



Office of the City Auditor

INFORMATION CALENDAR
February 26, 2008

To: Honorable Mayor and Members of the City Council
From: Ann-Marie Hogan, City Auditor
Submitted by: Ann-Marie Hogan, City Auditor
Subject: City Auditor’s Annual Report for Fiscal Year 2007

SUMMARY

Attached is the City Auditor’s Annual Report for Fiscal Year 2007. This report details accomplishments of the Performance Audit division and will be available on the City Auditor’s website.

CURRENT SITUATION AND ITS EFFECTS

During fiscal year 2007, the City Auditor’s Office issued the following audit reports:

- Emergency Medical Personal Protective Equipment Review
- Fire Department Ambulance Billing Audit
- Fire Department Audit – Lost Time and Overtime
- Follow-up Audit of Public Works Construction Contracts
- Business License Tax Program Audit Report for Fiscal Year 2006

We also successfully passed our Peer Review, amended BMC Chapter 2.24: City Auditor’s Duties and Authority, and reported to Council on the status of outstanding recommendations.

The City Auditor’s Office reviewed 441 contracts and selected payments and continued to present our *Internal Controls for City Staff: Safeguarding Assets, Preventing Fraud, and Measuring Performance* PowerPoint presentation on internal controls and fraud prevention to City staff.

The Auditor’s Office assessed 24 residential rental property owners a total of \$128,460 in unpaid business license taxes, penalties, and interest. The Business License Tax Audit report for fiscal year 2007 is being presented to Council this evening.

Attached is Exhibit A, the most recent list of outstanding recommendations. These recommendations are either partially implemented or not implemented. As part of our performance measures we track the percentage of audit recommendations implemented timely.

POSSIBLE FUTURE ACTION AND FISCAL IMPACTS

We will continue to allocate staff resources that will result in the City receiving tax revenue it may not otherwise receive, and through our audits we will continue to develop recommendations to identify and mitigate risks and to reduce costs in the long run.

CONTACT PERSON

Ann-Marie Hogan, City Auditor, 981-6750

Attachment

1: Audit: City Auditor's Annual Report for Fiscal Year 2007

City of Berkeley



City Auditor's Annual Report For Fiscal Year 2007

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Presented to Council on February 26, 2008

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City Auditor's Annual Report for Fiscal Year 2007
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I. Mission, Measurement, and Results

The City Auditor's Office Mission

The City Auditor's Office mission is to provide independent oversight of City operations and to be a catalyst for improving City government. Performance audits provide unbiased assessments of the use of public resources.

"The concept of accountability for public resources is key to our nation's governing process and a critical element for a healthy democracy."

U.S. Comptroller General David Walker, cover letter to 2003 Government Audit Standards

Independent Auditors are a Good Investment

Audit work can lead to new revenue, cost recovery, and increased efficiency, which have an economic impact well beyond the audit costs. An independent performance audit department is an investment that benefits the City.

Measuring Quality: Who Audits the Auditor?

Berkeley's auditors have been in the forefront of the move to improve the quality and usefulness of audit work. We asked the voters to amend the Charter in 1998, to require that we follow Government Audit Standards. The standards require peer reviews of our audit work every three years.

In October 2006, peer reviewers awarded our office the highest rating possible for quality and professionalism.

Who Are the Auditors?

Collectively, City of Berkeley auditors have over 90 years of combined professional audit experience. Our active engagement in local and national audit organizations has included board membership, publication in professional journals, presentations at audit conferences and the League of California Cities, and conducting peer reviews.

Audit staff hold the following certifications:

| <i>Type of Certification</i> | <i>Number*</i> |
|---|----------------|
| Certified Public Accountant (CPA) | 1 |
| Certified Internal Auditor (CIA) | 3 |
| Certified Government Auditing Professional (CGAP) | 3 |
| Certified Fraud Examiner (CFE) | 2 |

* Most audit staff have more than one certification.

Key Performance Measures

“Legitimacy and trust are essential values in all government undertakings, and performance auditing may contribute to strengthening these values by producing public and reliable information on the economy, efficiency, and effectiveness of government programs.”

*INTOSAI's
Implementation
Guidelines for
Performance
Auditing*

A significant benefit of performing audit work in house is that we are able to track and follow-up on the status of findings and recommendations on a continuing basis. The most important measure of an auditor's work is this: What changed for the better because we were here?

As part of our performance measures, we measure agreement with or acceptance of our recommendations. We have continued to exceed our target measure of a 95% acceptance rate.

