerations.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Litigation from improver use of land or housing requirements > Inability to properly grow and develop the City based on local priorities and community values > Non-compliance to State regulations resulting in delays in development, sanctions and citations 	3	3	26	Financial Legal & Compliance Reputation
12	Org Wide	Procurement and Supply Chain		<p>Worldwide raw materials and supply shortages from COVID-19 and the lack of available workforce, will continue to produce challenges for the City. There is also an associated increase in products as a result of the lack of available materials.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Increased costs of goods not incorporated into project budgets > Project schedule times will increase, increasing labor costs, opportunity costs and financial constraints > Impact to community trust and understanding as community services take longer to fulfill 	4	3	34	Strategic Operational Financial

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
13	Org Wide	Aging Population		<p>Palo Alto's community continues to age. Rising costs of living and the limited available housing have limited the ability for younger families and individuals to move into the area.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Loss of population that impacts revenues > Changing demographics that result in change of City priorities and community needs 	1	1	2	Environmental Political & Economic
14	Org Wide	Citywide Risk Management		<p>Some of the risk assessment interviewees have a concern about risk management and expressed a need for citywide risk assessment.</p> <p>The City currently has some risk management processes in Human Resources department for insurance and in Utilities department for safety.</p> <p>Excerpt from IIA position paper THE ROLE OF INTERNAL AUDITING IN ENTERPRISE-WIDE RISK MANAGEMENT "Enterprise-wide risk management (ERM) is a structured, consistent and continuous process across the whole organization for identifying, assessing, deciding on responses to and reporting on opportunities and threats that affect the achievement of its objectives.</p> <p>Responsibility for ERM The board has overall responsibility for ensuring that risks are managed. In practice, the board will delegate the operation of the risk management framework to the management team, who will be responsible for completing the activities below. There may be a separate function that co-ordinates and project-manages these activities and brings to bear specialist skills and knowledge.</p> <p>Benefits of ERM ERM can make a major contribution towards helping an organization manage the risks to achieving its objectives. The benefits include:</p> <ul style="list-style-type: none"> • Greater likelihood of achieving those objectives; • Consolidated reporting of disparate risks at board level; • Improved understanding of the key risks and their wider implications; • Identification and sharing of cross business risks; • Greater management focus on the issues that really matter; • Fewer surprises or crises; • More focus internally on doing the right things in the right way; • Increased likelihood of change initiatives being achieved; • Capability to take on greater risk for greater reward and • More informed risk-taking and decision-making." 	4	4	42	Strategic Operational Legal & Compliance Reputation Political & Economic

Risk Matrix - Major Projects & Initiatives (Risks 15-44)

The following table summarizes risks related to **Major Projects and Initiatives**.

Note: Examples of Potential Risks included in the Risk Detail column of the Risk Matrix on the following pages are examples of potential risks inherent to the function. These are examples of risks in the activities before any controls are applied to reduce risks. The inherent risks are identified to understand what could go wrong without mitigating factors or controls. These are not intended to communicate actual issues or challenges.

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
15	City Wide	COVID-19 Response		<p>Palo Alto has operated under emergency response orders in some capacity since March 2020. Mitigation and control of COVID-19 is imperative for citizen and employee safety and continued operation of City services.</p> <p>COVID-19 has created additional needs and hurdles for the City, including:</p> <ul style="list-style-type: none"> > Compliance with Federal vaccination requirements > Increased demand for public services > Transition to a hybrid virtual and in-person environment > More centralized need for internal and external communications > Discontinued shuttle services <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Inability to meet citizens demands given current financial and operational constraints > Transition of communications and operations to normal operational status > Health and safety of citizens and employees 	5	5	50	Strategic Operational Financial Legal & Compliance Reputation Political & Economic
16	Uplift Local Program	Parking Revenue		<p>FY22 Risk Updates: Length of time of road closures and suspending parking payments increased the City's risk for removing those regulations and reintroducing parking payments for Citizens. Prolonged lack of parking revenues may also impact the City's ability to fund existing projects and budgeted items. Citizens and businesses may also push-back on reopening streets and reinstating parking payments.</p> <p>FY21 Risks: The City has closed or partially closed several streets to allow restaurants and patrons more space for socially distanced outdoor dining. The City has also removed parking meters and garage parking fees during this time. The City implemented the Uplift Local Program to help support the economy and local businesses, residents and visitors.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Loss of revenues from closure or suspending parking meter and parking garage fees > Logistics for reopening of closed streets after sustained closures > Resistance from businesses and vendors on reopening streets and stopping outdoor dining and shopping 	5	2	32	Operational Financial Legal & Compliance Reputation Political & Economic
17	Administrative Services	ERP System Upgrade		<p>FY22 Risk Updates: ERP system upgrade is still planned to be done. Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: The City of Palo Alto is currently undergoing an upgrade of the ERP system. This includes two phases of efforts. The first phase is migrating upgrading to a new version of SAP. The second phase focuses on process improvement through use of the upgraded system.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Unforeseen barriers in implementation requiring change orders that delay the process and increase overall expenses > Strain on capacity associated with the level of attention required by ERP implementation > Data loss during system upgrade or subsequent efforts > System downtime leading to stoppage in the ability to provide services 	3	4	36	Operational Financial Legal & Compliance IT Reputational
18	Public Safety	Public Safety Building Construction		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes construction of the Public Safety Building. The total project budget is \$118M, \$9.4M is budgeted from FY22-FY26. Justification for the project was included in the 2014 Council approved Infrastructure Plan, which was preceded by a recommendation by the Infrastructure Blue Ribbon Commission report in 2011. Construction Contract was awarded in early 2021, with plans to complete construction in Summer 2023.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Design and operating effectiveness of internal controls over various financial aspects of the construction project > Adherence to construction contract terms and conditions > Mathematical accuracy of project related costs > Justification for change orders or changes in delivery schedules 	3	5	44	Operational Financial

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
19	Public Works	Newell Road/San Francisquito Creek Bridge Replacement		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes the continued replacement of the Newell Road/San Francisquito Creek Bridge. The total project budget is \$18.2M, \$15.0M is budgeted from FY22-FY26. Removal of the existing bridge is a necessary element of the San Francisquito Creek Joint Powers Authority (JPA) comprehensive flood management program.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Increased costs related to project delays and need to coordinate with other agencies >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation
20	Public Works	Fire Station 4 Replacement		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes construction of Fire Station 4. The total project budget is \$10.2M, all of which is budgeted from FY22-FY26. This project provides funding to replace Fire Station #4 at the corner of Middlefield Road and East Meadow Drive. The replacement facility will be based on the prior Replacement Study and Needs Assessment prepared in 2005 and the station being operationally and technologically deficient.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation
21	Public Works	Street Maintenance		<p>FY22 Risk Updates: The City approved the FY22-FY26 Capital Improvement Plan, which includes the continued upkeep and repair of various City streets. The total project budget is \$26.0M, all of which is budgeted from FY22-FY26. This project provides funding for annual resurfacing, slurry sealing, crack sealing, and reconstruction of various City streets. Using Pavement Maintenance Management Systems (PMMS) and Metropolitan Transportation Agency's Street Saver software, streets determined to be below the pavement condition index (PCI) standard minimum of 60, are to be repaired. The City Council established a goal of achieving an average City-wide PCI of 85, and intends to bring all City streets to a PCI of 85 or greater.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	4	28	Operational Financial Legal & Compliance Reputation
22	Office of Transportation	Railroad Grade Separation and Safety Improvements		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes the construction and upkeep of safety measure at railroad crossings. The total project budget is \$15.9M, \$11.7M is budgeted from FY22-FY26. Connecting Palo Alto, is a community-based process to advance the railroad grade crossing circulation study and context sensitive solutions study envisioned by the City Council.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation
23	Public Works	Airport Apron Reconstruction		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes the repaving of airport pathways. The total project budget is \$41.9M, \$4.9M is budgeted from FY22-FY26, with \$17.8M being distributed in FY21. The project includes the total re-pavement of airport runways, taxiways and pavement surfaces critical to airport safety. Average pavement condition index (PCI) for the airport was 36, below the industry standard minimum of 60, and below the City's goal of a PCI of 85. A PCI of 36 indicated a need for full pavement reconstruction.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	1	3	Operational Financial Legal & Compliance Reputation
24	Utilities	Electric Customer Connections		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes the installations of services, transformers and meters for new customers. The total project budget is \$13.5M, all of which is budgeted from FY22-FY26. During a typical year, over 200 electric services are installed or upgraded in the City. This is a recurring CIP.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
25	Utilities	Electrical Systems Improvement		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes improve the Electrical Distribution System. The total project budget is \$12.6M, all of which is budgeted from FY22-FY26. Typical activities include: increasing system capacity for load growth, replacing deteriorated capital facilities, reconfiguring/adding to the system to improve service reliability, repairing and replacing storm damaged equipment, and making general improvements to the system. This is a recurring CIP.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation
26	Utilities	Smart Grid Technology Installation		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes building a smart grid. The total project budget is \$17.6M, \$17M is budgeted from FY22-FY26. Smart grid technology, including the Smart Grid Road Map leads to cost operation savings and energy conservation.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation
27	Utilities	Fiber To The Home		<p>The City has been exploring the possibility of providing the option for residents to connect to a fiber optic network for faster internet. This would involve expanding the current fiber optic network and formalizing a new utility function. Interest in the service has been rising and the Utilities Department have been exploring the possibility of implementing a greater network of fiber optic.</p> <p>The City has engaged a consultant to perform a feasibility study.</p> <p>Examples of Potential Risks (Note)</p> <ul style="list-style-type: none"> >Financial loss associated with learning curve of new service >Resources associated with operating the new service >Risk of misalignment with broader City strategy 	2	4	28	Operational Financial Legal & Compliance Reputation
28	Utilities	Gas Main Replacements		<p>FY22 Risk Updates: The City is replacing gas mains that may be leaking, inadequately sized, and/or structurally deficient based on the City's Distribution Integrity Management Plan's mathematical model. The model is used to evaluate risks presented by PVC and steel facilities located within business districts that have been assigned the highest probability and consequence scores. The project will target replacing PVC mains and services located in business districts and steel mains and services with ineffective corrosion protection, also known as cathodic protection. Targeted streets will be coordinated with the Public Works Street Maintenance Program to complete replacement before streets are paved.</p> <p>Gas main replacements totals \$22.46M, includes four projects</p> <ul style="list-style-type: none"> > Project 23: 21,700 linear feet, at \$.46M (remaining from FY21) > Project 24: 20,209 linear feet, at \$9M > Project 25: 31,260 linear feet, at \$11M > Project 26: 13,471 linear feet, at \$2M <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation
29	Public Works	Wastewater Collection System Rehabilitation/ Augmentation		<p>FY22 Risk Updates: The City is replacing wastewater mains for outdated, rusted and under capacity wastewater systems. The 2004 Collection System Master Plan update indicated facilities that are in need of augmentation to handle growth and peak flow increases. Priority will be given to areas identified by Public Works are targeted work zones.</p> <p>Wastewater aim replacement total \$11.3M , includes four projects</p> <ul style="list-style-type: none"> > Project 29: 9,965 linear feet, at \$.35M > Project 30: 8,778 linear feet, at \$.41M > Project 31: 10,474 linear feet, at \$.52M > Project 32: 9,756 linear feet, at \$1.65M <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
30	Public Works	New Laboratory and Environment Services Building		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes construction of the Wastewater Laboratory and Environmental Services building. The total project budget is \$24.1M, \$23.8M is budgeted from FY22-FY26. The existing laboratory does not have adequate space for staff, instruments, chemical storage, and microbiology testing, the new building will allow for consolidation of staff in a single building and a larger updated lab.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	3	3	26	Operational Financial
31	Public Works	Advanced Water Purification Facility		<p>The project provides funding for an Advanced Water Purification Facility, with a total project budget of \$20.2M, \$17.2M is budgeted from FY22-FY26. The Regional Water Quality Control Plant (RWQCP) provides recycled water to the City, and currently have a TDS level of 800-900 mg/L. In 2010 City Council adopted a goal to reduce TDS to 600 mg/L, with approximately 40 potential users of recycled water waiting for connection still pending until TDS levels are lowered.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial
32	Public Works	Headworks Facility Replacement		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes the replacement of the Headworks Facility. The total project budget is \$49.1M, with the entire amount budgeted from FY22-FY26. The project was identified in the Long Range Facilities Plan and adopted by City Council in 2012. The project will replace pumping, suction and discharge pipes, manifolds, valve and additional control system and equipment of the water facility.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	4	28	Operational Financial
33	Public Works	Outfall Line Construction		<p>The project provides funding for the construction of a new parallel outfall pipe of the San Francisco Bay. The total project budget is \$10.7M, with \$10.6M budgeted for FY22-FY26. The Long Range Facilities Plan identified the need for the construction of the water line, as the system has a 54-inch outfall line and a 36 in-inch legacy outfall line, which is inadequate in passing the Plant's peak wet-weather hydraulic flow capacity of 8- million gallons per day.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	2	10	Operational Financial
34	Public Works	RWQCP Plant Repair, Retrofit and Equipment Replacement		<p>This project provides funding for the assessment, repair, and retrofit of the Regional Water Quality Control Plant's (RWQCP) concrete and metal structures; the replacement of necessary RWQCP equipment and ancillary facilities to maintain treatment reliability and existing infrastructure; and the replacement of large diameter flow meters built into the wastewater treatment system on sewers, pipes, wires, transformers, switches and components of medium voltage electrical equipment.</p> <p>The budget from FY22-FY26 is \$23.2M.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation
35	Public Works	Secondary Treatment Upgrades		<p>FY22 Risk Updates: Upgrades to the Secondary Treatment process at the Regional Water Quality Control Plant (RWQCP). The existing Secondary Treatment process has two main components: the Fixed Film Reactors (FFR) and the Activated Sludge (AS) Process. This project includes the reconfiguration of the aeration basins, modification of the AS Process, and the elimination of the FFRs.</p> <p>Justification of the project was identified in the Long-Range Facilities Plan accepted by Council in 2012. The components of the Secondary Treatment process are between 35 and 45 years old and show signs of wear and structural weakness. In FY22 the project was expanded to address the sea level rise policy implications.</p> <p>The budget from FY22-FY26 is \$126.0M, with a total project budget of \$129.0M.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	5	38	Operational Financial Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
36	Utilities	Water Tank Seismic Upgrade and Rehabilitation		<p>The City approved the FY22-FY26 Capital Improvement Plan, which includes upgrades and repairs to the water tank seismic system. The total project budget is \$26.3M, \$15.6M is budgeted from FY22-FY26.</p> <p>Work at the reservoir sites will also include the installation of: new seismic shut off valves between the reservoirs and valve vaults, new plug valves, piping and pipe supports in the valve vaults, and recoating of the interior and exterior reservoir walls.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	3	18	Operational Financial Legal & Compliance Reputation
37	Utilities	Water Main Replacement		<p>FY22 Risk Updates: The project will fund the design and replacement of structurally deficient water mains and appurtenances in Fiscal Years 2024 and 2026. Mains are selected by researching the maintenance history of the system and identifying those that are undersized, corroded, and subject to breaks.</p> <p>Water main replacements totals \$29.9M, include four projects</p> <ul style="list-style-type: none"> > Project 28:18,985 linear feet, at \$11.1M > Project 29:13,425 linear feet, at \$9.4M > Project 30:13,025 linear feet, \$9.4M <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	4	28	Operational Financial Legal & Compliance Reputation
38	Public Works	Scheduled Vehicle and Equipment Replacement		<p>The ongoing replacement of City fleet vehicles and equipment is prescribed by the City's policy on vehicle replacement, which includes guidelines based on age, mileage accumulation, and obsolescence. Timely replacement of vehicles lowers maintenance costs, helps to maintain or even increase the productivity of client departments, and allows the City to take advantage of new technology.</p> <p>The largest vehicle replacement costs are scheduled for FY23-FY26. Total budget amounts for FY22-FY26 is \$15.1M.</p> <ul style="list-style-type: none"> > FY22: \$1.4M > FY23: \$3.4M > FY24: \$3.5M > FY25: \$3.4M > FY26: \$3.4M <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to contract terms and conditions >Justification for change orders or changes in delivery schedules >On-going funding for replacement 	2	3	18	Operational Financial Legal & Compliance Reputation
39	Utilities	Gas Main Replacements		<p>The City is replacing gas mains that may be leaking, inadequately sized, and/or structurally deficient based on the City's Distribution Integrity Management Plan's mathematical model. The model is used to evaluate risks presented by PVC and steel facilities located within business districts that have been assigned the highest probability and consequence scores. The project will target replacing PVC mains and services located in business districts and steel mains and services with ineffective corrosion protection, also known as catholic protection. Targeted streets will be coordinated with the Public Works Street Maintenance Program to complete replacement before streets are paved.</p> <p>Gas main replacements totals \$29.6M, include three projects</p> <ul style="list-style-type: none"> > Project 23: 21,700 linear feet, at \$7.6M > Project 24:33,050 linear feet, at \$11M > Project 25:31,260 linear feet, at \$11M <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Design and operating effectiveness of internal controls over various financial aspects of the construction project >Adherence to construction contract terms and conditions >Mathematical accuracy of project related costs >Justification for change orders or changes in delivery schedules 	2	4	28	Operational Financial Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal Code Reference (From City Municipal and Process Ordinances)	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
40	Public Works	ADA Compliance Upgrade		<p>According to Palo Alto's ADA Transition Plan, the ADA Transition "project identifies potential noncompliant items and other physical barriers at City buildings, parking lots, and recreational facilities. The work to be performed under this contract includes the evaluation of site and program accessibility compliance to provide the basis for identification, prioritization, budgeting, and implementation of plans, as well as an updated plan and database which will be used in continuing efforts to comply with accessibility requirements as established by the ADA and State of California Building Code (CBC) accessibility provisions." This will be a multi-decade project to upgrade City-owned properties to align with ADA requirements.</p> <p>Examples of Potential Risks (Note): >Unforeseen costs associated with a multi-decade project, consuming greater Capital Improvement funds than expected >Changes in ADA regulations during the course of the project, requiring changes to the existing plan</p>	2	5	38	Operational Financial Legal & Compliance Reputation
41	City Wide	Sustainability and Climate Action Plan		<p>FY22 Risk Update: - FY22 Adopted Operating Budget reports one of the four priorities City Council selected was Climate Change (Protection and Adaptation). - Two of the risk assessment interviewees are concerned about sea level rise and one of them is concerned about climate risk in terms of adaptation of the plan and funding and the other is concerned about wildland fire.</p> <p>FY21 Risks: Palo Alto's goal is to reduce our greenhouse gas emissions 80 percent below 1990 levels by 2030. In early 2020, the City launched an update to the Sustainability and Climate Action Plan (S/CAP) to help meet our sustainability goals, including our goal of reducing GHG emissions 80 percent below 1990 levels and being completely carbon neutral by 2030. The plan includes goals and key actions in seven areas: Energy, Mobility, Electric Vehicles, Water, Climate Adaptation and Sea Level Rise, Natural Environment, and Zero Waste.</p> <p>The City currently has 100% renewable energy resource through several power purchase agreements. Next steps include electrification of cars and elimination of natural gas use in home and commercial electric appliances. As of 2019,</p> <p>Examples of Potential Risks (Note): >Reputational risk of not achieving stated goals >Costs associated with marginal improvements in greenhouse gas emission reductions</p>	3	4	36	Operational Financial Reputation
42	City Wide	Noise Pollution		<p>FY22 Risk Updates: Palo Alto is impacted by three arrival routes into San Francisco International Airport (SFO). These routes have had an ongoing negative health impact on our community and intensified due to the implementation of the Federal Aviation Administration's NextGEN Initiative.</p> <p>The City is committed to working with our citizens, Congress, the Federal Aviation Administration (FAA), SFO, SFO's Community Roundtable, neighboring city and county agencies, regional airports, noise groups, and all stakeholders associated with air traffic in Silicon Valley to find solutions which restore the quality of life of our community.</p> <p>Examples of Potential Risks (Note): >Health and safety risk associated with noise pollution. >Property value reductions >Community trust and engagement</p>	4	3	34	Financial Legal & Compliance Reputation
43	City Wide	College Terrace Market		<p>The PC ordinance (5069), and the associated Restrictive Covenant, require that a grocery store must be in continuous operation. If the grocery store ceases operations, a new grocery operator must be found. There is a six-month grace period for the property owner to find a new grocery tenant.</p> <p>Starting on February 13, 2020, daily fines of \$2,157/day began to be assessed against the property owner for its failure to have a grocery store in operation. This requirement for the continuous operation of a grocery store was established by PC Ordinance 5069 and was further amended by a restrictive covenant put in place in 2015.</p> <p>Examples of Potential Risks (Note): >Inability to identify and retain a tenant >Reputational risk associated requiring a grocery store</p>	2	2	10	Legal & Compliance Reputation
44	City Wide	Race & Equity Initiative		<p>In June 2020, the City Council adopted a resolution affirming that Black lives matter and committed to address systemic racism and bias, and honored the lives of George Floyd, Breonna Taylor, Ahmaud Arbery, and others that have fallen victim to violence at the hands of authorities. The City Council also approved the Race & Equity Framework and action plan and a series of actions including reviewing policing practices, making changes to use-of-force policies to reduce the potential for violence, and engaging the community in ongoing, thoughtful dialogue and leadership.</p> <p>Examples of Potential Risks (Note): >Inaction causing reputational damage >Improper use of force</p>	2	4	28	Financial Legal & Compliance Reputation

