



CITY OF PALO ALTO OFFICE OF THE CITY AUDITOR

October 18, 2010

The Honorable City Council
Palo Alto, California

Auditor's Office Quarterly Report as of September 30, 2010

SUMMARY OF RESULTS

In accordance with the Municipal Code, the City Auditor prepares an annual work plan and issues quarterly reports to the City Council describing the status and progress towards completion of the work plan. This report provides the City Council with an update on the first quarter activities and summarizes our Fiscal Year (FY) 2011 Work Plan activities. Information on the status of each assigned project is attached (pages A-1 through A-4). We are sending this report as an Informational Item to ensure the City Council receives the required report during my leave of absence. We anticipate the City Council will be appointing an Acting City Auditor in the near future.

Completed Projects

During the first quarter of FY 2011, the City Auditor's Office issued the following reports to the City Council:

- Report on the Status of Audit Recommendations (October - 2010)
- Audit of Citywide Cash Handling and Travel Expenses (September - 2010)
- Restatement of Greenhouse Gas Emissions and Energy Savings in City Operations -
Joint memo issued with the City Manager's Office (August - 2010)
- City of Palo Alto Sales Tax Digest Summary First Quarter Sales for January -
March 2010 (July - 2010)
- Annual Audit Work Plan with Risk Assessment (July -2010)
- Auditor's Office Quarterly Report as of June 30, 2010 (July - 2010)
- Follow-Up Discussion of Options to Implement a Fraud, Waste, and Abuse Hotline (July -2010)
- Discussion of Survey Options for the FY 2010 Service Efforts and Accomplishments Report (July - 2010)

Highlights of the completed projects including the following:

- The City Auditor's annual report on the status of audit recommendations identified additional savings and program improvements from the departments' implementation of audit recommendations. During the last two years, departments implemented 82% of 142 backlogged audit recommendations with significant results, and 96% of audit recommendations from reports issued during 2009.

- The Audit of Citywide Cash Handling and Travel Expenses identified internal control improvements for the City's \$14M decentralized revenue processing system. The audit also recommended steps to coordinate the travel expense payment process while improving oversight.
- The City Auditor's Office promptly responded to the Finance Committee's special request to review greenhouse gas emissions data, identified additional savings of \$240,000 and worked collaboratively with the Climate Protection Plan Team to issue a joint memo with the City Manager's Office.
- The City Auditor's Office followed up with the Policy & Services Committee to identify additional survey options for use in the upcoming SEA Report and to discuss options for a fraud, waste, and abuse hotline.

In-process Projects

The following projects are in-process:

- Prospective Analysis of Library Bond Measure Proceeds
- Audit of Purchasing Card Transactions
- SAP Account Sampling
- Annual Service Efforts and Accomplishment Report (SEA)
- Audit of Utilities Department

Other Information

- In September 2010, Mimi Nguyen joined our office as a Senior Performance Auditor. This position is part of the City Council's approval in the FY 2011 Budget to provide continuous and on-going audits of Enterprise Funds.
- Senior Performance Auditor, Ian Hagerman, completed the certification process for the Certified Internal Auditor (CIA) and the Certified Fraud Examiner (CFE) certifications.

On behalf of the City Auditor's Office, I would like to express my appreciation to City staff for their cooperation and assistance during our reviews throughout this year.

Respectfully submitted,



Lynda Flores Brouchoud
City Auditor

Attachment:

- Status of Audit Projects as of September 30, 2010

Status of Audit Projects as of September 30, 2010

Original Audit Project Description and Preliminary Objectives	Status	Accomplishments Year-To-Date	Items to be Completed
AUDIT ADMINISTRATION, FOLLOW-UP AND OTHER RESPONSIBILITIES			
1) Annual Audit Work Plan and Quarterly Status Reports – The Auditor's Office submits quarterly reports to the City Council outlining project status and progress towards completing the assignments on this annual work plan.	Completed	Development of FY 2011 Work Plan completed. First quarterly report completed.	
2) Annual Audit Recommendation Status Report – The Municipal Code requires the City Auditor to issue an annual report on the implementation status of recommendations from recently completed audits. We also meet with the departments involved during the year to discuss progress towards implementing open audit recommendations.	Completed	Report issued October 2010. The report summarized the status of 71 audit recommendations from 12 different reports. During the last two years, departments implemented 82% of 142 backlogged audit recommendations with significant results, and 96% of audit recommendations from reports issued during 2009.	
3) Meeting Attendance – To facilitate internal communication and coordination of efforts, the City Auditor attends: <i>a. City Manager's weekly executive leadership team meetings budget meetings.</i> <i>b. Utility Risk Oversight and Coordinating Committee (UROCC)</i> – Since issuance of our <i>Assessment of Utility Risk Management Procedures</i> in July 2002, the City Auditor has acted as an advisor to the UROCC.	On-going On-going		
4) Request for Proposals (RFP) for the External Financial Auditor Contract (NEW) – The City's Charter requires the City Council to engage a certified public accounting firm to conduct the City's annual financial statement audit and also requires the City Auditor to coordinate the audit. The City's contract with the current vendor expires in FY 2011.			Target date: April 2011

Original Audit Project Description and Preliminary Objectives	Status	Accomplishments Year-To-Date	Items to be Completed
REVENUE AUDITS AND MONITORING			
4) Sales and Use Tax Allocation Reviews – Sales and use tax represented about 13%, or \$18.2 million, of projected General Fund revenue in the City's Adopted Operating Budget for FY 2011. The Auditor's Office contracts with MuniServices for quarterly sales and use tax recovery and information services, and we also conduct sales and use tax monitoring in-house. The purpose of this monitoring is to identify misallocations of local sales and use tax of companies doing business in Palo Alto. In addition, MuniServices prepares the quarterly sales and use tax information reports that are provided to the City Council as informational items. The contract with MuniServices expires in March 2011.	On-going	In the first quarter of FY 2010, the City received \$6,232 in sales and use tax recoveries related to misallocation of tax from 6 companies. In addition, potential misallocations from – 44 companies (15 MuniServices and 29 City of Palo Alto) are pending resolution by the State Board of Equalization. Total Sales and Use Tax Recoveries: FY 2011 \$6,232 (MuniServices - \$2,229 and the City Auditor's Office - \$4,003)	
5) Alternative Fuel Tax Credit Recoveries – As part of the Auditor's Office continuous revenue monitoring efforts and findings from the Audit of Fleet Utilization and Replacement, the Auditor's Office initiated revenue recoveries from the Federal government's alternative fuel tax program, which was in effect through December 31, 2009. Extensions have not yet been determined.	On-going	The Auditor's Office worked with ASD, Utilities, and our revenue consultant to prepare a claim for the alternative fuel tax credit for FY 2010. We anticipate filing the claim next quarter once extensions have been determined.	
FINANCIAL AUDITS AND PROCEDURAL REVIEWS			
7) Annual External Financial Audit (contracted audit service) – The City Charter requires that the City Council engage an independent certified public accounting firm to conduct the annual external audit.	In process	Maze & Associates began interim audit work in March to prepare for the audit of the June 30, 2010 financial statements.	Dec- 2010
8) SAP Account Sampling – The City implemented the SAP system and upgrades to serve as an enterprise management system for a variety of key financial information and transactions including payroll, utility billing and financial transactions. The purpose of these reviews will be to provide continuous monitoring and sampling of accounts within the SAP system to test for internal controls and to identify efficiencies and cost savings.	In process	Preliminary survey completed. Risk Assessment phase in process.	Target completion date: TBD