Secondly, we measure impact: the percent of audit recommendations implemented timely (before the report goes to Council). This outcome measure tells us “what changed” because of our work. It is also an indication of whether we communicated well with departmental management and whether those managers took prompt action.

Our target measure is a 40% implementation rate at the time the audit goes to Council. In FY02 and FY03, staff achieved about a 60% implementation rate. In FY04 through FY06, however, implementation declined sharply, to a low of 26% in both FY05 and FY06.

As we reported last year, the City Auditor, Audit Committee and City Manager were concerned that staff was not timely implementing our recommendations. We discussed the possibility that three years of budget cuts resulting in reduced staffing in oversight and support functions, may have created unacceptable levels of risk.

These risks were discussed in our reports, “Internal Control Risks Associated with Budget Cuts and Freezes” issued December 9, 2003 and “Delayed Implementation of Audit Recommendations “ issued December 13, 2005, which can be viewed at <http://www.cityofberkeley.info/auditor/currentaudits.htm>.

In FY07, departments reported implementation rates averaging 42% before the reports went to Council. Better yet, preliminary results for the first half of FY08 show a 68% rate of implementation before report issuance.

| Key Performance Measures | | | | |
|--|------|------|------|------------------|
| | FY04 | FY05 | FY06 | FY07 |
| Number of completed audits per fiscal year as a percent of plan | 73% | 50% | 71% | 63% ¹ |
| Percent of recommendations accepted by auditee (goal: 95%) | 100% | 97% | 100% | 100% |
| Average percent of recommendations (by audit) reported implemented or partially implemented by operating departments before report issued ² (goal: 40%) | 37% | 26% | 26% | 42% |
| Percent of all recommendations reported implemented or partially implemented by operating departments within one year ³ (goal: 65%) | 61% | 79% | 91% | 48% |
| Percent of all recommendations reported implemented or partially implemented by operating departments within two years ⁴ (goal: 95%) | 81% | 96% | 91% | 91% |

¹An audit that was not included on the original audit plan was requested and added toward the end of the fiscal year. The percent of audits completed based on the original audits planned was 71%.