Risk Matrix - Function Specific Risks (Risks 45 -154)

The following table summarizes **Function Specific Risks**.

Note: Examples of Potential Risks included in the Risk Detail column of the Risk Matrix on the following pages are examples of potential risks inherent to the function. These are examples of risks in the activities before any controls are applied to reduce risks. The inherent risks are identified to understand what could go wrong without mitigating factors or controls. These are not intended to communicate actual issues or challenges.

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
45	Administrative Services	Real Estate and Property Management	2.08.150 Department of Administrative Services	<p>FY22 Risk Updates: The Real Estate team started using a new database called Spacebase to centrally manage all lease agreements. The requirements of GASB 87 (Leases) are effective for the City's fiscal year ending June 30, 2022.</p> <p>FY21 Risks: The City of Palo Alto handles many different real estate and property agreements such as easements, rights of way, leases, tie back agreements, and more. The Real Property team provides expertise on real estate matters and partners with client departments on specific real estate needs.</p> <p>Examples in which the Real Property team coordinates with client department include leases at the Cubberley Community Center and hangar space at the airport.</p> <p>Examples of Potential Risks (Note): >Inadequate technology to manage lease agreements >Lack of capacity to manage and ensure accuracy in real estate agreements >Revenue collection errors >Failure to properly implement GASB 87</p>	4	3	34	Operational Financial Legal & Compliance
46	Administrative Services	P-Card Program	2.08.150 Department of Administrative Services 2.30.240 Designated Employees' Use of Petty Cash, P-Card, or Other Credit Card	<p>The City of Palo Alto uses P-Cards throughout the organization to leverage purchasing power and improve purchasing processes. The organization has hundreds of P-Cards assigned to individuals throughout the City. P-Cards can be requested through purchasing and require supervisor approval for use. Transactions have a threshold of \$10k.</p> <p>Examples of Potential Risks (Note): >Personal expenditures on City P-Cards for items that could be interpreted as business expenses >Circumventing policy, such as splitting transactions to fall below the \$10K threshold >Information technology purchases that do not allow for proper IT oversight or governance</p>	4	2	24	Financial Legal & Compliance
47	Administrative Services	Vendor Master File	2.08.150 Department of Administrative Services	<p>At City of Palo Alto, segregation of duties as it pertains to changes to the Vendor Master File are segregated such that one individual cannot process payments and modify the vendor master file.</p> <p>Examples of Potential Risks (Note): >Accounts Payable changing payment information to a personal bank account routing number >Erroneous Vendor data leading improper payments</p>	1	3	12	Financial Reputation
48	Administrative Services	Print and Mail Services	2.08.150 Department of Administrative Services	<p>The City of Palo Alto operates a print and mail services department, managing the mailing of all utility bills, acting as a central receiving area in City Hall, and also completing any printing services. The print services division handles printing of Council packets for City Council members.</p> <p>Examples of Potential Risks (Note): >Financial and operational opportunity costs of running in-house mail services department compared to outsourcing the function</p>	2	2	10	Strategic Operational Financial
49	Attorney	Claims & Claim Reserves	2.28.240 Settlement of Claims and Actions 2.08.120 Office and Duties of the City Attorney State of California Tort Claims Act	<p>As provided in Section 935.4 of the Government Code of California, the City Attorney is designated to perform the functions of the City Council relative to claims and actions against the City or any of its officers or employees under the provisions of Division 3.6 of the Government Code.</p> <p>The City may be liable for a variety of claims including: >Torts Claims >Law Claims >Labor and Employment Claims >Contract Claims</p> <p>Risk to the City is mitigated though the City's membership in the Authority for California Cities Excess Liability (ACCEL) pool, though which the insures itself.</p> <p>Examples of Potential Risks (Note): >Property damage resulting from City actions >Motorist injuries due to an interaction with a Palo Alto staff member acting within scope of her/his employment >An employee suffers an injury while performing their job duties</p>	3	3	26	Legal & Compliance

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
50	Clerk	Public Records Requests	2.08.110 Office and Duties of the City Clerk 2.08.300 Books and records. (Ord. 4274 § 1 (part), 1995)	The City receives upwards of 400 requests for information every year. Public records requests come in a variety of ways; written, in person, online and over the phone. Compliance with the Freedom of Information Act (FOIA) and state and local jurisdiction dictate the availability of requests and outlines the procedures for providing documents to the public. Examples of Potential Risks (Note) >Incoming requests are decentralized, leaving possibility for requests to go unfulfilled >Fulfilling of requests is centralized, burdening the department and causing inefficiencies >Noncompliance with applicable laws	2	3	18	Financial Legal & Compliance Reputation
51	Clerk	Elections	Chapter 2.40 Municipal Elections	The City Clerk is the local Filing Officer for the State of California. All local campaign Committees are required to file Campaign Statements with the City Clerk. The City Clerk maintains regulations and forms under the State of California Fair Political Practices Commission. Examples of Potential Risks (Note) >Non-compliance with regulatory requirements	1	2	6	Reputation
52	Clerk	Records Management	2.08.110 Office and Duties of the City Clerk 2.08.300 Books and records. (Ord. 4274 § 1 (part), 1995)	The City Clerk is the Records Manager for the City and is responsible for maintaining the City's Records Retention Schedule and for providing departments with guidance on policies and best practices of records management. The City Clerk's Office records official actions and legislation of the municipal government and retains other legal and historical records. The City Clerk manages the proper maintenance and disposition of City records and information according to statute, and helps to preserve City history. Formalized Standard Operating Procedures (SOPs) communicate the correct way of carrying out records management activities. SOPs help the organization operate efficiently, maintain consistency, and communicate clearly. The City Clerk does not have current SOPs detailing records management and retention practices. A modern/centralized records management system may increase efficiency and offer functionality such as analytics and reporting capability. Without a centralized repository, employees use paper based files and multiple online platforms. The City of Palo Alto operates on a decentralized records management process. Examples of Potential Risks (Note) >Damage to documents from improper storage >Inability for documents and information to be accurately recorded and sourced for public information requests and public is given inaccurate information about the availability of documents >Institutional knowledge is lost when employees retire or leave the department >Records are destroyed prematurely or stored longer than legally necessary	4	2	24	Operational Legal & Compliance Reputation
53	Communications	Social Media Management	Brown Act (California Government Code Section 54950 et seq.)	Social media accounts are handled and managed by separate, decentralized departments. Content published by these accounts are not generated from a central office, but are monitored by the Communications Office. Additionally, elected official's social media posts may be considered public record and may be subject to State law. The majority of instances include the use of personal platforms to promote City agenda, issues and positions. Examples of Potential Risks (Note): >False or misleading information is published by City owned accounts >Conflicting information is provided by multiple City owned accounts >Lack of internal controls for publishing content on City owned accounts >Publishing of inappropriate or inaccurate content >Inaccurately holding and/or of managing public information for records management	3	3	26	Strategic Legal & Compliance Reputation Political & Economic
54	Communications	Digital Marketing		Digital platforms, such as websites, social media, online platforms, blog posts (Palo Alto Connect) and digital newsletters are used to disperse information and inform community members and City employees. Additionally, these platforms are used to advertise City services and events. Examples of Potential Risks (Note): >False and/or misleading information is published by the City >Publishing of inappropriate or inaccurate content	1	3	12	Strategic Legal & Compliance Reputation Political & Economic
55	Communications	External Affairs		Relations with the media and general public are primarily handled by the Communications Office. The City of Palo Alto works to timely and accurately inform the media, including a monthly newsletter, press releases, interviews, news releases to 400 media contacts and statements on behalf of departments and the City. Requests for information from media is decentralized, with the majority of responses for comments and communication coming from the Communications Department. Multiple channels are used by the City to build relationships and inform the citizens of Palo Alto and surrounding communities. The City works to engage stakeholders and provide a positive public perception by: >Communicating through its multiple platforms >Hosting community service events >Maintaining open and transparent government Examples of Potential Risks (Note): >False or misleading information is published by the City	2	2	10	Strategic Legal & Compliance Reputation Political & Economic

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
				>Conflicting statements made by City officials >Lack of internal controls for managing media requests				
56	Communications	Website		FY22 Risk Updates: 1) City website updated 2) Website maintained centrally with records of who has back-end access FY21 Risks: The City's website and affiliated websites are maintained and updated in conjunction with the Communications Office and the Information Technology Department. Both departments work with website host to update information and publish new webpages. Additionally, Individual departments have access to back-end website publishing. Examples of Potential Risks (Note) >Lack of internal controls for website access >Publishing of inappropriate or inaccurate content	2	2	10	Legal & Compliance Reputation IT
57	Communications	Internal Communications	18.79.010 Purposes	Communications oversees formal internal communications, including creation and/or review of Citywide emails, internal newsletters and communications. A centralized place of issuance for organization wide communication including City Manager and department head presentations and reporting. Examples of Potential Risks (Note): >Conflicting information is provided to City Employees >Internal communications are improperly published to the community	2	1	3	Operational
58	Community Services	Contract Monitoring	2.30 Contracts and Purchasing Procedures	FY22 Risk Updates: 1) Non-profit agreements internal audit 2) Updated internal controls for contract and vendor management 3) Diversification of contractors 4) Updated software FY21 Risks: Community Services relies on third-party contractors to manage the animal shelter, deliver recreational services (i.e. swimming pool, athletic fields, the golf course), and provide arts and theatre programs. As a result, Community Services oversees dozens of contracts and independent contractors. Examples of Potential Risks (Note): >Loss of revenue due to overpayments on contracts >Reputational risk associated with actions of a 3rd party >Failure to adhere to contract terms including scope of work and other critical provisions >Failure to monitor vendor performance	3	4	36	Strategic Operational Financial Legal & Compliance Reputation
59	Community Services	Background Check Procedures	2.08.210 Department of community services.	Community Services offers a variety of programs where workers may come into contact with children. The following is a non-inclusive list of screening practices the City uses: local criminal record check, state criminal record check, FBI criminal record check, employment reference checks, and personal reference checks. Examples of Potential Risks (Note): >Hiring of unqualified individuals >Employing an individual that should be ineligible for employment involving interactions with children	3	3	26	Operational Legal & Compliance Reputation
60	Community Services	Recreations Services		Recreation Services has a focus on youth wellbeing. Facilities include the historic Lucie Stern Community Center, Mitchell Park Community Center, Cubberley Community Center, and Rinconada Pool. Recreation Services also coordinates a variety of recreation programs including middle school athletics, the Teen Center, Palo Alto Youth Leadership programs, year-round Life-Long Learning classes, adult sports leagues, dynamic summer camp and aquatics program. Examples of Potential Risks (Note): >Resources are expended on services that are not of sufficient benefit to the community >Employing an individual that should be ineligible for employment involving interactions with children >Improper payment for services (e.g., a referee)	2	3	18	Strategic Financial Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
61	Community Services	Human Services	2.08.210 Department of community services.	<p>The Office of Human Services provides services and works toward enhancing the quality of life in Palo Alto in a variety of ways. Services relate to the following areas:</p> <ul style="list-style-type: none"> >Children Resources >Family Resources >Tenant/Landlord >Human Services Grants >Emerging Needs Funds <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Resources are expended on services that are not of sufficient benefit to the community >Ineligible program participation >Fraud/waste/abuse of public funds 	1	3	12	Operational Financial Legal & Compliance Reputation
62	Community Services	Children's Theatre	2.08.210 Department of community services.	<p>Palo Alto's Children Theatre serves more than 57,000 community members each year with theatrical productions and programs for youth ages 3 through high school. Performing arts education opportunities include onsite classes, camps, and production experiences, as well as theatrical Outreach Productions (grades 3-5) and Dance in Schools classes (grades K-2) in all twelve PAUSD Elementary Schools.</p> <p>Children's Theatre offers a variety of programs where workers may come into contact with children.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Resources are expended on services that are not of sufficient benefit to the community >Employing an individual that should be ineligible for employment involving interactions with children 	1	3	12	Strategic Financial Legal & Compliance Reputation
63	Community Services	Open Space, Parks, & Baylands Golf Links		<p>The City of Palo Alto has almost 4,000 acres of open space to explore, recreate and relax in. Park Services handles the maintenance of 162 developed acres of urban parklands. Individual parks range in size from under two acres to large community parks such as Rinconada Park, Mitchell Park, and Greer Park. Besides maintaining urban parks, Parks Services handles landscape maintenance of libraries, community centers, business districts and utility sub-stations.</p> <p>Troon, previously OB Sports, manages the newly constructed Baylands Golf Links. According to the contract, Troon is responsible for course maintenance, leases a cafe from the City, and manages a pro shop. The City receives a percentage of revenue from the pro shop. This approach to golf course management is new to the City within the past few years.</p> <p>The City has a contract with Brightview for maintenance and landscaping services on other open space and parks land.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Resources are expended on services that are not of sufficient benefit to the community >3rd party management of City resources, such as the golf course 	1	3	12	Strategic Legal & Compliance Reputation
64	Community Services	Palo Alto Art Center	2.08.210 Department of community services. 2.18 Public Art Commission	<p>The Palo Alto Art Center has a partnership with the Palo Alto Art Center (PAAC) Foundation Board. Successful fundraising efforts of the PAAC Foundation are necessary, in addition to City funds, to sustain the Art Center. The Art Center measures its progress based on the following priorities:</p> <ul style="list-style-type: none"> >Community Engagement >Financial Sustainability >Leadership capacity <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Resources are expended on services that are not of sufficient benefit to the community >Employing an individual that should be ineligible for employment involving interactions with children 	1	2	6	Strategic Financial Legal & Compliance Reputation
65	Community Services	Junior Museum & Zoo	2.08.210 Department of community services.	<p>The Palo Alto Junior Museum & Zoo has a partnership with the Friends of Palo Alto Junior Museum & Zoo. Successful fundraising efforts of Friends of Palo Alto Junior Museum & Zoo are necessary, in addition to City funds, to sustain the museum and zoo. The JMZ is owned and operated by the City of Palo Alto. The JMZ hosts more than 17,000 local students annually from schools, science camps, and field trips. In total, the JMZ has approximately 180,000 visitors per year.</p> <p>The City is exploring potential opportunities to relinquish day-to-day operations responsibilities to Friends of Palo Alto Junior Museum & Zoo. These discussions are still early stage.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Resources are expended on services that are not of sufficient benefit to the community >Transferring operating responsibilities to a non-profit may result in legal challenge from existing City employees >Failure to properly manage the JMZ may result in negative publicity and reputational damage 	1	2	6	Strategic Financial Legal & Compliance Reputation
66	Community Services	Public Art Program	Chapter 2.26 15.61.110 Public Art Fund 2.26.070 Public Art for Municipal Projects 2.26.030 Duties of the Public Art Commission	<p>The Public Art Program operates in accordance with Chapter 2.26 of Palo Alto Municipal Code to provide opportunities for the placement of permanent and temporary site-specific public art projects in municipal projects across Palo Alto. Additionally, the Program oversees the implementation of the Ordinance requirement to incorporate public art in private development projects. The Public Art Commission (PAC) reviews and advises the Public Art Program on selection, placement, and care of public art throughout the City of Palo Alto.</p> <p>The City collection of public art is comprised of approximately 100 permanently sited works and approximately 200 portable works of art in a diverse range of media. All works are commissioned and acquired through a public process.</p>	1	2	6	Strategic Financial