Original Audit Project Description and Preliminary Objectives	Status	Accomplishments Year-To-Date	Items to be Completed
PERFORMANCE AUDITS AND SPECIAL PROJECTS			
9) Annual Service Efforts and Accomplishments (SEA) Report	In process	The 9th annual SEA Report is in process. Surveys were mailed to residents and collection is in process.	Jan-2011
10) Audit of Citywide Cash Handling - The purpose of this review is to study Citywide cash handling and travel reimbursement, oversight procedures, and the City Auditor's history of audits on cash services.	Completed	<i>Audit of Citywide Cash Handling and Travel Expenses</i> issued Sept-2010.	
11) Prospective Analysis of Bond Measure Proceeds – Through the 2008 voter-approved Measure N, the City is preparing to issue general obligation bonds to rebuild the Mitchell Park Library and adjacent community center, and renovate the Main and Downtown libraries. This audit will prospectively evaluate controls for the use of the general obligation bond funds to ensure the funds are used efficiently and in compliance with federal regulations for the use of tax-exempt bond funds.	In process	Preliminary Findings have been shared with the departments and report writing is in process.	Nov-2010
12) Audit of Purchasing Card Transactions – The purpose of this audit is to determine the adequacy of controls over purchasing card transactions, and to assess compliance with existing guidelines and procedures.	In process	Preliminary survey completed. Risk Assessment phase in process.	Target completion date: March-2011
13) Utilities Department – Several of the highest risk areas identified in the Citywide Risk Assessment pertain to the Utilities Department. This audit will conduct a preliminary survey of the Utilities Department and develop an audit scope to identify opportunities for improvements in efficiency and effectiveness.	In process	Audit initiated Sept-2010.	Target completion date: TBD
14) Wastewater Treatment Fund – The Regional Water Quality Control Plant provides services to Mountain View, Los Altos, Los Altos Hills, Stanford, and East Palo Alto. With proposed revenues of \$22 million, proposed expenditures of \$20 million, this is one of the areas consistently targeted by our annual citywide risk assessment model. The purpose of our audit would be to review the cost-sharing agreements and allocation of charges to partner agencies.	Not started		Target completion date: TBD

Original Audit Project Description and Preliminary Objectives	Status	Accomplishments Year-To-Date	Items to be Completed
15) Planning and Community Development Permit Process (NEW) – Two of the top ten risk assessment areas pertain to the Development Center Services and Planning and Community Environment Department. In FY 2010, Council requested the Auditor's Office review the permit process to identify opportunities for efficiency and effectiveness. Simultaneously, the City Manager and Department also initiated efforts to study the permit process and identify improvements. Because these staff improvements are in-process, the City Manager has requested a temporary deferral of this audit to coordinate the audit work with Staff's improvement efforts.	Not started	Audit temporarily deferred to provide the City Manager and Planning and Community Development Department time to implement program improvements.	Target completion date: TBD
16) Audit of Fleet Purchases (NEW) – As a result of the April 2010 Audit of Fleet Utilization and Replacement, the Finance Committee recommended the City Auditor review the City's fleet purchases to assess whether the City is purchasing appropriately-sized vehicles at the lowest available cost.	Not started		
17) Follow-up Recommendation Status on the 2010 Audit of Fleet Utilization and Replacement (NEW) - As a result of the April 2010 Audit of Fleet Utilization and Replacement, the Finance Committee directed the Public Works Department to return in January 2011 with an assessment of their implementation of the audit recommendations. The Finance Committee directed the City Auditor's Office to identify any audit recommendations staff was not adequately implementing.	In process	The Auditor's Office and Public Works staff reviewed the audit recommendations as part of the annual recommendation status report. Of the 22 audit recommendations, 15 had made progress (2 completed and 13 in process).	
18) Human Resources Employee Benefits (NEW) – Two of the top ten risk assessment areas pertain to the Human Resources Department and employee benefits. In FY 2011, the projected benefit costs are expected to be over \$43M. This audit would review benefit oversight, costs and administration through the Human Resources Department.	Not started		