²Report issue date falls between 7/1/06-6/30/07

³Report issue date falls between 7/1/05-6/30/06

⁴Report issue date falls between 7/1/04-6/30/05

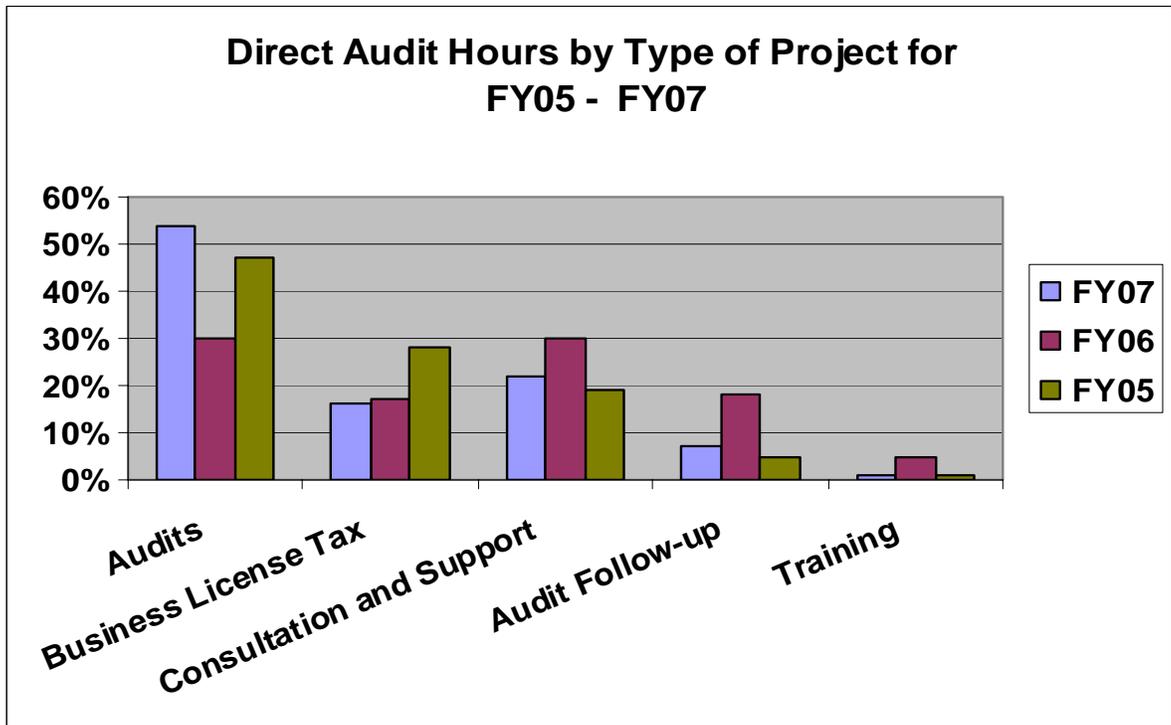
Responding to Changing Conditions

The difficulties City staff was having implementing our recommendations caused us to make some changes in our allocation of audit staff time in 2006, which appears to have had a positive impact in FY07. In FY06, we decided that we would spend less time performing audits, and more time giving City staff the guidance needed to implement change. We spent more time training – especially in Internal Controls and Fraud Prevention, consulting, and following-up on outstanding recommendations through monitoring and reporting.

We believe that spending less of our time on audits and more time on follow up and training may have helped City staff improve the timeliness of making needed changes. Support from the City Manager and the Finance Director was also a factor, and much appreciated.

For FY07, Council audit advisors asked us to spend more audit resources on operational performance, particularly in Public Safety. We began a series of audits in Fire and Police, which are continuing in 2008. Due to heightened concerns about weak internal controls and unmitigated risks, we also received a number of audit requests from Department heads and management. These are being assessed for risk and if selected for audit will be completed along with the Public Safety audits.

Time devoted to revenue identification (Business License Tax) was reduced in FY07 because of the implementation of the City Manager's budget cuts, eliminating two (of seven) staff auditors. As noted in our budget message, these resources (and the corresponding revenue) will be further reduced by additional budget cuts in 2009.



II. Audit Reports

The average business lifespan is five years, the exception being rental properties. However, if all Business License Tax auditees were still in business, the City would be collecting an additional \$811,485 in business license tax per year.

Business License Tax Program Audit Report for Fiscal Year 2006 (Issued February 13, 2007)

http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3_-_General/BLTFY2006.pdf

This report documents the Business License Tax revenue identification efforts and accomplishments of the Auditor's Office during FY06, primarily audits of Berkeley residential rental properties carried over from FY05. The Auditor's Office was able to use the passage of Ballot Measure P (which permits the City to use Rent Board information to help enforce City ordinances) as a new opportunity to identify rental properties that were unlicensed or were paying significantly less tax than what was due. Business License Tax audits resulted in 11 businesses being billed a total of \$44,002 during FY06. As of June 30, 2006, five cases totaling \$71,657 were referred to Finance for collection. During FY06, four appeals were presented to the City's Hearing Officer. As a result the City waived a total of \$80,153 in taxes, penalties, and interest.

Follow-up Audit of Public Works Construction Contracts (Issued February 27, 2007)

http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3_-_General/FollowupConstructionAudit2-27-07.pdf

The City was not holding the utility companies accountable for paying for or adequately repairing damage done to our City streets. Results: Bumpy streets and insufficient revenue.

Many of the recommendations of our earlier report were implemented. However, we found that utility company street cuts in the City are causing bumpy streets, increasing the cost of street maintenance, and reducing the life of City pavement. We made recommendations to better hold the utility companies accountable, to monitor the workload of the engineers, to examine the impact of the street cuts and resultant repair work due to utility work, and to improve the transparency of the bidding process. We identified \$140,000 in fees not billed, and \$62,000 in billings, going back to December 2005, not collected. As an immediate result of this audit, \$19,000 in outstanding billings was collected and deposited in the General Fund in December 2006.

This is an excellent report and provides the clearest analysis of key Fire Department budget issues that I have yet seen in Berkeley.

Berkeley Resident

Fire Department Audit – Lost Time and Overtime (Issued May 22, 2007)
[http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3 -
_General/FireOvertimeLosttimeAudit5-22-07.pdf](http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3_-_General/FireOvertimeLosttimeAudit5-22-07.pdf)

From FY02 to FY06, the Berkeley Fire Department incurred an average payroll cost for lost time of \$806,980 a year. Lost time and overtime were costly, but systems were in place for monitoring lost time and for assigning overtime equitably. The use of overtime in the Berkeley Fire Department was considerably less expensive than hiring new staff.