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
				<p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Resources are expended on services that are not of sufficient benefit to the community 				
67	Emergency Services	Disaster Response	2.08.185 Office of Emergency Services.	<p>The mission of the Office of Emergency Services is to prevent, prepare for, mitigate, respond to, and recover from all hazards. This involves:</p> <ul style="list-style-type: none"> >Executing a training plan for designated staff >Maintaining emergency management facilities, critical infrastructure, and essential equipment >Coordinating with private sector, non-governmental organizations to promote continuity of operations >Maintaining disaster plans for the City <p>The City has developed many resources and have placed them on the website: www.cityofpaloalto.org/thira.</p> <p>Example of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Inadequate response to an emergency such as an earthquake, fire, urban flood, or active shooter situation may result in injury, loss of life, financial hardship, and reputational damage to the City and its employees 	1	5	30	Strategic Operational Financial Legal & Compliance Reputation Political & Economic
68	Emergency Services	Emergency Volunteer Coverage	<p>Palo Alto Municipal Code (PAMC) Sec. 2.12.070</p> <p>2.08.185 Office of Emergency Services.</p>	<p>FY22 Risk Updates:</p> <ol style="list-style-type: none"> 1) On-going pandemic has impacted the ability to find volunteers <ul style="list-style-type: none"> • Additional COVID19 protocols • Apprehension of working with the community during the pandemic • Availability of vaccinated or proven negative volunteers 2) Aging population <p>FY21 Risks:</p> <p>In the case of emergency, the Office of Emergency Services may enlist the assistance of the community through a volunteer network. The mission of the Palo Alto Emergency Services Volunteers (ESV) is to: 1) provide supplemental resources to the professional first responders of the City and surrounding communities and 2) facilitate means for neighbors to help neighbors (including business and other entities). Emergency Service Volunteers are often times geographically concentrated in some, but not all, neighborhoods.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Lack of volunteer participation across the City/concentration of volunteers leading to inconsistent emergency response depending on location 	3	3	26	Strategic Operational Financial Legal & Compliance Reputation Political & Economic
69	Administrative Services	Tax Revenue	2.08.150 Department of Administrative Services	<p>FY22 Risk Updates:</p> <p>In the risk assessment survey, Economy was rated as the seventh highest risk by management. One of the risk assessment interviewees wants the structure of revenue sources to be looked at.</p> <p>FY21 Risks:</p> <p>The City of Palo Alto's largest sources of revenue include property taxes, sales taxes, and transient occupancy taxes. These three main sources of tax revenue. Palo Alto has been a hub for large technology businesses which bring in visitors to hotels, restaurants, and retail. These visitors and daytime population help feed the sales and transient occupancy taxes. Palo Alto property values have also risen over the last few decades, driving an increase in property tax revenue.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Large businesses moving to other locations or decreasing the focus on in-person interactions at headquarters lowers the daytime population and visitors >Decreasing real estate values due to external factors decreases City revenues from property taxes 	3	5	44	Strategic Financial Political & Economic
70	Administrative Services	Asset Management	2.08.150 Department of Administrative Services	<p>FY22 Risk Updates:</p> <p>The requirements of GASB 87 (Leases) and GASB 89 (Interest Cost) are effective for the City's fiscal year ending June 30, 2022.</p> <p>FY21 Risks:</p> <p>The City manages assets to ensure that all assets are properly accounted for both operationally and financially. Asset management is important to the accounting function as well to ensure that depreciation on all assets is being properly tracked and applied as well as classification of various assets.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Misclassification of assets, hampering the ability to properly account for depreciation and other accounting requirements >Lack of internal controls in managing and accounting for assets 	3	4	36	Operational Financial

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
71	Administrative Services	Investments, Debt, and Cash Management	2.08.150 Department of Administrative Services 2.28.140 Depositories and Investments	<p>FY22 Risk Updates: Based on the FY2022 survey and interview, investments is an area where the City may benefit from an internal audit. There is a need to update the City's investment policy to increase flexibility based on the current environment.</p> <p>FY21 Risks: Palo Alto manages their investment, debt, and cash portfolio through a single internal investment manager. This investment manager maintains the City's investment portfolio subject to the investment policy, including limits on holdings of various financial products. Maintaining an internal investments manager allows for the City of Palo Alto to avoid commissions/fees.</p> <p>In addition, the investment manager also performs cash management and cash flow modeling, executes wire transactions, serves as the bank custodian, and performs a daily cash flow reconciliation.</p> <p>Examples of Potential Risks (Note): >Financial opportunity cost from an optimized portfolio managed by an outsourced firm >Operational inefficiencies due to lack of economies of scale in comparison to an outsourced firm >Fraud/misuse/abuse risk associated with lacking or failed internal controls in regards to investments >Noncompliance with the investment policy >Over reliance on one individual to manage City investments</p>	2	5	38	Strategic Financial Legal & Compliance
72	Administrative Services	Accounts Receivable	2.08.150 Department of Administrative Services	<p>FY22 Risk Updates: > There is a lack of communication and transparency with other City Departments. >The department has goals that change frequently which may result in the inability to focus and follow through with any one goal. > The department struggles is attracting and retaining staff. > Public meetings increase pressure on the department to perform.</p> <p>FY21 Risks: The Revenue Collection and General Accounting teams manage the City's accounts receivable function. This function ensures that bills are timely, accurate and include adequate information for those who paying the City. Additionally, this function manages what payments are expected, any overdue payments, and any necessary collections. Note that this function is not responsible for utility billing.</p> <p>Examples of Potential Risks (Note): >Outstanding balances for extended periods of time >Redirected payments to personal accounts</p>	3	4	36	Operational Financial Legal & Compliance
73	Administrative Services	Credit & Debt	2.08.150 Department of Administrative Services	<p>Palo Alto's credit rating is currently AAA, the highest rating a municipality can receive. This is due in large part to high fund balances and low debt burdens. Healthy fund balances and low reliance on debt equips the City to face economic hardships or other external factors outside the City's control.</p> <p>Example of Potential Risks (Note): >Sustained decreasing revenues may require the City to diminish fund balances and rely more heavily on debt >Operational inefficiencies may result from sustained economic prosperity, leaving the City vulnerable to inefficient uses of debt and fund balances during times of economic hardship</p>	2	4	28	Financial Reputation Political & Economic
74	Administrative Services	General Accounting	2.08.150 Department of Administrative Services	<p>FY22 Risk Updates: There is a lack of skills and/or time to implement new accounting pronouncements / GASB's, which may result in being noncompliant with applicable laws.</p> <p>FY21 Risks: Palo Alto's accountants ensure that the City has accurate financial information with which to make decisions and to report to the public. The accounting function ensures that the financial statements reflect the true operations and financial state of the City.</p> <p>Examples of Potential Risks (Note): >Misstatement on financial statements >Lack of internal controls to catch accounting errors</p>	3	3	26	Strategy Operational Financial Legal & Compliance
75	Administrative Services	Budget Management	2.08.150 Department of Administrative Services	<p>FY22 Risk Updates: > There can be challenges with the OMB due to the need for coordination between City Departments and City Leadership to ensure information/requests provided align with the needs of the department to provide services in addition to that fact that various financial systems are used to maintain the budget. > OMB staff have been tasked with updating policies and procedures when changes occur to keep them current; however, turnover in staff and the decentralization of where policies are stored has caused some documentation to be updated more slowly. > There is a need for a central budgeting tool and specialized budget training. One of the risk assessment interviewees has a concern about lack of a plan around funding for infrastructure</p>	3	3	26	Operational Financial

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
76	Administrative Services	Accounts Payable	2.08.150 Department of Administrative Services	<p>FY22 Risk Updates: > There have been fraud attempts surrounding the wire payments process. Currently, the City is working to establish a formal for this process. > Staffing changes are impacting the department. There is a need to better define staff responsibilities.</p> <p>FY21 Risks: The Accounts Payable division handles payment of vendor invoices, p-card transactions, and other payments. The Accounts Payable department issues payments in a number of manners, including ACH and Checks. Accounts Payable is managed in SAP and any paper invoices are inputted into the system.</p> <p>Examples of Potential Risks (Note): >Late payment of invoices in the event invoices are not inputted into SAP >Invoices entered into the system with incorrect information, such as dates miskeyed</p>	4	2	24	Financial Legal & Compliance
77	Administrative Services	Procurement	2.08.150 Department of Administrative Services 2.30.040 Centralized Purchasing	<p>FY22 Risk Updates: > Staffing constraints may prevent the department from meeting its goals and objectives. > Financial constraints may prevent the department from meeting its goals and objectives. > Some of the risk assessment interviewees mentioned the inefficient procurement process. > Procurement/Sourcing was rated 14th highest risk factor (out of 38 risk factors) in the risk assessment</p> <p>FY21 Risks: Palo Alto has detailed policies and procedures in place for purchasing and procurement. The process includes internal controls to ensure that the organization is protected against fraud, misuse and abuse in the purchasing process. If any areas within the purchasing process are missing controls, it opens an opportunity for unethical, fraudulent, or erroneous activities. If the purchasing process has too many controls, the City may be missing opportunities for cost savings and operational efficiencies.</p> <p>Examples of Potential Risks (Note): >Burdensome internal controls slowing the purchasing process down, discouraging good vendors from bidding on projects >Lack on internal purchasing controls, opening opportunities for fraud, misuse and abuse</p>	4	4	42	Operational Financial Legal & Compliance
78	Administrative Services	Payroll	2.08.150 Department of Administrative Services	<p>Payroll ensures that all City employees are paid on time and with accuracy. Payroll must ensure that all benefit deductions, taxes, withholdings, and other individual differences in paychecks are proper and included in paychecks. This includes ensuring that any changes to employee statuses are properly reflected in paychecks.</p> <p>Examples of Potential Risks (Note): >Lack of audit prior to payroll disbursements leading to errors in paychecks, including over or under payments >Not accounting for updates to qualifying events such as marriage or new children</p>	4	2	24	Operational Financial Legal & Compliance
79	Administrative Services	Grants Management	2.08.150 Department of Administrative Services	<p>Grants Management include the pursuit of grants, the tracking of outstanding grant decisions, reporting managing any awards and associated reporting and spending deadlines.</p> <p>The City of Palo Alto does not have a centralized Grant Management Function. Rather, each department pursues grant opportunities applicable to a specific program or the department as a whole and manages the grant in accordance with the grant agreement and applicable law.</p> <p>The Administrative Services Department prepares pertinent financial reports including the Schedule of Expenditures of Federal Awards (SEFA).</p> <p>Examples of Potential Risks (Note): >Missed grant reporting deadlines >Use of grant funding on ineligible expenses >Missed grant opportunities due to inaction or delays in application writing</p>	3	2	16	Operational Financial Legal & Compliance
80	Administrative Services	Proposition 13	2.08.150 Department of Administrative Services	<p>Proposition 13, or "The Peoples Amendment to Control Taxation", caps property tax rates according to a percentage of the property value or the Consumer Product Index. This proposition limits the amount that residents can be taxed on their property in the midst of rising property values, while also limits the ability for the City to collect revenue at a rate in pace with the Palo Alto real estate market.</p> <p>Examples of Potential Risks (Note): >Lost revenue for the City to fund City services with Prop 13 in place >High taxation on residents due to increased property values, especially long term Palo Alto residents, in the absence of Prop 13</p>	1	3	12	Financial Reputation Political & Economic

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
81	Fire	Emergency Medical Service	State of California Senate Bill 201 2.08.180 Fire department.	<p>FY22 Risk Update: Various changes were noted in responses to the risk assessment survey.</p> <ul style="list-style-type: none"> - There have been numerous employee reductions - Redeployed the resources to optimize our response with less personnel (based on predictive analysis with previous years incident data and response times). - Had a higher than normal number of personnel on injury, likely from fatigue related to COVID - The increase in mandatory overtime due to personnel reductions. - The goals identified in the 5 year strategic plan and other work flows were negatively impacted due to COVID responses and reduction in staff and line positions. <p>FY21 Risks: The Fire Department operates an ambulance transfer service. The EMS Director oversees equipment, staffing, training, and all other activities associated with this ambulance function. The City is implementing an Ambulance Subscription Fee Program. The program will be voluntary and proposes to waive the insurance co-pay participants would otherwise be charged when transported to the hospital by ambulance.</p> <p>Examples of Potential Risks (Note): >Compliance with EMS Act, including Section 201 and service level requirements >Proper billing and collection of subscription fees</p>	4	4	42	Operational Financial Legal & Compliance Reputation
82	Fire	Fire Suppression	2.08.180 Fire department.	<p>FY22 Risk Update: Various changes were noted in responses to the risk assessment survey.</p> <ul style="list-style-type: none"> - There have been numerous employee reductions - Redeployed the resources to optimize our response with less personnel (based on predictive analysis with previous years incident data and response times). - Had a higher than normal number of personnel on injury, likely from fatigue related to COVID - The increase in mandatory overtime due to personnel reductions. - The goals identified in the 5 year strategic plan and other work flows were negatively impacted due to COVID responses and reduction in staff and line positions. <p>Other</p> <ul style="list-style-type: none"> - A technical rescue over a hillside or a large structure fire can be very technical. - Response time data is regularly reviewed, and an annual update is completed to the accreditation (CFAI - Commission on Fire Accreditation International) that details the performance in relation to the benchmarks established by council. <p>==== Respond to emergency and non-emergency calls Palo Alto's Hazardous Materials Team responds to calls involving hazardous materials.</p> <p>Examples of Potential Risks (Note): >Inadequate training, and certification >Improper staffing of firetruck and ambulance units</p>	3	4	36	Operational Legal & Compliance
83	Fire	Fire Prevention - Palo Alto Foothills & Wildland Fire Risk	2.08.180 Fire department.	<p>FIRE PREVENTION BUREAU Improve the quality of life for the Palo Alto community through risk assessment, code enforcement, fire investigation, public education, and hazardous materials management.</p> <p>FY22 Risk Update: - Current workforce constraints for the City and surrounding communities, as well as larger workforce shortages impact the response time or availability for mutual support. - Fire department's initiative includes rigorous wildland fire drills and trainings in order to prepare for the increased risk of a longer and more intense California fire season (FY22 Operating Budget) - One focus of climate adaption is preparation for and protection from wildfires (City of Palo Alto website) - One of the risk assessment interviewees mentioned a wildland fire risk and the effect on the climate. - One of the risk assessment survey respondents wants to see study of staffing and compensation package among similar departments. Another respondent suggests a review of the Self-Assessment Manual and a review of the current training facilities.</p> <p>FY21 Risks: The City includes land west of Highway 280, including Foothills Park. This area is served by Fire Station 8. When Fire Station 8 is not staffed, the City is heavily reliant on mutual aid.</p> <p>Examples of Potential Risks (Note): >Lack of staffing to respond to emergencies in the Foothills Park area</p>	3	4	36	Operational Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
84	Fire	Fire/EMS Training	2.08.180 Fire department.	<p>EMPLOYEE FIRE/EMS CERTIFICATION TRAINING Provide training to certify that staff maintain safe, efficient, and effective practices when responding to emergencies. Ensure personnel are familiar with and able to utilize the most up-to-date and proven techniques. Training specific to required EMT and/or Paramedic re-certification is also incorporated. FY22 Risk Update: Current workforce constraints for the City and larger shortage of EMT/EMS workers impacts the ability for the City to hire and/or train employees for proper staffing of EMT's.</p> <p>FY21 Risks: The majority of City of Palo Alto Firefighters are also certified as either EMT's or Paramedics. Palo Alto offers training for firefighters to be certified as EMT's. Paramedics and EMT's both respond to medical/rescue and fire calls. Paramedics are trained to perform additional medical services that EMT's are not certified to perform, including; starting IV's, administering medication and beginning intubation. According to NFPA safety standards and best practices, two paramedics and two EMT or BLS trained individuals should be on scene for every event.</p> <p>Examples of Potential Risks (Note): >Inadequate training facilities and staff training and certification</p>	2	3	18	Operational Legal & Compliance Reputation
85	Human Resources	High Cost Claims	2.08.160 Department of human resources.	<p>Managing high-cost claimants, including individuals suspected of "gaming the system" is critical for controlling benefits costs. Staffing models should plan for high-cost scenarios such as employees with chronic illnesses and sick leave abuse. High cost claims include both expensive chronic medical conditions and acute conditions. Major cost drivers include: >Cardiovascular disease >Pulmonary conditions >Neurological conditions</p> <p>Examples of Potential Risks (Note): >Public safety employees may place a significant financial burden on the City given the dangerous nature of the role</p>	4	4	42	Financial Legal & Compliance
86	Human Resources	Workload	2.08.160 Department of human resources.	<p>Due to departmental workload, there is a risk of employees may experience the below. Examples of Potential Risks (Note): > Lower morale > Employee health (e.g. physical, mental and emotional) > Poor communication > Human error</p>	4	4	42	Human Capital Management
87	Human Resources	Staffing Levels	2.08.160 Department of human resources.	<p>FY22 Risk Updates: The HR department experiences some technology issues that prevent the department from meeting its goals and objectives. The City is still at risk for losing HR professionals.</p> <p>FY21 Risks: Multiple departments within the City expressed challenges with staffing levels. Hiring limitations in response to COVID-19 worsened these existing challenges.</p> <p>Example of Potential Risk: >Relying on unqualified employees to perform critical tasks due to an unfilled vacancy >Non-compliance with state and federal laws due to capacity limitations >Reductions in service quality due to capacity limitations</p>	4	3	34	Operational Legal & Compliance
88	Human Resources	Employee Separation and Offboarding		<p>The City adheres to a detailed offboarding process including a formalized employee termination checklist. Departmental management, Human Resources, and IT coordinate to gather necessary paperwork, update IT permissions and access rights, discuss knowledge transfer, schedule and conduct an exit interview, and recover city-owned assets. This process is not supported in SAP. Instead, it involves multiple workflows and manual communications.</p> <p>Example of Potential Risks (Note): >Payroll fraud >Compliance with relevant laws and regulations regarding employee separation >On-going, improper physical access or business/information systems</p>	3	3	26	Strategic Operational Financial Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
89	Human Resources	Hiring	2.08.160 Department of human resources.	<p>FY22 Risk Updates: City Council Staff Report #11973 meeting date 3/15/2021 - Finding and recommendation for fire departments in Santa Clara County: Increase the recruitment and hiring of more female firefighters Lack of diversity in Fire or Police departments were noted in the survey response and one of interviews we conducted. It was noted that the actions are being taken to correct the issue.</p> <p>FY21 Risks: The Human Resources Department oversees the hiring process. The hiring process starts with departments submitting a requisition to fill a vacancy. Upon receipt of approval from the Budget Office, Human Resources goes through a planning process with the department to identify urgency, develop a timeline, and agree on a process. Most positions are governed by merit rule and require public posting. At this stage, the City details position requirements including whether exams are necessary.</p> <p>Human Resources completes an initial review to eliminate candidates that fail to meet minimum requirements. Screening processes (i.e. phone, paper-based) differ depending on the position. Interview processes are structured and questions require sign-off from Human Resources. Human Resources works with departments to conduct a job analysis and author interview questions tied to job duties. To score interviews, the City uses a scoring matrix.</p> <p>Human Resources has plans to promote diversity, for example, blind resume reviews. To address issues related to diversity, the City focuses on job outreach to encourage a diverse candidate pools.</p> <p>Examples of Potential Risk: >Hiring of unqualified individuals >Employing an individual that should be ineligible for employment >Litigation due to an illegal interview question >Implicit bias in the hiring process</p>	3	3	26	Operational Legal & Compliance Reputation
90	Human Resources	Records Management	2.08.160 Department of human resources. CA Labor Code Section 226 - Record Keeping Requirements	<p>Human Resources lacks a centralized repository for employee records. As a result, tracking employee data is oftentimes cumbersome. Within the past three years, Human Resources started converting files in an effort to go paperless. Due to issues with the vendor partner, the department has been unable to complete this transition. Completing this transition would enhance the department's ability to store, retrieve, and archive information.</p> <p>In addition, it is unclear whether the department has policy language detailing proper handling of personal identifiable information (PII). This topic is covered through annual trainings.</p> <p>Examples of Potential Risks (Note): >Failure to establish clear record keeping guidelines increases the likelihood the City will be noncompliant with state and federal record keeping requirements such as USCIS, the EEOC, and numerous federal employment acts (such as ERISA, ADA, FMLA and OSHA) >Increased difficulty responding to various legal actions and unemployment claims</p>	3	3	26	Legal & Compliance
91	Human Resources	Succession Planning	2.08.160 Department of human resources.	<p>FY22 Risk Updates: Succession Planning is noted as a risk</p> <p>FY21 Risks: The City used to conduct "people-focused" succession planning exercises and is considering a transition to a more "skill-focused" approach. This process may include: >Determining current and short-term departmental needs >Compiling critical skillsets >Analyzing the current in-house talent pool >Assessing risk of turnover for critical positions</p> <p>Examples of Potential Risks (Note): >Successors may lack readiness >Loss of institutional knowledge >Costs associated with recruiting a replacement</p>	3	3	26	Strategic
92	Human Resources	Systems and Technology	2.08.160 Department of human resources.	<p>FY22 Risk Updates: 1) Changes in compliance related to COVID-19 workplace regulations. 2) Vacancies in HR due to turnover. 3) The City has not yet acquired a centralized Human Resources Information System (HRIS). i.e., HRIS is not fully utilized Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: The City does not have a centralized HRIS. Instead, Human Resources relies on multiple systems and software, especially the finance system powered by SAP. Due to system limitations, Human Resources is required to conduct critical processes manually. These processes include adjusting hazard pay and bilingual worker pay. In addition, Human Resources experiences challenges coordinating with the pension system and making salary adjustments when certain employee types are promoted.</p> <p>Example of Potential Risks (Note): >Human error due to manual processes >Inaccurate calculation of employee compensation and pension balance</p>	3	3	26	Operational

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
93	Human Resources	Class and Comp	2.08.160 Department of human resources.	<p>Due to COVID-19, cost of living increases (COLA) and merit-based increases are frozen for non-union, management-level employees. For unionized employees, the City has contractual obligations to adhere to agreed upon pay structures and step advancements.</p> <p>In the case of union employees, classification and compensation are determined through market analysis based on agreed upon comparable firms. In some instances, agreeing upon these comparable firms has been an obstacle.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Choosing an inappropriate market sample may result in an noncompetitive salary ranges >Noncompetitive salary ranges on the high end may result in an increased financial burden on the City >Noncompetitive salary ranges on the low end may result in difficulties with recruitment and retention 	3	3	26	Operational
94	Human Resources	Standard Operating Procedures	2.08.160 Department of human resources.	<p>FY22 Risk Updates:</p> <p>A flow chart of hiring process was presented to Council meeting. There is a restrictive merit fuels and policy was noted as a weakness in the risk assessment survey Need a study of remote positions which affect recruitment and retention as many people prefer remote positions Safety is a concern of HR department especially during COVID-19 pandemic since the City does not have a Safety Officer</p> <p>FY21 Risks:</p> <p>Formalized SOPs are a critical tool as they communicate the correct way of carrying out HR activities. SOPs help the organization operate efficiently, maintain consistency, and communicate clearly. Based on interviews, it is unclear whether SOPs cover all critical processes and are updated.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >A lack of standard operating procedures detailing appropriate HR practices >A lack of standard operating procedures may result in loss of institutional knowledge if an employee leaves the organization >A lack of standard operating procedures related to employee safety may result in preventable injury claims 	2	3	18	Strategic Operational Financial Legal & Compliance
95	Human Resources	Contract Employees	State of California Assembly Bill (AB) 5	<p>State of California Assembly Bill (AB) 5 requires the application of the "ABC test" to determine if workers in California are employees or independent contractors. Under the ABC test, a worker is considered an employee and not an independent contractor, unless the hiring entity satisfies all three of the following conditions:</p> <ol style="list-style-type: none"> 1. The worker is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact; 2. The worker performs work that is outside the usual course of the hiring entity's business; and 3. The worker is customarily engaged in an independently established trade, occupation, or business of the same nature as that involved in the work performed <p>Some City departments rely on third-party contractors to deliver services. For example, Community Services relies on third-party contractors to manage the golf course, deliver recreational services (i.e. swimming pool, athletic fields) and provide arts and theatre programs. The City uses a variety of methods to mitigate risk in this area including management-level trainings led by the City Attorney and detailed reviews by Procurement. The City relies on a variety of "flags" such as previous employees trying to work as contractors. In these cases, the City can share the contract with CalPERS for review.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Litigation against the City for improper employment practices 	3	2	16	Strategic Operational Financial Legal & Compliance
96	Human Resources	Onboarding Employee Set-up	2.08.160 Department of human resources.	<p>The City relies on NEOGOV HR Software to assist with the onboarding process and Check to assist with the background check process. Before the implementation of the NEOGOV onboarding module, the onboarding process was more paper-based. Once an employee is selected for hiring, their information is transferred from the applicant tracking system to the onboarding system.</p> <p>The City leverages the onboarding tool to ensure candidates receive benefits, payroll, and tax documents along with critical policies and procedures. The NEOGOV system allows the City to share paperwork with new employees before their first day and eliminate the step of creating applicant packets.</p> <p>Human Resources oversees a two-day onboarding training with new employees. In the past, the City conducted this training monthly thus allowing for a natural cohort structure. Employees would receive a tour, meet key employees, meet their union representative, and attend a variety of trainings reviewing policies and other key information. Since COVID-19, the City has shifted to an on demand hiring approach instead of the cohort model.</p> <p>Examples of Potential Risk:</p> <ul style="list-style-type: none"> >New hires do not understand critical policies and procedures >New hires do not gain access to important employment documents in a timely manner 	3	2	16	Strategic Operational Legal & Compliance
97	Human Resources	Performance Management	2.08.160 Department of human resources.	<p>The performance management process is predominantly manual. The City has not transitioned to an automated process that would assist with critical steps such as notifying supervisors and employees about upcoming evaluation deadlines.</p> <p>Performance evaluations for non-union, management employees is less structured and involves greater discretion to determine merit based increases. Departments conduct these reviews on the anniversary of the employee's first day to determine if an employee moves to the next step.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Failure to eliminate unconscious bias from the performance appraisal process may increase the risk of litigation against the City based on the Lilly Ledbetter Act (2009) and/or the State of California Fair Pay Act (2016) >Failure to accurately track and recognize employee performance may lead to reduced engagement, especially among high-performers >Failure to recognize employee performance may result in unwanted turnover of high-performers 	3	2	16	Strategic Operational Financial Legal & Compliance Reputation Political & Economic IT

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
98	Information Technology	Disaster Recovery Preparedness and Testing	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was High in the internal audit report, IT Risk Management Report Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: This area focuses on the IT department's preparations and testing for disaster recovery (DR). In-scope activities include the following:</p> <ul style="list-style-type: none"> • Disaster recovery strategy and alignment with the organization's business continuity plans • Disaster recovery plan preparation • Disaster recovery testing <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Inability to establish a formal disaster recovery team that has the authority to declare a disaster and does not have defined roles during an event may result in financial penalties for service level misses > Inadequate disaster recovery preparedness may result in a disruption of essential process and service delivery thus preventing business continuity > Lack of restoration testing may result in false assurance that your organization has functional backups to restore operations in the event of an emergency 	3	5	44	Strategic Operational Reputational IT
99	Information Technology	Host Intrusion and Malware Defense	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was High in the internal audit report, IT Risk Management Report One of the risk assessment interviewees is interested in understanding the risk the City faces in comparison with the risks others face</p> <p>FY21 Risks: This area focuses on the IT department's practices for protecting network connected computers, telephones, printers and infrastructure hardware devices from intrusive activity and malicious software exploitation. In-scope activities include the following:</p> <ul style="list-style-type: none"> • Intrusion detection and prevention deployment, operation, and monitoring • Malware defense deployment, operation (e.g., signature updating), and monitoring for hosts and applications (e.g., spam email) <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Loss of system/application availability and integrity > Possible data breach and hijacking (ransomware) of organization data > Lack of intrusion detection and protection controls may result in the untimely identification of an attack 	3	5	44	Strategic Operational Financial Legal & Compliance Reputational IT
100	Information Technology	Problem Management and Incident Response	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was High in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the IT department's practices for managing problems and incidents. In scope are the following activities:</p> <ul style="list-style-type: none"> • The method(s) by which IT problems are reported and resolved • Problem tracking, reporting and communication • Incident response preparation and response testing • Incident identification, triaging, containment, eradication and recovery <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Loss of IT asset confidentiality, integrity and availability >Inability to properly identify the root cause of an incident thus preventing the ability to implement the appropriate corrective controls to reduce the risk a future incidents 	3	5	44	Strategic Operational Reputational IT
101	Information Technology	Mobile Device Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: This area focuses on the IT department's management of mobile devices. In-scope activities include the following:</p> <ul style="list-style-type: none"> >Authorization to use mobile devices >Mobile device provisioning, monitoring, support and de-provisioning >Mobile device incident response <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Unauthorized device access due to compromised security PINs >Unauthorized access by installed mobile applications to stored email, text messages, media and data >Unauthorized user access to stored email, text messages, media and data as well as network applications via VPN >Lack of mobile device monitoring may result in the untimely identification of an incident 	5	3	40	Operational IT

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
102	Information Technology	Strategy and Governance	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was High in the internal audit report, IT Risk Management Report Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: This area focuses on IT strategy and governance practices. In-scope activities include the following: <ul style="list-style-type: none"> • Development, maintenance and approval of an IT strategic plan that is aligned with the organization's business strategy • Development and execution of tactical IT plans that are aligned to the IT strategy • Development, maintenance and approval of an IT operating budget • Recurring performance and risk reporting to Executive Management and the Board of Directors • Oversight of IT operation and resource consumption by Executive Management and the Board of Directors </p> <p>Examples of Potential Risks (Note): <ul style="list-style-type: none"> >Executive management and the Board of Directors are unaware of IT risks and their severity >IT service delivery is misaligned with the organization and/or over-spends and under-delivers </p>	5	3	40	Strategic Operational, Reputational IT
103	Information Technology	Information Security	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: This area focuses on the IT department's practice of information security. Information security programs are developed to protect an organization's information systems and information from plausible threats and vulnerability exploitation that could result in one or more losses of security: confidentiality, integrity, availability, authenticity and/or non-repudiation. Programs should address the following: <ul style="list-style-type: none"> • Policy development and enforcement • Identity and access management • Threat identification and management • Vulnerability identification and management • Security roles and responsibilities • Security training and awareness for IT and non-IT personnel </p> <p>Examples of Potential Risks (Note): <ul style="list-style-type: none"> > Increased probability that the systems and data within the systems are not adequately protected from technical and malicious threats. > Lack of security awareness training may result in internal employees exposing the organization to security threats. > Lack of vulnerability monitoring may result in untimely threat identification and a lag in response time </p>	2	5	38	Strategic Operational Financial Legal & Compliance Reputational IT
104	Information Technology	Operations and Monitoring	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the IT department's practices for operating, monitoring and maintaining the computer systems and supporting infrastructure that are used by the work staff. In-scope activities include the following: <ul style="list-style-type: none"> >Capacity management > Hardware and software maintenance </p> <p>Examples of Potential Risks (Note): <ul style="list-style-type: none"> >Increased costs due to insufficient planning and forecasting >Disruption of business processes and service delivery >Financial penalties for service level misses </p>	2	5	38	Operational IT
105	Information Technology	Physical and Environmental Controls	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on IT physical and environmental safeguards that are deployed to protect the organization's application systems and information. In scope activities include the following: <ul style="list-style-type: none"> • Deployment and monitoring of physical access controls that protect IT assets • Deployment and monitoring of environmental controls that protect IT assets </p> <p>Examples of Potential Risks (Note): <ul style="list-style-type: none"> >Inappropriate or unauthorized physical access to data centers, server rooms, wiring closets, or facilities containing end-user IT hardware >Inappropriate or unauthorized physical access to IT hardware >IT hardware and/or infrastructure loss due to poor environmental controls </p>	2	5	38	Strategic Operational Legal & Compliance IT

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
106	Information Technology	Asset Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the IT department's asset management practices. In-scope activities include the following:</p> <ul style="list-style-type: none"> • Tracking information technology assets from procurement through disposal. • Reusing and decommissioning information technology assets • Ensuring information technology assets have an assigned owner, who is a stakeholder in the asset's protection • Ensuring information technology assets are properly maintained to maximize their useful life • Tracking software usage and ensuring that vendors' software license agreements are followed <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Inadequate security management of untracked IT assets > Lack of asset longevity and usefulness of assets > Data loss due to unsecured assets 	3	3	26	Strategic Operational Financial IT
107	Information Technology	Compliance Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the IT department's practices for complying with IT-related contract requirements, governmental regulations (e.g., HIPAA Security Rule) and industry standards (e.g., PCI Data Security Standard). In-scope are the following activities:</p> <ul style="list-style-type: none"> • Compliance program development and maintenance • Compliance program monitoring and reporting <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Poor compliance management practices may result in regulatory fines and oversight stemming from non-compliance. > Inability to management compliance requirements may result in increased operating expenses (e.g., payment card transaction costs). > Legal costs and ramifications that damage reputation and hinder business operations 	3	3	26	Legal & Compliance IT
108	Information Technology	Procurement and Service Provider Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: This area focuses on the IT department's practices for procuring hardware, soft-ware, facilities and services as well as managing the contracted service providers. In scope are the following activities:</p> <ul style="list-style-type: none"> >Procurement strategy > Vendor and service provider due diligence and performance monitoring <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Insufficient oversight of procurement strategy and methods could result in the failure to optimize the cost and effectiveness of IT asset and service purchases >Insufficient oversight of service provider contract performance could result in the non-timely detection of product/service delivery problems >Insufficient oversight of service provider activity and security controls could cause security problems including a data breach 	3	3	26	Strategic Operational Financial Legal & Compliance Reputational IT
109	Information Technology	Risk Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the IT department's risk management practices. In-scope activities include IT risk identification, triaging, treatment, tracking and management reporting.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Reputational damage >Monetary loss and penalties >Inadequate risk identification may lead to unmitigated threats to the organization 	3	3	26	Strategic Operational Reputational IT
110	Information Technology	Application Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the management of the organization's business applications – how they are developed, procured, modified and managed as well as how application security is performed and the role of the IT department in managing an application.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> > Inability to implement application changes and provide application support in a timely manner due to critical staff shortage or turn-over > Disruption of core business functions due to application downtime > Shared or generically named and/or shared among a group of users, the lack of accountability may result in inappropriate activity 	2	3	18	Operational IT