Fire Department Ambulance Billing Audit (Issued June 12, 2007)
[http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3 -
_General/FireAmbulanceBilling6-12-07.pdf](http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3_-_General/FireAmbulanceBilling6-12-07.pdf)

Neither the Fire Department nor the Finance Department provided sufficient oversight and direction to the outside contractor charged with ambulance billing and collection, and neither sufficiently monitored the contractor's performance. Additionally, neither took a sufficient leadership role in ambulance billing and collection operations.

Could insuring more residents decrease Fire calls for service? Better data collection and reports, as well as assertive coordination with other City and health-related stakeholders could pay off.

Although only 12% of Berkeley residents between 18 and 64 are reportedly uninsured, the rate of uninsured among users of the ambulance service appears closer to 30%. According to Berkeley's Health Officer, this could be because the uninsured do not have access to routine health services. Approximately \$1.8 million of the nearly \$5.7 million ambulance billings in FY06 were for presumable uninsured patients. Any efforts the City can make to partner with other stakeholders and to support proposals for expanding health coverage such as Medi-Cal could positively impact not only the fiscal health of the City and workload of City staff, but the health of the community.

Emergency Medical Personal Protective Equipment Audit (Issued June 26, 2007)
[http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3 -
_General/FireAudit_ProtectiveEquip6-26-07.pdf](http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3_-_General/FireAudit_ProtectiveEquip6-26-07.pdf)

The Fire department appeared to be providing emergency medical service (EMS) staff with appropriate medical personal protective equipment (PPE). However, EMS responders were not always using some types of medical PPE when appropriate. The reasons given were complacency and lack of enforcement. We also identified some concerns with the medical supply inventory procedures, which could result in instances of out-of-stock medical PPE as well as other types of inventory problems.

III. Other Reports

Amending BMC Chapter 2.24: City Auditor's Duties and Authority (Issued October 24, 2006)

http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3_-_General/AmendingBMCcitations10-24-06.pdf

This amendment to the BMC gives the auditors the authority to issue administrative citations. Authorization to issue administrative citations provides the auditors with a means to enforce their right to audit businesses and rental property owners, and help ensure taxpayers pay their fair share.

Peer Review of the City of Berkeley Auditor's Office (Issued February 13, 2007)

http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3_-_General/PeerReview2-13-07.pdf

The peer review found that the Berkeley City Auditor's Office was in full compliance with Generally Accepted Government Auditing Standards for fiscal years 2004 through 2006 and awarded us the highest rating possible for quality and professionalism.

Outstanding Audit Recommendations (Issued March 13, 2007)

http://www.ci.berkeley.ca.us/uploadedFiles/Auditor/Level_3_-_General/OutstandingAudits3-13-07.pdf

Outstanding Audit Recommendations (Issued June 26, 2007)

http://www.ci.berkeley.ca.us/auditor/pdf/Outstanding%20Audit%20Recom%20as%20of%205-31-07_6-26-07.pdf

A significant benefit of performing audit work in house, rather than contracting it out, is that we are able to track and follow-up on the status of findings and recommendations on a continuing basis. The purpose of the two **Outstanding Audit Recommendations** reports above were to inform Council of the status of audits in which recommendations were not yet implemented.

IV. Revenue, Oversight, and Training

Revenue Audits: Business License Tax (BLT)

During FY07, the Auditor's Office assessed 24 residential rental property owners a total of \$128,460 in unpaid taxes, penalties, and interest.

Between 1982 and 2007, auditors have billed taxes, penalties, and interests totaling \$4,868,810. Since non-compliant businesses will often pay the correct tax after the audit, the identified revenue is not a one-time windfall, but generally becomes part of the future revenue stream. For each \$100,000 identified by audit, about \$16,666 in additional revenue can be expected for each future year, as long as the audited businesses continue to generate consistent sales.

Contracts

The City Charter requires that all contracts be countersigned and registered by the City Auditor. Our office performs limited reviews of selected contracts. During FY07, 441 contracts were reviewed by the City Auditor's Office.

Citywide Training

- During FY07, we presented our *Internal Controls for City Staff: Safeguarding Assets, Preventing Fraud, and Measuring Performance* Power Point presentation on internal controls and fraud prevention to 56 employees. Between FY03 and FY07 the City Auditor's Office trained 440 employees in fraud prevention and internal controls.

V. Looking Towards the Future

One of the key challenges for local governments, and for their auditors, is the extent to which structural deficits exist at the federal and state level, regardless of conditions in an individual locality.