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
111	Information Technology	Architecture and Deployment	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the architecture and deployment of organization's information technology. In-scope elements include:</p> <ul style="list-style-type: none"> • The network architecture and deployed technology that is used to provide intra-site, inter-site connectivity and Internet connectivity • The organization's server and storage infrastructure • The computer hardware that is deployed for end-users <p>Examples of Potential Risks (Note): > Poor or unreliable IT service delivery that may result in customer dissatisfaction</p>	2	3	18	Strategic Operational IT
112	Information Technology	Change Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the IT department's practices for controlling changes to the IT environment. In-scope activities include the following:</p> <ul style="list-style-type: none"> • Management of infrastructure hardware, software and configuration changes • Management of host system software and configuration changes • Management of normal and emergency changes • Application release management • Delineation of the activities that are controlled by change management versus help desk request ticketing <p>Examples of Potential Risks (Note): > Inappropriate, unauthorized, under-planned and/or under-tested system changes may be implemented that negatively impact agency operations and/or reputation > Lack of managements approval prior to moving changes into production may result in disruptions in business operations. > Lack of a formal documented change management process may result in the inconsistent application of changes. > Lack of segregation of duties between environments related to development, testing and production can result in inappropriate changes that may disrupt operations</p>	2	3	18	Strategic Operational IT
113	Information Technology	Database and Data Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report Noted as a risk area by risk assessment interviewees</p> <p>FY21 Risks: This area focuses on the IT department's practices for controlling changes to the IT environment. In-scope activities include the following:</p> <ul style="list-style-type: none"> • Management of infrastructure hardware, software and configuration changes • Management of host system software and configuration changes • Management of normal and emergency changes • Application release management • Delineation of the activities that are controlled by change management versus help desk request ticketing <p>Examples of Potential Risks (Note): > Inappropriate, unauthorized, under-planned and/or under-tested system changes may be implemented that negatively impact agency operations and/or reputation > Lack of managements approval prior to moving changes into production may result in disruptions in business operations. > Lack of a formal documented change management process may result in the inconsistent application of changes. > Lack of segregation of duties between environments related to development, testing and production can result in inappropriate changes that may disrupt operations</p>	2	3	18	Operational IT
114	Information Technology	Organizational Architecture	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: This area focuses on the organization of the IT department, its placement within the organization and its approach to staffing.</p> <p>Examples of Potential Risks (Note): >A decentralized IT Department may result in inefficient operations by resulting in shadow IT. >Unaligned organizational structure may result in inefficient service delivery resulting in increased operating costs and potential service disruption >Lack of cross-training to backfill critical job roles and tasks may result in inadequate staffing >Lack of professional development for staff may result in the inability to recruit and retain qualified talent</p>	2	3	18	Strategic Operational IT

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
115	Information Technology	Project Management	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Low in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the IT department's project management practices. In-scope activities include: >Initiating, planning, executing, controlling, and closing projects >Managing projects' scope, milestones, quality and budget >Ensuring projects are adequately staffed >Reporting project progress and issues on a recurring basis to management and stakeholders</p> <p>Examples of Potential Risks (Note): >Poor project deliverable quality >Project cost overruns and late project completion >Inadequate project management may lead to fines due to unmet project milestones or non-compliance</p>	2	2	10	Operational IT
116	Information Technology	End-User Support and Perceptions	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Risk rating for this risk area was Medium in the internal audit report, IT Risk Management Report</p> <p>FY21 Risks: This area focuses on the IT department's scope and approach for providing end-user support as well as the perceptions that end-users have regarding IT service delivery. In-scope activities include the following: • End-user request intake • Help Desk triaging of end-user requests and problems • Help Desk request tracking and reporting • End-user notification of request handling progress and completion • Requesting and receiving end-user feedback on completed or abandoned service requests</p> <p>Examples of Potential Risks (Note): > Loss of end-user sponsorship and partnership in IT initiatives > Inefficient help desk processes related to request in-take, triaging, tracking and reporting may result in end-user dissatisfaction</p>	3	1	8	Operational Reputational IT
117	Information Technology	Ransomware	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Noted as a risk area by a risk assessment interviewee</p> <p>FY21 Risks: Governments are subject to cybersecurity threats, including but not limited to hacking, malware, ransomware. These crimes are becoming more common and costly for local governments to detect and deter.</p> <p>Examples of Potential Risk: >Financial loss as a result of a cyber attacker demanding a monetary payment in exchange organization data. >Service delivery disruption as a result of organizational data being held ransom thus preventing employee access to essential data.</p>	2	5	38	Reputational IT
118	Information Technology	Business Continuity Plan (BCP) and Disaster Recovery Plan (DRP)	2.08.240 Department of information technology.	<p>FY22 Risk Updates: Reference notes under "Disaster Recovery Preparedness and Testing"</p> <p>FY21 Risks: As a best practice, the City can benefit from a BCP which includes a DRP that is communicated to all staff. There is a lack of awareness across several functions on whether or not the City has a formal BCP and DRP. Failure to establish a plan leaves the potential for an interruption in services and the inability for all parties to know their roles, responsibilities and sequence of operations in the instance of an identified disasters.</p> <p>Examples of Potential Risks (Note): >Less effective and timely recovery from disaster events resulting in increased disruption of business operations or service delivery, increased expenditures for system recovery and potentially reputational damage</p>	2	4	28	Strategic Financial IT
119	Information Technology	IT Roadmap	2.08.240 Department of information technology.	<p>FY22 Risk Updates: • The City's three-year IT strategy is ending in 2021. Also, reference "Strategy and Governance"</p> <p>FY21 Risks: As a best practice, an IT Department's 1-3 year strategic roadmap is recommended to specifically align with the City's strategic goals. Failure to implement a documented roadmap may result in an insufficient use of limited resources and the inability of the department to support the overall business operations of the City. This can reveal itself when operations tend to be more reactive in nature. Proactive measures such as a roadmap will support alignment of network security, replacing aging application with new systems, hardware and software and technical items with the business goals of the City.</p> <p>Examples of Potential Risks (Note): >Absence of a formal IT Capital Plan approach has limited the transparency into the IT Capital Plan budget and misses the opportunity to facilitate a cohesive, City-wide IT investment strategy</p>	2	3	18	Strategic Legal & Compliance Reputational IT

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
120	Library	Events	2.08.230 Department of libraries.	Throughout the year, the library hosts many events, holiday parties and seminars. These events are interactive, often involving food, music and performances. Events are hosted by the library in conjunction with external non-profits, community agencies, faith-based organizations and individual persons and groups. The library also works with internal departments such as Police and Fire to host events. Events are designed to be educational and to help engage the community. Examples of Potential Risks (Note): >Health and safety for gatherings of large groups of individuals >Culturally insensitive events	1	3	12	Strategic Legal & Compliance Reputation
121	Library	Inventory Management	2.08.230 Department of libraries.	The largest business of the library involves the management of the book inventory (check-in and check-out). An inherent risk to lending is the ability to recoup and collect items loaned. The City does not charge late fees for book rentals but does impose fines and fees for replacement of books that are 42 days late. Laptop's and other library collection items are subject to late fees and replacement costs. Examples of Potential Risks (Note): >Book return process and inventory management	3	2	16	Financial
122	Library	Library Programs	2.08.230 Department of libraries.	Palo Alto's library offers hundreds of adult, children and family programs and services. These programs and services are open to any member of the community or library card holder. These programs include; >Book Clubs >ESL Classes >Writers workshops and contests >Arts and Crafts >Story Times Library offered programs are services are traditionally in person and virtual. Programs may require pre-registration, while others are readily available online, to be used at any time. Examples of Potential Risks (Note): >Program demand	1	3	12	Strategic Financial Legal & Compliance Reputation
123	Library	Privacy	2.08.230 Department of libraries.	Privacy is a concern for both the City and its citizens. Holding and storing of personal information safely, even for minimal periods of time, is essential. The library collects personal information from residents when evaluating citizens requests for a library card, no information is retained by any of the City's libraries. Examples of Potential Risks (Note): >Users do not log off when using the library computers//hardware >Private information regarding uses of libraries and its services is stored improperly	3	1	8	Legal & Compliance Reputation IT
124	Library	Locations Management	2.08.230 Department of libraries.	FY22 Risk Updates: The Libraries organizational structure was reorganized and diminished during previous rounds of budgeting. Limited staff has increased workload on existing staff without changes in technology for inventory management. FY21 Risks: Palo Alto has 5 library branches spaced throughout the City. Each library has unique services and function and is situated near other City services. The placement and special function of each library is to best serve the local community surrounding the library. Individuals are able to use any library and may request books from another library be transferred to their chosen community library for reservation and check-out. Additionally, books may be returned to any library or book-drop, regardless of where the book was originally checked-out. Examples of Potential Risks (Note): >Internal management of book returns and logistics is inefficient, and books are temporarily or permanently lost >Balance of staff and service offerings	3	1	8	Strategic Operational Financial Reputational
125	Planning and Development Services	Long Range Planning	2.08.220 Department of planning and development services Chapter 16.65 CITYWIDE AFFORDABLE HOUSING REQUIREMENTS Chapter 19.04 PLANNING COMMISSION	FY22 Risk Updates: • Uncertainty of aging population • Workforce constraints • Economic uncertainty • Inflation • State mandated initiatives and/or funding requirements FY21 Risks: The Long Range Planning division within the Department of Planning & Development Services guides and develops visioning and implementation programs for the City's community development policies and programs. Division areas of focus include: >Affordable housing >Housing planning and policies >Land Use and zoning >Weatherization >Comprehensive Planning >Community Block Grants Examples of Potential Risks (Note): >Unforeseen changes in economic or political conditions leading to required changes and inability to forecast future circumstances	5	4	46	Strategic Operational Financial Legal & Compliance Reputation Political & Economic

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
126	Planning and Development Services	Current Planning	2.08.220 Department of planning and development services	<p>FY22 Risk Updates:</p> <ul style="list-style-type: none"> Internal audit review of permitting processes, specific to solar panels Updated ERP system for tracking permitting, and payments <p>FY21 Risks: For anyone desiring to build in Palo Alto, they will first need to receive a building permit. The planning function will provide building permits based on the function's broader Comprehensive Plan 2030, compliance with the California Environmental Quality Act (CEQA), Plan Review (a fully outsourced service) and other codes and regulations. There is also an Architecture Review Board that consults on the decision for new proposals. All of these factors are considered when making decisions regarding proposals and requests.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Disagreement amount interpretation of current codes and regulations increasing the amount of discretion necessary in decision making >High quantities of new building proposals required for review, putting pressure on existing staff and lowering overall quality 	4	3	34	Strategic Operational Financial Legal & Compliance Reputation
127	Planning and Development Services	Development Services	2.08.220 Department of planning and development services	<p>FY22 Risk Updates:</p> <ul style="list-style-type: none"> Internal audit review of permitting processes, specific to solar panels Updated ERP system for tracking permitting, and payments <p>FY21 Risks: Development Services includes the Development Center, Plan Review Services, and the Inspection program. Permits are filed in person at City Hall or through the new Online Permit Services System. Permits and inspections are mandated before construction and/or remodeling for a variety of projects.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Individuals and businesses do not request permits or inspections before initiating projects >Delays or backlogs in providing permitting and inspection services 	3	3	26	Operational Financial Legal & Compliance Reputation
128	Planning and Development Services	Code Enforcement	2.08.220 Department of planning and development services	<p>The Code Enforcement Division of the Department of Planning & Development Services is responsible for enforcement of property maintenance, zoning, and building codes throughout Palo Alto.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >High volume of development and/or renovations without adequate capacity to enforce all codes >Inability to respond to all complaints made by community members 	3	2	16	Operational Legal & Compliance Reputation
129	Planning and Development Services	Building Division	2.08.220 Department of planning and development services	<p>The City of Palo Alto Building Division serves as a resource for homeowners, businesses, designers and contractors. The goal is to help customers build safe, healthy and sustainable buildings that comply with applicable codes and regulations.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Volume of requests due to high demand for new builds and renovation, leading to lower quality of advice or inability to answer all incoming questions 	3	2	16	Operational Legal & Compliance Reputation
130	Planning and Development Services	Historic Preservation	2.08.220 Department of planning and development services 18.12.140 Historical Review and Incentives 18.10.130 Historical Review and Incentives	<p>The City of Palo Alto looks to preserve and protect its culturally, historically and architecturally significant places in order to create a vibrant and sustainable community that fully reflects Palo Alto's diverse past. The City of Palo Alto's Historic Preservation Program began in 1979 and currently boasts four National Register Districts and hundreds of individually significant resources.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Cultural significance of historic homes and architecturally significant places increases reputational risk related to preservation >Process efficiency and customer service 	1	2	6	Financial Legal & Compliance Reputation Political & Economic
131	Police	Use of Force and Officer Conduct	2.08.170 Police department.	<p>The Independent Police Auditor has the authority to review and assess for objectivity, thoroughness, and appropriateness of disposition citizen complaint investigations of misconduct and internal affairs investigations associated with the Police Department and makes recommendations to the Police Chief.</p> <p>Loss of trust in law enforcement is a common externality. Research shows that perceived legitimacy of law enforcement is critical to effective law enforcement.</p> <p>High profile officer-involved interactions carry with them a variety of risks.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Litigation due to perceived or actual misconduct may result in legal action and expensive settlements >Reputational harm from improper use of force 	2	5	38	Operational Financial Reputation

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
132	Police	Staffing Levels	2.08.170 Police department.	<p>FY22 Risk Updates: In the survey, an audit of hiring, recruiting, and retention was recommended. Some interviewees noted lack of diversity, which they are currently trying to address.</p> <p>FY21 Risks: As of November 2020, nine employees are eligible for retirement and the City recently offered a retirement incentive. In addition, PD is also experiencing attrition among line-level officers, some of whom make lateral moves to work in other communities. Due to hiring constraints, turnover typically results in prolonged position vacancies.</p> <p>Examples of Potential Risks (Note): >Costs associated with position vacancy including lost productivity, overtime paid to officers, and training costs</p>	3	3	26	Strategic Operational Financial Legal & Compliance Reputation Political & Economic IT
133	Police	Overtime	2.08.170 Police department.	<p>FY22 Risk Updates: Staffing shortages for police officers and first responders are common across the State and within the City. Additionally, public pressure to not grow police forces, and the retirement of City Officers.</p> <p>FY21 Risks: Unpaid overtime claims are the largest category of complaints filed under California's wage and hours laws. Palo Alto police officers frequently work overtime. A common issue is having step based officers working dispatch during times of need.</p> <p>Examples of Potential Risks (Note): >Increased stress and fatigue among officers >Increased financial burden on the City as officers are paid at a higher rate</p>	4	2	24	Strategic Operational Financial Legal & Compliance Reputation Political & Economic IT
134	Police	Records Management	2.08.170 Police department.	<p>Law enforcement records management systems are a valuable source of information essential to the investigative, arrest, and judicial processes. Failure to manage records can affect the successful prosecution of criminal violators, resulting in liability or loss of public confidence.</p> <p>The City of Palo Alto Police Department relies on Sun Ridge Systems, Inc. to manage its police records.</p> <p>Examples of Potential Risks (Note): >Mismanagement of records, resulting in non-compliance from federal and/or State standards >Insufficient record retainage for important, highly visible cases</p>	2	3	18	Strategic Operational Financial Legal & Compliance Reputation Political & Economic IT
135	Police	Dispatch	2.08.170 Police department.	<p>The City of Palo Alto uses the dispatch function within the Police Department in order to dispatch for multiple functions, including police calls, Stanford matters, utilities, fire, and others. This dispatching service provides a conduit from citizens to City public safety and emergency services.</p> <p>Examples of Potential Risks (Note): > Mishandling of emergency calls from the public could lead to unfavorable views of City Police and other services > Multiple services addressed by dispatch may raise the risk for errors or bottlenecks in dispatching processes > Inaccurate allocation of dispatch related costs to other departments or organizations</p>	3	2	16	Operational Reputation
136	Police	Onboarding/Training	2.08.170 Police department.	<p>FY22 Risk Updates: Staffing shortages for police officers and first responders are common across the State and within the City. Additionally, given the actual or perception of public pressure for law enforcement, training is increasingly important for public trust.</p> <p>FY21 Risks: Officers are required to reach a minimum of 32 hours of ongoing professional training every 24 months. Officer training is integrated into officers' schedules throughout the year. Trainings are both in-person and virtual, and can be in both group or individual settings. Additionally, training and onboarding of a new officer recruit can take upwards of 18 months.</p> <p>Examples of Potential Risks (Note): >Noncompliance with training requirements >Inadequately trained personnel resulting in improper handling of public safety matters</p>	2	3	18	Operational Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
137	Public Works	Engineering Services	12.04.030 Public Works 2.30.100 Public Works Contracts 2.30.300 Public Works Contracts 2.08.190 Department of Public Works	<p>FY22 Risk Updates:</p> <ul style="list-style-type: none"> Collective cost of repairs, upgrades and new building projects has increased Pipeline monies from State and Federal dollars Supply chain constraints for raw materials and supplies Cost of materials and labor, particularly for contracted work <p>The internal audit report, Construction Project Controls Assessment, provided recommendations in the following areas:</p> <ul style="list-style-type: none"> Project Reporting Document Control Prevailing Wage Monitoring Schedule Management Allowance Usage <p>FY21 Risks:</p> <p>The Engineering Services Division designs and constructs City-owned facilities, streets, sidewalks, storm drains and parks infrastructure; provides engineering support to City Departments and the private development community for construction in the public right of way.</p> <p>The City oversees approximately 400,000 square feet of City-owned facilities including multiple community centers and libraries. Usage and maintenance patterns differ for each of these facilities. For example, the City leases space within the Cubberley Community Center to a variety of long-term leases.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Lack of funding may cause some capital projects to be significantly delayed and risk cost over-run from lack of continuous activities (i.e. start-up/shut-down operations) >Unfavorable contract terms resulting in unexpected expenses 	2	5	38	Strategic Operational Financial Legal & Compliance Reputation Political & Economic IT
138	Public Works	Public Services - Fleet	2.30.100 Public works contract.	<p>FY22 Risk Updates:</p> <ul style="list-style-type: none"> Supply chain constraints for raw materials and supplies Cost of materials and labor, particularly for contracted work <p>FY21 Risks:</p> <p>The Public Services Division maintains the City's fleet. Due to spending restrictions because of the COVID-19 pandemic, the City has limited fleet maintenance efforts as a cost savings measure.</p> <p>The City maintains a pool of vehicles that may be used for City business.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >An ageing fleet may result in increased maintenance costs >Lack of funding stability may harm the City's ability to maintain and replace vehicles >Charges to user departments may not sufficiently cover the City's full fleet costs >Policies and procedures that fail to clearly define replacement criteria may result in inefficient replacement methods 	3	4	36	Strategic Operational Financial Legal & Compliance Reputation
139	Public Works	Wastewater Treatment Plant Operations		<p>The City operates the Regional Water Quality Control Plant (RWQCP), which cleans and treats wastewater before it is discharged to San Francisco Bay. The plant is owned and operated by the City of Palo Alto, and it treats wastewater for the communities of Los Altos, Los Altos Hills, Mountain View, Palo Alto, Stanford University and the East Palo Alto Sanitary District. There is an agreement in place to allocate costs to each community.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Accuracy of cost allocation to each community >Compliance with applicable environmental laws 	3	4	36	Operational Financial Legal & Compliance
140	Public Works	Airport	2.30.100 Public works contract.	<p>FY22 Risk Updates:</p> <p>In the survey, the following opportunity was identified: New Airport technologies for streamlining administrative processes</p> <p>FY21 Risks:</p> <p>The Airport Division operates and maintains the Palo Alto Airport, the 3rd busiest airport in the Bay Area. The Air Traffic Control Tower is operated by the Federal Aviation Administration.</p> <p>The Airport generates revenues through tie-down fees and hangar rentals. The fee schedule is updated periodically.</p> <p>The Airport Division is overseeing a multi-phase apron reconstruction project. Construction began in 2018 and is expected to be complete in 2021. Construction of Phase I was completed in June 2018. Construction of Phase II began in December 2018 and was completed in January 2020.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Unfavorable contract terms may result in in unexpected expenses >Failure to reconcile contractor invoices may result in overpayments >Poor project planning may result in expensive change orders >Improper billing or management of fees for service >Impact of repayment plan established by Airport to the General Fund causing impacts on airport operations 	2	4	28	Strategic Operational Financial Legal & Compliance

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
141	Public Works	Public Services - Facilities		<p>FY22 Risk Updates: State requirements to maintain facilities that are related to environmental impacts and controls have increased and oversight has changed. Larger workforce issues for the City and for outside Vendors.</p> <p>FY21 Risks: The City must prioritize capital projects based on a variety of factors. The 2011 Blue Ribbon Commission (IBCR) report highlighted conclusions the City uses to assist with project prioritization and funding models. Key conclusions include: >The City underfunded its infrastructure maintenance in the amount of over \$2 million per year. >The City permitted the infrastructure underfunding to accumulate, building a backlog of "catch-up" needs totaling over \$40 million. >Five major City-owned facilities fell below current standards of safety, capacity, and functionality.</p> <p>Examples of Potential Risks (Note): >Inadequate preventative maintenance resulting in long-term financial burden of managing emergency maintenance needs >Failure to adhere to an infrastructure management system may hinder the City's ability to track the condition and use of all City infrastructure >Failure to effectively maintain City-owned facilities may result in more costly long-term repairs and replacement in the future</p>	3	4	36	Operational Financial
142	Public Works	Environmental Services	2.30.100 Public works contract.	<p>FY22 Risk Updates: The City incorporated the building of a new Environmental Laboratory and Environmental Services Building. The building will allow for new technology and testing for water, wastewater and stormwater systems.</p> <p>FY21 Risks: The Environmental Services division operates and maintains the Regional Water Quality Control Plant; maintains a Pretreatment Program for control of industrial and commercial dischargers; provides pollution prevention information and programs to residents and businesses; manages the City's solid waste programs. Environmental Services helps implement Zero Waste Palo Alto's mission, to help the community virtually eliminate waste being buried or burned. This effort involves garbage collection and sorting, recycling, and composting. Environmental Services contracts out these waste collection and sorting services.</p> <p>Examples of Potential Risks (Note): >Failure to detect non-compliant industrial dischargers may result in preventable pollution >Failure to achieve Zero Waste goals may harm the City's reputation</p>	3	3	26	Strategic Operational Financial Legal & Compliance Reputation
143	Public Works	Urban Forestry		<p>The Public Works Urban Forestry Section maintains nearly 66,000 trees of Palo Alto's urban forest. The urban forest provides a variety of benefits including: >Reduce the effects of urban density >Increase property values >Assist with storm water mitigation >Remove air pollutants >Assist with greenhouse gas sequestration</p> <p>The City has established a Urban Forest Master Plan, which was adopted in February 2019. The "Implementation Plan" includes planning for: >Budget need >Inter-departmental collaboration >Municipal Code updates >Monitoring</p> <p>Examples of Potential Risks (Note): >Risks associated with contract management</p>	1	3	12	Operational Legal & Compliance Reputation
144	Public Works	Building Deconstruction	2.30.100 Public works contract.	<p>As part of an ongoing effort to reduce waste in Palo Alto, City Council approved a Deconstruction Ordinance. The goal is for building materials to be reused or recycled, so workers will have to disassemble structures instead of wrecking buildings. Two of the largest components of landfill waste are food waste and construction and demolition (C&D) related materials. C&D materials represent more than 40% of Palo Alto debris that gets disposed in landfills.</p> <p>Examples of Potential Risks (Note): >This ordinance may place a financial burden on residential, commercial, and industrial property owners interested in demolishing a building >The City may weaken its reputation as "business-friendly" >Property owners may avoid needed upgrades to circumvent additional costs</p>	2	2	10	Financial Reputation Political & Economic
145	Transportation	Safety Improvement Projects and Traffic Operations	2.08.260 Office of transportation.	<p>FY22 Risk Updates: The California Department of Transportation's mission was changed in FY22 to make transportation more equitable and defend the climate. State missions and funding streams will be used to advance this mission.</p> <p>FY21 Risks: The Office of Transportation works to enhance quality of life and improve the safety of the users of all modes of transportation. To achieve these goals, the Office manages safety improvement projects, collects transportation data, sets speed limits, follows signage and striping best practices, and implements traffic control measures.</p> <p>Examples of Potential Risks (Note): >Improper roadway safety and operations decisions may result in preventable roadway incidents with legal ramifications for the City >Failure to obtain community support for a project may result in expensive change orders and reputational harm</p>	2	4	28	Strategic Financial Legal & Compliance Reputation

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
146	Transportation	Contract Management	2.08.260 Office of transportation.	<p>FY22 Risk Updates: The contract with Duncan Solution was amended to implement ALPR technology and the Surveillance Use Policy were approved by City Council on 2/22/2021. There is a public's concern about privacy, and the contract is to comply with SB 210. The policy states, "ALPR system audits will be conducted on a regular, annual basis." Staff anticipates being able to procure the essential hardware by April 2021 or shortly thereafter, with full implementation expected to launch by late Summer 2021.</p> <p>FY21 Risks: The Office of Transportation relies on contracted services for a variety of areas including construction, parking enforcement, and permitting. Noteworthy contractors include Serco and Duncan Solutions.</p> <p>The Serco contract is three years, in an amount not-to-exceed \$2,322,285 for residential preferential parking enforcement services. The Duncan Solution contract is \$627,000 over a five-year term to develop, implement, support and maintain a parking permit and citation management system.</p> <p>Examples of Potential Risks (Note): >Unfavorable contract terms resulting in unexpected expenses >Contract compliance and cost control issues >Failure to reconcile contractor invoices may result in overpayments</p>	3	5	44	Operational Financial Legal & Compliance
147	Utilities	Workforce & Succession Planning	2.08.200 Department of Utilities	<p>FY22 Risk Updates - The department may be impacted by a loss of institutional knowledge due to long-term staff retirements creating position vacancies which results in the hiring of new staff that is unaware of the City's processes. There are also challenges with attracting and retaining staff due to non-competitive salaries. - One of the risk assessment interviewees mentioned that a salary is being increased as a currently vacant position cannot be filled.</p> <p>FY21 Risks: With Palo Alto's high cost of living, the City has had trouble recruiting and retaining positions such as lineman and operations crew as there are other organizations (such as investor-owned utilities) in more affordable areas that are also in need of these positions. These employees can oftentimes make the same or higher salaries at other organizations with lower costs of living. This creates an issue for the City in regards to recruiting and retaining positions in high demand such as linemen.</p> <p>Examples of Potential Risks (Note): >Sustained high vacancy of positions decrease the ability for Palo Alto to maintain pace of capital improvements and maintenance >High turnover of employees increases personnel expenses associated with onboarding and training >Difficulty hiring high-quality employees in these types of positions</p>	2	3	18	Operational Financial Reputation Political & Economic
148	Utilities	AMI Project	2.08.200 Department of Utilities	<p>FY22 Risk Updates: The City has the opportunity to improve its metering process.</p> <p>FY21 Risks: Palo Alto is moving towards an implementation of AMI technology for meter reading. AMI will allow for the City to conduct meter readings with more efficiency and accuracy. The costs associated with such an implementation are significant. Any implementation with such an effort may run into unexpected challenges and barriers to implementation. Additionally, redeploying current meter readers is also a challenge.</p> <p>Examples of Potential Risks (Note): >Customers desiring to opt out of AMI technology may introduce additional challenges in creating efficient meter reading processes >Implementation of AMI can introduce financial risks for unexpected challenges</p>	3	4	36	Strategic Operational Financial IT
149	Utilities	Word Order & Asset Management	2.08.200 Department of Utilities	<p>For any operations and maintenance, a proper work order system is vital to the operations of the utility. Modern day technology and automation can improve the work order process and reduce the number of steps required from employees.</p> <p>Examples of Potential Risks (Note): >Implementation of an automated work order system can be costly and disruptive >Lack of an automated work order system can create efficiency issues and opportunities for human error >Improper use of the work order system resulting in improper classification of assets</p>	3	3	26	Operational IT
150	Utilities	Rebates and Programs	2.08.200 Department of Utilities	<p>FY22 Risk Updates: - FY22 Adopted Operating Budget document states that it assumes various rate changes. - One of the risk assessment interviewees is concerned about capacity and costs to increase renewable energy.</p> <p>FY21 Risks: The City offers both residential and commercial utility customers rebates and programs to assist with efficiency and cost savings. In particular, both residential and commercial customers can take advantage of city resources to learn more about solar energy. The City also offers tips and tricks regarding energy efficiency. For residential customers, you can receive landscape rebates, rebates for outdoor surveys, home water surveys, EV rebates, heat pump water heater rebates, permeable pavement rebates just to name a few. Commercial customers also can receive water rebates and other business specific rebates. Commercial can also take advantage of the fiber program, renewable energy program and others.</p> <p>Examples of Potential Risks (Note): >Decreased consumption impacting rates >Rebates and programs become cost inefficient, producing less benefits than inputs required to run the program</p>	3	3	26	Operational Financial Reputation

Risk ID	Functional Area	Risk Title	Municipal / State Code Reference	Risk Detail (From documents provided, audit reports, interviews)	Likelihood (1-5)	Impact (1-5)	Score	Risk Areas
151	Utilities	Purchase Power Contract Management	2.08.200 Department of Utilities	<p>FY22 Risk Updates (Based on PPA Audit):</p> <ul style="list-style-type: none"> > There is no formal process to monitor and document vendor compliance with Power Purchase Agreements. > Changes made to the front office model do not require approvals, which may increase the likelihood of inaccurate reporting. > The OCA identified during process interviews that CPAU does not have a process in place to validate NCPA settlement processes that include the verification of invoice calculations, contract rates, and matching ARB amounts on behalf of the City. <p>FY21 Risks: The City purchases all of their power from external sources, without any generation operations of their own. This requires a greater effort in monitoring these Purchase Power Agreements. Monitoring these agreements is important both from a compliance standpoint, ensuring that state and local requirements are being met, as well as a financial standpoint, ensuring that costs are reasonable.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >The cost of purchased power exceeding the cost of generating power >Noncompliance with purchase power agreements 	4	4	42	Strategic Financial Legal & Compliance
152	Utilities	Rates and Rate Adjustments	2.08.200 Department of Utilities	<p>FY22 Risk Updates: The City needs improvement with processing large rate adjustments.</p> <p>FY21 Risks: Palo Alto owns and operates its own utilities. However, the City purchases all of its electric, water, and gas from other sources. The City must set its rates according to the cost to purchase power, water, and gas as well all O&M and capital costs associated with administering the utilities. For example, the City purchases water from a different source than its neighbors and subsequently has higher water rates.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Competitive rates in neighboring communities may provide incentive for any prospective residents to choose neighboring communities >Rising rates may indicate operational inefficiencies that contribute to a greater cost of service >Compliance with regulatory requirements in the rate setting process >Reputational risk associated with rate setting >Delay in cost recovery after provider's cost increase >Allocation of costs across utilities 	3	4	36	Strategic Operational Financial Reputation
153	Utilities	Utility Bill Collections	2.08.200 Department of Utilities	<p>As a practice, the City of Palo Alto does not currently shut off utilities for those who are regularly missing payments. This includes both commercial and residential customers. The City maintains financial reserves that fluctuate over time, but attempt to remain above 70 days. Continued customers who do not pay their bills will reduce financial reserves.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Continued practices of no water shut offs may encourage late payments or missed payments >The City may not have the option to complete water shut offs during times like COVID-19, or may not want to complete shut offs due to reputational risk 	3	2	16	Financial Legal & Compliance Reputation Political & Economic
154	Utilities	Customer Service	2.08.200 Department of Utilities	<p>The City of Palo Alto Utilities Customer Service supports the Utilities mission to provide safe, reliable, environmentally sustainable and cost effective services. Customer Services supports residential and commercial customers with questions about the Utilities services: electric, fiber optics, natural gas, water, and wastewater. Customer Services helps customers pay their bill, start new services, and access rebates.</p> <p>Examples of Potential Risks (Note):</p> <ul style="list-style-type: none"> >Negative customer interactions reflect poorly upon the City >COVID-19 and other emergency utility disconnection moratoriums cause a financial burden for the City >Improper handling of customer accounts 	3	2	16	Operational Reputation



City of Palo Alto

Office of the City Auditor
FY22/FY23 Annual Audit
Plan

February 15, 2022

Attachment: OCA - FY22-23 Audit Plan (Final Draft for P&S) [Revision 1] (13911 : Presentation of the Office of the City Auditor's FY22/FY23 Risk

Overview

Introduction

The purpose of the audit activities performed by the Office of the City Auditor (OCA) for the City of Palo Alto (the City) is “to ensure that city management is using its financial, physical, and informational resources effectively, efficiently, economically, ethically, and equitably, and in compliance with laws, regulations, contract and grant requirements, and city policies and procedures”, according to the Palo Alto Municipal Code ([Section 2.08.130](#)). It requires the City Auditor prepare an annual audit plan for the City Council’s approval at the beginning of each fiscal year.

In accordance with Task #2 of the Baker Tilly agreement ([City of Palo Alto Contract No. C21179340](#)), Baker Tilly US, LLP (Baker Tilly) performed the initial risk assessment after having started to serve as OCA in October 2020 and submitted in early 2021 the FY21-FY22 annual audit plan identifying audit activities across an 18-months horizon (through FY22).

The OCA updated the initial risk assessment in January 2022, one year after our initial risk assessment. This audit plan for the remaining FY22 and FY23 was prepared based on the results of the updated risk assessment. The OCA will seek approval of contract task orders iteratively during that timeframe in order to remain agile and accommodate changes to the plan as time passes.

Other activities are addressed in separate task orders corresponding to the tasks in the Baker Tilly agreement. For example, the City Auditor performs follow up on audit findings and recommendations, as outlined in Task #5.

Conformance with Local Ordinances and Standards

Section 2.08.130 of the Palo Alto Municipal Code defines that the mission of OCA is to promote honest, efficient, effective, economical, and fully accountable and transparent city government. Audits are to be conducted and nonaudit services provided in accordance with Government Auditing Standards, as established by the Comptroller General of the United States, Governmental Accountability Office.

The following duties of the City Auditor exist regarding the plan and scope of internal audits.

[Palo Alto City Charter](#)

Article IV Sec. 12 requires the City Auditor to perform the following:

- Conduct audits in accordance with a schedule approved by the City Council and may conduct unscheduled audits from time to time.
- Conducts internal audits of all the fiscal transactions of the City.