The U.S. Comptroller General, David Walker, has undertaken a major public education campaign on the subject of the long term federal structural deficit. An excellent resource that links his presentation to the problems of individual cities is a report by the Kansas City Auditor's Office. It can be viewed at <http://www.kcmo.org/auditor/05-06audits/financialfutureforum.pdf>

Given the state and federal structural deficits, our audit strategy continues to address improving the ability of City staff to monitor the effective use of City resources, through our training, consulting, follow up work, and performance audits.

We have also increased our efforts to empower City staff by providing training about the importance of management (internal) controls.

Finally, by providing reliable and objective information about City programs and services, we hope to enhance the ability of staff, City Council, and Berkeley residents to make informed decisions about performance, programs, and resources.

Status of Report on Open Audits
Number of Outstanding Recommendations
As of February 1, 2008

| Audit Title | Date of Audit Report | Scheduled Council Report | Total Recom. | Total Outstanding Recom. |
|---|----------------------|--------------------------|--------------|--------------------------|
| FY 2008 Surprise Cash Count: Permit Service Center | 11/6/2007 | 5/15/2008 | 5 | 2 |
| Nature Center Surprise Cash Count Audit: Controls Over Cash Receipts Need Improvement | 11/6/2007 | 2/26/2008 | 7 | 3 |
| FY 2008 Surprise Cash Count: Berkeley Animal Shelter | 10/9/2007 | 2/26/2008 | 6 | 5 |
| Marina Surprise Cash Count Audit: Controls Over Cash Receipts Need Improvement | 10/9/2007 | 2/26/2008 | 5 | 5 |
| Fire Department Audit - Controlled Substances | 10/9/2007 | 9/23/2008 | 12 | 12 |
| Audit of Police Asset Forfeiture Deposit Accounts | 9/11/2007 | 3/25/2008 | 9 | 3 |
| Emergency Medical Personal Protective Equipment Review | 6/26/2007 | 3/31/2008 | 4 | 4 |
| Fire Department Audit - Ambulance Billing | 6/12/2007 | 9/30/2008 | 23 | 19 |
| Fire Department Audit - Lost Time and Overtime | 5/22/2007 | 9/30/2008 | 6 | 4 |
| Follow-Up Audit of Public Works Construction Contracts | 2/27/2007 | 3/25/2008 | 22 | 14 |
| Audit of the Association of Sports Field Users | 5/23/2006 | 3/25/2008 | 13 | 7 |
| Follow-up Cash Receipts / Cash Handling Audit | 5/16/2006 | 5/6/2008 | 7 | 2 |
| Parcel Based Special Taxes, Fees, and Assessments Audit | 3/15/2005 | 7/31/2008 | 22 | 6 |

Status of Report on Open Audits
Number of Outstanding Recommendations
As of February 1, 2008

| | | | | |
|--|------------|-----------|------------|------------|
| Purchase Order Audit - Select Public Works Divisions At the Corporation Yard | 3/15/2005 | 6/24/2008 | 23 | 3 |
| Citywide Contract Compliance Audit | 5/18/2004 | 2/26/2008 | 18 | 4 |
| FUND\$ Change Management Audit | 5/4/2004 | 3/25/2008 | 23 | 12 |
| Accounts Payable Audit | 12/16/2003 | 4/8/2008 | 16 | 2 |
| Information Systems General Controls Audit | 9/16/2003 | 3/25/2008 | 27 | 3 |
| Customer Service Cash Receipts / Cash Handling Audit | 4/8/2003 | 5/6/2008 | 23 | 5 |
| Cash Receipts/Cash Handling Audit - Treasury | 9/17/2002 | 5/6/2008 | 19 | 1 |
| Cash Receipts/Cash Handling Audit - Parks, Recreation & Waterfront | 9/17/2002 | 2/26/2008 | 20 | 2 |
| Police Staffing Audit | 4/30/2002 | 5/20/2008 | 11 | 5 |
| Business License Tax Audit Report For Year Ending June 30, 1999 | 4/11/2000 | 6/17/2008 | 7 | 1 |
| Departmental Budget Monitoring Audit | 11/23/1999 | 3/25/2008 | 15 | 6 |
| Safety Members Pension Fund Audit for The Year Ended June 30, 1998 | 4/20/1999 | 3/25/2008 | 8 | 1 |
| Public Works Grants Audit | 9/16/1997 | 4/8/2008 | 8 | 1 |
| Accounts Payable Audit (Dated September 26, 1995) | 9/26/1995 | 4/8/2008 | 8 | 1 |
| Berkeley Police Department Cash Receipts Audit | 9/12/1995 | 3/25/2008 | 17 | 1 |
| TOTAL - 28 Audits | | | 384 | 134 |