[Title 2 Administrative Code](#)

Section 2.08.130 requires the City Auditor to perform the following:

- Prepare an annual audit plan for city council approval.
- Identify the preliminary objectives of each audit to be performed, reflecting the purpose of the engagement and a preliminary description of the areas that may be addressed.
- Conduct performance audits and perform nonaudit services of any city department, program, service, or activity as approved by the city council.

[California Government Code](#)

Section 1236 requires all cities that conduct audit activities to conduct their work under the general and specified standards prescribed by the Institute of Internal Auditors (IIA) or the Government Auditing Standards (GAO) issued by the Comptroller General of the United States, as appropriate.

Audit Activity Types

OCA will conduct performance audits and perform financial/operational analyses of any City department, program, service, or activity as approved by the City Council in accordance with the Baker Tilly agreement.

Performance Audits

According to the Government Auditing Standards ([GAO-18-568G](#), Section 1.21 and 1.22, page 10-12), performance audits provide objective analysis, findings, and conclusions to assist management and those charged with governance and oversight with, among other things, improving program performance and operations, reducing costs, facilitating decision making by parties responsible for overseeing or initiating corrective action, and contributing to public accountability. Performance audits may include the following four (4) audit objectives:

- Program effectiveness and results
- Internal control design and effectiveness
- Compliance with laws, regulations, and policies
- Prospective analysis

Audit Planning Considerations

While maintaining its independence and objectivity in accordance with standards, the City Auditor considers a variety of matters when developing the Annual Audit Plan, including but not limited to:

- Risk assessment – OCA performed a risk assessment and summarized the results in a separate report (Task #2). Generally speaking, audit activities target high(er) risk areas. The results are shown the following page.
- Ability to add value – audit seeks to add value through independent and objective analysis.
- City Council – the City Auditor reports to the City Council and seeks input on audit priorities.
- Coverage and Prior Audits – the City Auditor considers prior audits conducted by OCA, the financial audit, and other audit and consulting reports recently issued.
- “Ripeness” and On-Going Initiatives – certain risk areas may be addressed through operational activities, which could mean they are not be ripe for audit to add value.
- Scheduling – the City Auditor takes into consideration the timing of an audit and other on-going initiatives that directly relate. Putting an undue burden on City staff may exacerbate the risk at hand or other interrelated risks.

Risk Assessment Results

The OCA performed a citywide risk assessment to plan for FY22 and FY23 audit activities and documented the methodology and the detailed results in a separate Risk Assessment Report. In summary, we identified the following areas rated as High or High-Moderate risks. In determining the audit activities to be performed in FY22 and in FY23, we further reviewed these risks and functional areas and considered the matters listed in the previous page.

Functional Area	Title	Likelihood (1-5)	Impact (1-5)	Score
City Wide	COVID-19 Response	5	5	50
Org Wide	Employee Retention & Succession Planning	5	4	46
Planning and Development Services	Long Range Planning	5	4	46
Information Technology	Disaster Recovery Preparedness and Testing	3	5	44
Information Technology	Host Intrusion and Malware Defense	3	5	44
Information Technology	Problem Management and Incident Response	3	5	44
Transportation	Contract Management	3	5	44
Org Wide	Workforce	4	4	42
Org Wide	Citywide Risk Management	4	4	42
Administrative Services	Procurement	4	4	42
Fire	Emergency Medical Service	4	4	42
Human Resources	High Cost Claims	4	4	42
Human Resources	Workload	4	4	42
Information Technology	Mobile Device Management	5	3	40
Information Technology	Strategy and Governance	5	3	40
Public Works	Secondary Treatment Upgrades	2	5	38
Public Works	ADA Compliance Upgrade	2	5	38
Administrative Services	Investments, Debt, and Cash Management	2	5	38
Information Technology	Information Security	2	5	38
Information Technology	Operations and Monitoring	2	5	38
Information Technology	Physical and Environmental Controls	2	5	38
Information Technology	Ransomware	2	5	38
Police	Use of Force and Officer Conduct	2	5	38
Org Wide	Governance	3	4	36
Org Wide	Organizational Culture	3	4	36
Administrative Services	ERP System Upgrade	3	4	36
City Wide	Sustainability and Climate Action Plan	3	4	36
Administrative Services	Accounts Receivable	3	4	36
Fire	Fire Suppression	3	4	36
Fire	Fire Prevention - Palo Alto Foothills & Wildland Fire Risk	3	4	36
Public Works	Public Services - Fleet	3	4	36
Public Works	Wastewater Treatment Plant Operations	3	4	36
Public Works	Public Services -Facilities	3	4	36
Utilities	AMI (Advanced Metering Infrastructure) Project	3	4	36
Utilities	Rates and Rate Adjustments	3	4	36

Proposed Audit Activities for FY2022-2023

Included in the tables below are the proposed audit activities for the remainder of FY2022 and FY2023. Each audit activity corresponds to a risk rated as High or Moderate in the Risk Assessment Report and selected based on other factors outlined on page 3.

The preliminary audit objectives are described for each audit listed. These objectives and scope of each audit activity will be further defined based on the result of a project planning risk assessment processes performed at the beginning of each activity.

Audits are planned in three overall phases – note that the timing may differ slightly for each audit activity:

- **Phase I** – Activities projected to start before March 2022 and end by June 2022
- **Phase II** – Activities projected to start in March 2022 and end by December 2022
- **Phase III** – Activities projected to start in June 2022 or January 2023 and end by June 2023

Amendments to the proposed audit plan will be proposed either as needed or after conducting an annual risk assessment and update the audit plan, as needed, during FY23. Amendments may be proposed in response to changes in the City's environment such as organizational structure, operations, risks, systems, and controls. Please note that the City Auditor will actively manage projects and overall budgets and workload in its execution of the workplan.

For each audit activity, a task order is submitted to the City Council for approval before the work is commenced. We have prepared and attached to this report multiple task orders that correspond to audit activities we have prioritized (e.g., those in Phase I). Those audit activities for are marked with an "X" in the 'Seeking Approval' column of the table below, and the Task Orders are included in the Appendix.

Phase I Activities

Seeking Approval	Function	Project Title	Audit Objectives	Timeline	Estimated Hours	FY22 Cost	FY23 Cost (*)	Total Cost FY21+22+23
	Administrative Services	Economic Recovery Advisory (Task Order 4.7)	<ul style="list-style-type: none"> Review the City's long-term financial planning model and offer recommendations for improvement. Identify and evaluate key revenue sources categories that present long term risk to the City's financial sustainability. Perform scenario analysis and advise in the development of long term financial projections. 	March - December 2021	400	\$64,663		\$64,663
	Public Works	Public Safety Building - Construction Audit (Task Order 4.8)	<ul style="list-style-type: none"> Monthly invoice review Change order testing Contingency and allowance testing Lien waiver control Compliance with insurance requirements 	March 2021 - June 2023	420	\$26,633	\$26,633	\$51,266
	Planning and Development Services	Building Permit & Inspection Process Review (Task Order 4.9)	<ul style="list-style-type: none"> Identify highest impact area to focus the assessment (e.g., specific permit type(s), specific sub-processes, etc.). Document corresponding process(es) and evaluate for efficiency and effectiveness. Benchmark operational performance against industry practices and established standards. 	April – September 2021	360	\$48,300		\$48,300
	Citywide	Nonprofit Agreements Risk Management Review (Task Order 4.10)	<ul style="list-style-type: none"> Evaluate controls in place to ensure that nonprofit organizations are properly vetted prior to selection and monitored through the life of an agreement. Assess the performance monitoring process against the best practice. Follow up on relevant audit findings from past audit work. 	May – September 2021	400	\$55,246		\$55,246
	Utilities	Utility Work Order & Process Review (Task Order 4.11)	<ul style="list-style-type: none"> Determine whether adequate controls are in place and working effectively around the work order process Assess the work order process against best practices 	January - December 2022	400	\$81,400		\$81,400
	Administrative Services / Information Technology	Wire Payment Process and Controls (Task Order 4.12)	<ul style="list-style-type: none"> Determine whether adequate controls are in place and working effectively to ensure that all disbursements are valid and properly processed in compliance with City's policies and procedures Determine whether end user security awareness training is sufficient to prevent erroneous payments caused by phishing 	February - June 2022	270	\$54,550		\$54,550
Phase I Sub Total					2,250	\$329,792	\$26,633	\$355,425

* For the purpose of audit plan preparation, OCA used the FY22 budget amount for FY23

Phase II Activities

Seeking Approval	Function	Project Title	Audit Objectives (preliminary objectives for audits not currently subject to approval)	Timeline	Estimated Hours	FY22 Cost	FY23 Cost (*)	Total Cost
X	Human Resources	Remote and Flexible Work Study	<ul style="list-style-type: none"> Assess employee and management perspectives for long-term remote and flexible work viability and associated challenges Evaluate positive outcomes and challenges for managing a mixed location workforce Identify policies, processes, management practices and work culture improvements that may improve the City's ability to manage a remote workforce 	March - December 2022	285	\$50,000	\$10,000	\$60,000
X	Information Technology	Cybersecurity Assessment	<ul style="list-style-type: none"> Map current state security capabilities to the NIST Cybersecurity Framework and evaluate the maturity of current security processes Identify current risks related to weaknesses in the City's cybersecurity program Identify target state objectives utilizing the Capability Maturity Model (CMMI) and develop recommendation to meet the objectives 	March - December 2022	525	\$90,000	\$20,000	\$110,000
X	Public Works	Wastewater Treatment Plant Agreement Audit	<ul style="list-style-type: none"> Evaluate whether direct and indirect costs incurred by the City are properly allocated to the operation of the Wastewater Treatment Plant. Review whether costs are properly allocated to the various parties to the Wastewater Treatment Plant Agreement. 	March 2022 - December 2022	400	\$60,000	\$2,250	\$62,250
Phase II Sub Total					1,210	\$194,000	\$38,250	\$232,250

* For the purpose of audit plan preparation, OCA used the FY22 budget amount for FY23

Phase III Activities

Seeking Approval	Function	Project Title	Preliminary Audit Objectives	Timeline	Estimated Hours	FY22 Cost	FY23 Cost (*)	Total Cost
	Transportation	Contract Management - ALPR Technology	<ul style="list-style-type: none"> Determine whether policies and procedures are implemented effectively to protect the privacy of personal information gathered using ALPR technology for the City's parking management. Determine whether the City monitors the vendor's performance to ensure the compliance with contract terms and applicable laws and regulations related to data privacy. 	June 2022 - January 2023	400		\$82,500	\$82,500
	Administrative Services	Investment Management	<ul style="list-style-type: none"> Determine whether adequate controls are in place and operating effectively to ensure that investments are managed in accordance with the investment management and other relevant policies. Assess the organizational structure and operations of the investment portfolio management function against best practice. 	June 2022 - January 2023	350		\$61,550	\$61,550
	Information Technology	Disaster Recovery Preparedness	<ul style="list-style-type: none"> Determine whether a formal disaster recovery plan exists and aligns with the City's needs for business continuity Determine whether a disaster recovery plan is periodically tested and updated to ensure a successful recovery 	January - June 2023	400		\$87,500	\$87,500
	Administrative Services	Procurement Process	<ul style="list-style-type: none"> Determine whether adequate controls are in place and working effectively to ensure that the appropriate vendors are selected properly to achieve desired objectives Identify the opportunities to improve the efficiency and effectiveness of the procurement process 	January - June 2023	350		\$61,550	\$61,550
	Planning and Development Services	Long Range Planning	<ul style="list-style-type: none"> Review progress against intended goals and identify any gaps Determine whether an effective control environment exists for the Long Range Planning group to maintain City's Comprehensive Plan Determine whether adequate controls are in place and working effectively for data analyses 	January - June 2023	400		\$82,500	\$82,500
	Public Works	ADA Compliance	<ul style="list-style-type: none"> Determine whether improvements have been made to make facilities, programs, and services accessible in accordance with the Transition Plan and Self-Evaluation Final Study to ensure compliance with the Americans with Disabilities Act (ADA) OF 1990 	January - June 2023	350		\$61,550	\$61,550
	TBD	TBD / Ad Hoc Requests	TBD	TBD	TBD			
Phase III Sub Total					2,300	\$0	\$458,100	\$458,100
Phase I + II + III TOTAL					5,760	\$523,792	\$521,983	\$1,045,775
FY22 - FY23 Budget						\$600,000	\$560,000	\$1,160,000
FY23 Ad Hoc / Contingency						\$76,208	\$38,017	\$114,225

* For the purpose of audit plan preparation, OCA used the FY22 budget amount for FY23

Appendix: Task Orders

Audit Activity 4.13 – Remote and Flexible Work Study

PROFESSIONAL SERVICES TASK ORDER

TASK ORDER FY22-004.13

Consultant shall perform the Services detailed below in accordance with all the terms and conditions of the Agreement referenced in Item 1A below. All exhibits referenced in Item 8 below are incorporated into this Task Order by this reference. The Consultant shall furnish the necessary facilities, professional, technical and supporting personnel required by this Task Order as described below.

CONTRACT NO. C21179340
OR PURCHASE ORDER REQUISITION NO. (AS APPLICABLE)

- 1A. MASTER AGREEMENT NO. (MAY BE SAME AS CONTRACT / P.O. NO. ABOVE):
- 1B. TASK ORDER NO.: FY22-004.13
- 2. CONSULTANT NAME: Baker Tilly US, LLP
- 3. PERIOD OF PERFORMANCE: START: March 1, 2022 COMPLETION: December 31, 2022
- 4. TOTAL TASK ORDER PRICE: \$60,000
BALANCE REMAINING IN MASTER AGREEMENT/CONTRACT \$TBD
- 5. BUDGET CODE _____
COST CENTER _____
COST ELEMENT _____
WBS/CIP _____
PHASE _____
- 6. CITY PROJECT MANAGER’S NAME & DEPARTMENT:
Greer Stone, Chair of the City Council’s Policy and Services Committee
- 7. DESCRIPTION OF SCOPE OF SERVICES (Attachment A)
MUST INCLUDE:
 - SERVICES AND DELIVERABLES TO BE PROVIDED
 - SCHEDULE OF PERFORMANCE
 - MAXIMUM COMPENSATION AMOUNT AND RATE SCHEDULE (as applicable)
 - REIMBURSABLE EXPENSES, if any (with “not to exceed” amount)
- 8. ATTACHMENTS: A: Task Order Scope of Services B (if any): N/A

I hereby authorize the performance of the work described in this Task Order.

I hereby acknowledge receipt and acceptance of this Task Order and warrant that I have authority to sign on behalf of Consultant.

APPROVED:
CITY OF PALO ALTO

APPROVED:
COMPANY NAME: _____

BY: _____
Name _____
Title _____
Date _____

BY: _____
Name _____
Title _____
Date _____

Attachment A

DESCRIPTION OF SCOPE OF SERVICES

Introduction

Attachment A, the Description of Scope of Services, contains the following four (4) elements:

- Services and Deliverables To Be Provided
- Schedule of Performance
- Maximum Compensation Amount and Rate Schedule (*As Applicable*)
- Reimbursable Expenses, if any (With “Not To Exceed” Amount)

Services & Deliverables

Baker Tilly’s approach to conducting the Construction Controls Assessment involves four (3) primary steps:

- Step 1: Audit Planning
- Step 2: Control review and analysis
- Step 3: Reporting

Step 1 – Audit Planning

This step consists of the tasks performed to adequately plan the work necessary to address the overall audit objective and to solidify mutual understanding of the audit scope, objectives, audit process, and timing between stakeholders and auditors. Tasks include:

- Gather information to understand the environment under review
 - Understand the organization structure and objectives
 - Review the codes, regulations, policies, and other standards and expectations
 - Review the prior audit results, if any
 - Review previously conducted employee engagement and satisfaction surveys
 - Issue an employee survey centered on remote work capabilities
 - Issue a management survey centered on remote work capabilities
 - Review additional documentation and conduct interviews as necessary
- Assess the audit risk
- Write an audit plan and audit program
 - Define audit objectives and scope
 - Identify the audit procedures to be performed and the evidence to be obtained
- Announce the initiation of the audit and conduct a kick-off meeting with key stakeholders
 - Discuss audit objectives, scope, audit process, timing, resources, and expectations
 - Discuss documentation and interview requests for the audit

Step 2 – Control Review and Testing

This step involves executing the procedures in the audit program to gather information, interview individuals, and analyze the data and information to obtain sufficient evidence to address the audit objectives. The preliminary audit objective is to: (1) Assess employee and management perspectives for long-term remote and flexible work viability and associated challenges; (2) Evaluate positive outcomes and challenges for managing a mixed location workforce; (3) Identify policies, processes, management practices and work culture improvements that may improve the City’s ability to manage a remote workforce. Tasks include but are not limited to:

- Analyze employee and management surveys to identify management and policy change opportunities and barriers for managing a mixed location workforce
- Interview (focus group and/or individual) the Human Resources, employee representatives and management representatives to understand the current state, benefits and barriers to
- Review relevant policies and procedures as well as the position eligibility standards for remote work to identify the criteria to be used for evaluation of control design and effectiveness
- Research best practices and practices of surrounding communities
- Analyze available data to assess current practices impact on recruitment and retention
- Validate analysis with Human Resources

Step 3 – Reporting

In Step 3, the project team will perform tasks necessary to finalize audit working papers and submit a final audit report. Tasks include:

- Develop findings, conclusions, and recommendations based on the supporting evidence gathered
- Validate findings with the appropriate individuals
- Complete the supervisory review of working papers and a draft audit report
- Distribute a draft audit report and conduct a closing meeting with key stakeholders
 - Discuss the audit results, findings, conclusions, and recommendations
 - Discuss management responses
- Obtain written management responses and finalize a report

Deliverables:

The following deliverable will be prepared as part of this engagement:

- Audit Report with remote and flexible work data analysis and best practice recommendation

Schedule of Performance

Anticipated Start Date: March 1, 2022

Anticipated End Date: December 31, 2022

Maximum Compensation Amount and Rate Schedule

The not-to-exceed maximum, inclusive of reimbursable expenses (as summarized below) for this Task is \$60,000. The not-to-exceed budget is based on an estimate of 285 total project hours, of which 16 are estimated to be completed by the City Auditor.

Reimbursable Expenses

If circumstances allow, Baker Tilly anticipates planning one on-site fieldwork. Given this possibility, Baker Tilly could incur reimbursable expenses for this Task.

The not-to-exceed maximum for reimbursable expenses for this Task is \$5,000.

The following summarizes anticipated reimbursable expenses:

- Round-trip Airfare – \$1,200
- Rental Car - \$600
- Hotel accommodation - \$2,500 (8 nights)
- Food and incidentals – \$700

Note that, if current restrictions associated with COVID-19 continue, an on-site visit may not be possible. The project team will work with the City to consider circumstances at the time.

Audit Activity 4.14 – Cybersecurity Assessment

PROFESSIONAL SERVICES TASK ORDER

TASK ORDER FY22-004.14

Consultant shall perform the Services detailed below in accordance with all the terms and conditions of the Agreement referenced in Item 1A below. All exhibits referenced in Item 8 below are incorporated into this Task Order by this reference. The Consultant shall furnish the necessary facilities, professional, technical and supporting personnel required by this Task Order as described below.

CONTRACT NO. C21179340
OR PURCHASE ORDER REQUISITION NO. (AS APPLICABLE)

- 1A. MASTER AGREEMENT NO. (MAY BE SAME AS CONTRACT / P.O. NO. ABOVE):
- 1B. TASK ORDER NO.: FY22-004.14
- 2. CONSULTANT NAME: Baker Tilly US, LLP
- 3. PERIOD OF PERFORMANCE: START: March 1, 2022 COMPLETION: December 31, 2022
- 4. TOTAL TASK ORDER PRICE: \$110,000
BALANCE REMAINING IN MASTER AGREEMENT/CONTRACT \$TBD
- 5. BUDGET CODE _____
COST CENTER _____
COST ELEMENT _____
WBS/CIP _____
PHASE _____
- 6. CITY PROJECT MANAGER’S NAME & DEPARTMENT:
Greer Stone, Chair of the City Council’s Policy and Services Committee
- 7. DESCRIPTION OF SCOPE OF SERVICES (Attachment A)
MUST INCLUDE:
 - SERVICES AND DELIVERABLES TO BE PROVIDED
 - SCHEDULE OF PERFORMANCE
 - MAXIMUM COMPENSATION AMOUNT AND RATE SCHEDULE (as applicable)
 - REIMBURSABLE EXPENSES, if any (with “not to exceed” amount)
- 8. ATTACHMENTS: A: Task Order Scope of Services B (if any): N/A

I hereby authorize the performance of the work described in this Task Order.

I hereby acknowledge receipt and acceptance of this Task Order and warrant that I have authority to sign on behalf of Consultant.

APPROVED:
CITY OF PALO ALTO

APPROVED:
COMPANY NAME: _____

BY: _____
Name _____
Title _____
Date _____

BY: _____
Name _____
Title _____
Date _____

Attachment A DESCRIPTION OF SCOPE OF SERVICES

Introduction

Attachment A, the Description of Scope of Services, contains the following four (4) elements:

- Services and Deliverables To Be Provided
- Schedule of Performance
- Maximum Compensation Amount and Rate Schedule (*As Applicable*)
- Reimbursable Expenses, if any (With “Not To Exceed” Amount)

Services & Deliverables

Cybersecurity Maturity Assessment

Baker Tilly’s approach to conducting a cybersecurity assessment and developing a cybersecurity program strategy involves four (4) primary steps:

- Step 1: Assessment Planning and Kick-off
- Step 2: Information Gathering
- Step 3: Cybersecurity Capability Analysis and Recommendations
- Step 4: Reporting

Step 1 – Assessment Planning and Kick-off

This step consists of the tasks performed to adequately plan the work necessary to address the overall assessment objective and to solidify mutual understanding of the assessment scope, objectives, assessment process, and timing between stakeholders and assessors. Tasks include:

- Baker Tilly will work with the City to finalize the assessment scope and project timeline. Baker Tilly will also provide the City with an initial interview and documentation request list.
- Finally, Baker Tilly will perform a project kick-off discussion with the City to ensure alignment with the project timeline, interview schedule, and deliverables.

Step 2 – Information Gathering

This step involves conducting interviews with identified IT security personnel and key stakeholders to identify security capabilities, processes, and currently implemented technologies.

Baker Tilly will also review current IT security policy and procedure documentation, as well as network and infrastructure architecture documents.

Step 3 – Cybersecurity Capability Analysis and Recommendations

This step involves mapping current state security capabilities to the NIST Cybersecurity Framework and evaluate the maturity of current security processes. Baker Tilly will also identify current risks related to weaknesses in the City’s cybersecurity program.

Baker Tilly will then review current state capabilities and risks with the City to ensure alignment on Baker Tilly’s initial analysis and identify target state objectives utilizing the Capability Maturity Model (CMMI)

Finally, Baker Tilly will take the identified improvement areas and target state maturity objectives to develop our recommendations for the City’s cybersecurity program to meet its target state objectives.

Step 4 – Reporting

The project team will perform tasks necessary to finalize the initial draft cybersecurity assessment report and review a draft report with the stakeholders. Additionally, the team will submit a final assessment report to the City. Tasks include:

- Develop findings, conclusions, and recommendations based on the supporting evidence gathered
- Validate findings with the appropriate individuals
- Distribute a draft assessment report and conduct a closing meeting with key stakeholders
 - Discuss the assessment results, findings, conclusions, and recommendations
- Obtain written management responses and finalize a report

Deliverables:

The following deliverable will be prepared as part of this engagement:

- Cybersecurity Assessment Report and Program Strategy

External Penetration Testing

Baker Tilly will perform external penetration testing on behalf of the City. Baker Tilly’s approach to conducting these security testing activities involves four (4) primary steps:

- Step 1: Assessment Planning and Kick-off
- Step 2: Open-Source Information Gathering and Reconnaissance
- Step 3: External Penetration Testing
- Step 4: Reporting

Step 1 – Assessment Planning and Kick-off

This step consists of the tasks performed to adequately plan the work necessary to address the overall testing objective and to solidify mutual understanding of the testing scope, objectives, testing process, and timing between stakeholders and assessors. Tasks include:

- Baker Tilly will work with the City to finalize the testing scope and project timeline.
- Baker Tilly will perform a project kick-off discussion with the City to ensure alignment with the project timeline, testing approach, and deliverables.
- Baker Tilly will provide the City with an ISP authorization form and Rules of Engagement documents for signature to confirm testing scope and activities.

Step 2 – Open-Source Information Gathering and Reconnaissance

This step involves conducting interviews with identified IT security personnel and key stakeholders to identify security capabilities, processes, and currently implemented technologies.

Baker Tilly will also review current IT security policy and procedure documentation, as well as network and infrastructure architecture documents.

Step 3 – External Penetration Testing

Baker Tilly will conduct external penetration testing on up to 300 active and 208 dormant external IP addresses provided by the City. External penetration testing services include:

- Confirmation of active versus dormant IP addresses
- Identification of services and service versions running on each active system;
- Automated vulnerability discovery scanning for each active system;
- Penetration attempts on systems identified that have known exploitable vulnerabilities; and
- Deep dive exploitation of any identified exploitable vulnerabilities to gain unauthorized access to internal systems and/or data.

Step 4 – Reporting

The project team will perform tasks necessary to finalize our security testing report and review a draft report with City stakeholders. Additionally, the team will submit a final testing report to the City. Tasks include:

- Develop findings, conclusions, and recommendations based on the supporting evidence gathered
- Validate findings with the appropriate individuals
- Distribute a draft testing report and conduct a closing meeting with key stakeholders
 - Discuss the testing results, findings, conclusions, and recommendations
- Obtain written management responses and finalize a report

Deliverables:

The following deliverable will be prepared as part of this engagement:

- External Penetration Testing Report

Schedule of Performance

Anticipated Start Date: March 1, 2022

Anticipated End Date: December 31, 2022

Maximum Compensation Amount and Rate Schedule

The not-to-exceed maximum, inclusive of reimbursable expenses (as summarized below) for this Task is \$110,000. The not-to-exceed budget is based on an estimate of 525 total project hours, of which 30 are estimated to be completed by the City Auditor.

Reimbursable Expenses

We plan to complete the audit work remotely, including all interviews and documentation review. However, if the City requests the assessment team to travel on-site for meetings, interviews, or assessment report readouts, these travel related expenses will be billed in addition to the fees above.

Audit Activity 4.15 – Wastewater Treatment Plant Agreement

PROFESSIONAL SERVICES TASK ORDER

TASK ORDER FY22-004.15

Consultant shall perform the Services detailed below in accordance with all the terms and conditions of the Agreement referenced in Item 1A below. All exhibits referenced in Item 8 below are incorporated into this Task Order by this reference. The Consultant shall furnish the necessary facilities, professional, technical and supporting personnel required by this Task Order as described below.

CONTRACT NO. C21179340

OR PURCHASE ORDER REQUISITION NO. (AS APPLICABLE)

- 1A. MASTER AGREEMENT NO. (MAY BE SAME AS CONTRACT / P.O. NO. ABOVE):
- 1B. TASK ORDER NO.: FY22-004.14
- 2. CONSULTANT NAME: Baker Tilly US, LLP
- 3. PERIOD OF PERFORMANCE: START: March 1, 2022 COMPLETION: December 31, 2022
- 4. TOTAL TASK ORDER PRICE: \$110,000
BALANCE REMAINING IN MASTER AGREEMENT/CONTRACT \$TBD
- 5. BUDGET CODE _____
COST CENTER _____
COST ELEMENT _____
WBS/CIP _____
PHASE _____
- 6. CITY PROJECT MANAGER’S NAME & DEPARTMENT:
Greer Stone, Chair of the City Council’s Policy and Services Committee
- 7. DESCRIPTION OF SCOPE OF SERVICES (Attachment A)
MUST INCLUDE:
 - SERVICES AND DELIVERABLES TO BE PROVIDED
 - SCHEDULE OF PERFORMANCE
 - MAXIMUM COMPENSATION AMOUNT AND RATE SCHEDULE (as applicable)
 - REIMBURSABLE EXPENSES, if any (with “not to exceed” amount)
- 8. ATTACHMENTS: A: Task Order Scope of Services B (if any): N/A

I hereby authorize the performance of the work described in this Task Order.

I hereby acknowledge receipt and acceptance of this Task Order and warrant that I have authority to sign on behalf of Consultant.

APPROVED:
CITY OF PALO ALTO

APPROVED:
COMPANY NAME: _____

BY: _____
Name _____
Title _____
Date _____

BY: _____
Name _____
Title _____
Date _____

Attachment A DESCRIPTION OF SCOPE OF SERVICES

Introduction

Attachment A, the Description of Scope of Services, contains the following four (4) elements:

- Services and Deliverables To Be Provided
- Schedule of Performance
- Maximum Compensation Amount and Rate Schedule (*As Applicable*)
- Reimbursable Expenses, if any (With “Not To Exceed” Amount)

Services & Deliverables

Baker Tilly’s approach to conducting a Wasterwater Treatment Plant Agreement Review involves three (3) primary steps:

- Step 1: Audit Planning
- Step 2: Process and Control Review
- Step 3: Reporting

Step 1 – Audit Planning

This step consists of the tasks performed to adequately plan the work necessary to address the overall audit objective and to solidify mutual understanding of the audit scope, objectives, audit process, and timing between stakeholders and auditors. Tasks include:

- Gather information to understand the environment under review
 - Understand the organizational structure and objectives
 - Review the City code, regulations, and other standards and expectations
 - Review prior audit results, as applicable
 - Review additional documentation and conduct interviews as necessary
- Assess the audit risk
- Write an audit planning memo and audit program
 - Refine audit objectives and scope
 - Identify the audit procedures to be performed and the evidence to be obtained and examined
- Announce the initiation of the audit and conduct kick-off meeting with key stakeholders
 - Discuss audit objectives, scope, audit process, timing, resources, and expectations
 - Discuss documentation and interview requests for the audit

Step 2 – Process and Control Review

This step involves executing the procedures in the audit program to gather information, interview individuals, and analyze the data and information to obtain sufficient evidence to address the audit objectives. The preliminary audit objective is to: (1) Determine whether adequate controls are in place and working effectively to ensure that costs for treatment plan operations are properly accounted for and allocated; (2) Assess the compliance with contracts and regulations. Procedures include:

- Interview the appropriate individuals to understand the process, the information system used, and internal controls related to accounting and allocation of costs for treatment plan operations.
- Review the contracts, policies and procedures as well as the regulations and standards to identify the criteria to be used for evaluation of compliance and control design and effectiveness
- Review the documents (such as contracts and supporting documents for allocation) for the selected allocation transactions
- Compare the cost accounting and allocation methodology against the requirements

Step 3 – Reporting

In Step 3, the project team will perform tasks necessary to finalize audit working papers, prepare and review a draft report with the stakeholders, and submit a final audit report. Tasks include:

- Develop findings, conclusions, and recommendations based on the supporting evidence gathered
- Validate findings with the appropriate individuals and discuss the root cause of the identified findings
- Complete supervisory review of working papers and a draft audit report
- Distribute a draft audit report and conduct a closing meeting with key stakeholders
 - Discuss the audit results, findings, conclusions, and recommendations
 - Discuss management responses
- Obtain written management responses and finalize a report
- Review report with members of City Council and/or the appropriate Council Committee
- Present the final report to the City Council and/or appropriate Council Committee

Deliverables:

The following deliverable will be prepared as part of this engagement:

- Audit Report

Schedule of Performance

Anticipated Start Date: March 1, 2022
Anticipated End Date: December 31, 2022

Maximum Compensation Amount and Rate Schedule

The not-to-exceed maximum, inclusive of reimbursable expenses (as summarized below) for this Task is \$82,500. The not-to-exceed budget is based on an estimate of 400 total project hours, of which 20 are estimated to be completed by the City Auditor.

Reimbursable Expenses

If circumstances allow, Baker Tilly anticipates planning one on-site fieldwork week. Given this possibility, Baker Tilly could incur reimbursable expenses for this Task.

The not-to-exceed maximum for reimbursable expenses for this Task is \$4,750.

The following summarizes anticipated reimbursable expenses (for three team members):

- Round-trip Airfare – \$1500
- Rental Car - \$400
- Hotel accommodation - \$2500 (4 nights)
- Food and incidentals – \$750

Note that, if current restrictions associated with COVID-19 continue, an on-site visit may not be possible. The project team will work with the City to consider circumstances at the time.



City of Palo Alto

Policy and Services Committee Staff Report

(ID # 14011)

Meeting Date: 3/8/2022

Title: Presentation of the Office of the City Auditor Quarterly Status Report - October to December 2021

From: City Manager

Lead Department: City Auditor

Recommended Motion

The City Auditor recommends that the Policy & Services Committee take the following action:

- 1) Accept the Office of the City Auditor's Quarterly Status Report covering October – December 2021

Discussion

Quarterly Status Report – October – December 2021

In accordance with Task 5 [of our agreement with the City](#), Baker Tilly is required to report quarterly on a variety of topics, generally including progress to plan.

Our presentation includes the following high level status updates organized by task within our agreement with the City:

- Task 1 – Citywide Risk Assessment
 - Kicked-off the Risk Assessment process to be reported in Q3 of FY22 (March 2022)
- Task 2 – Annual Audit Plan
 - Kicked-off the Audit Planning process to be reported in Q3 of FY22 (March 2022)
- Task 3 – Financial Audit
 - Solicited and evaluated proposals for the Financial Auditor, to be presented to the Finance Committee in March/April 2022
 - Presented, in conjunction with the Administrative Services Department, the Financial Audit report prepared by Macias, Gini, O'Connell LLP ([Action Minutes](#); [Video](#))
- Task 4 – Execute Audit Plan

- Presented the Asset Management Audit Activity Report to the Policy & Services Committee, which was subsequently approved by City Council ([Action Minutes](#), [Video](#))
- Presented the IT Risk Management Audit Activity Report to Policy & Services Committee, which was subsequently approved by City Council ([Action Minutes](#), [Video](#))
- Presented the Construction Project Controls Audit Report to the Policy & Services Committee, which was subsequently approved by City Council in January 2022 ([Action Minutes](#), [Video](#))
- Presented the Power Purchase Agreement Report to the Policy & Services Committee, to be presented to Council for approval in Q3 of FY22 ([Action Minutes](#), [Video](#))
- Presented the Initial Public Safety Building Initial Monitoring Memo to the Policy & Services Committee, which was subsequently approved by City Council in January 2022 ([Video](#))
- Initiated the Power Purchase Agreement Audit Activity as approved by City Council on November 15, 2021 ([Action Minutes](#), [Video](#))
- Sought and received Policy & Services Approval for a Task Order to Complete a Wire Payment Process and Controls Review ([Video](#))
- Task 5 – Periodic Reporting and Hotline Monitoring
 - No hotline reports were received during this period.
 - Presented the Office of the City Auditor’s Annual Report ([Action Minutes](#); [Video](#))
- Task 6 – City Auditor evaluation
 - N/A

Timeline, Resource Impact, Policy Implications

The task order and corresponding budget associated with this report by the City Auditor were previously approved. Thus, this report has no impact on City resources.

Environmental Review

The Committee’s approval of the quarterly report does not meet the definition of a “project” under Public Resources Code 21065, therefore California Environmental Quality Act review is not required.