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# **PERFORMANCE AUDIT OF THE DEVELOPMENT SERVICES DEPARTMENT ADMINISTRATION OF DEPOSIT ACCOUNTS FOR DEVELOPMENT PROJECTS**

**Office of the  
City Auditor**

**City of San Diego**



The Development Services Department is Extending City Credit to Some Customers and is at Risk of Losing a Significant Amount of Money Due to the Ineffective Administration of Deposit Accounts

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## THE CITY OF SAN DIEGO

February 7, 2020

Honorable Mayor, City Council, and Audit Committee Members  
City of San Diego, California

Transmitted herewith is a performance audit report on the Development Services Department Administration of Deposit Accounts for Development Projects. This report was conducted in accordance with the City Auditor's Fiscal Year 2019 Audit Work Plan, and the report is presented in accordance with City Charter Section 39.2. The Results in Brief are presented on page 1. Audit Objectives, Scope, and Methodology are presented in Appendix B. Management's responses to our audit recommendations are presented after page 48 of this report.

We would like to thank staff from the Development Services Department, Public Works Department, Office of the City Treasurer, and Department of Finance for their assistance and cooperation during this audit. All of their valuable time and efforts spent on providing us information is greatly appreciated. The audit staff members responsible for this audit report are Chris Kime, Megan Garth, Zoya Ahmed, and Danielle Knighten.

Respectfully submitted,

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Interim City Auditor, CPA, CIA, CFE

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Honorable City Council Members  
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## Results in Brief

The Development Services Department (DSD) provides review, permit, inspection, and code enforcement services for private and public development projects throughout the City of San Diego (City). DSD's major functions include entitlements, building construction and safety, engineering mapping, current planning, and code enforcement which are organized in a manner to manage the development process for the City. DSD operates largely as an Enterprise Fund, separate from the City's General Fund, charging fees in exchange for services. Because its development review and inspection services component are operated without General Fund subsidy, customers pay for the operating costs similar to most businesses.

However, some projects with highly variable costs, if charged on a fee basis, would cause some customers to pay far more than the actual cost of processing their project while others would pay far less. In these cases, DSD requires customers to set up a deposit account to recover costs in some development projects that are less predictable on a single project basis in terms of costs. DSD has over 4,000 individual deposit accounts, together which compose the Subdivision Trust Fund. These accounts can be for discretionary or ministerial projects. Discretionary projects involve requesting approval for land use entitlements. Ministerial engineering projects are for grading and public right-of-way permits and mapping actions.

A deposit account is created with an initial deposit, which City staff draw against to pay for time and materials associated with project reviews and/or inspections. Customers are required to make subsequent deposits to maintain a minimum required balance (MRB) to pay for all City staff labor charges and other expenses associated with ongoing review.

We found that DSD does not follow its own policy in setting the MRB for ministerial and discretionary projects with deposit accounts. Accurately setting and enforcing the MRB is essential to ensure that projects have enough money to cover ongoing project expenses incurred by City staff who review projects. However, DSD management permits its project managers to use discretion when setting the MRB during project milestones as they estimate upcoming project costs. DSD management views the use of discretion as a necessary aspect of providing good customer service. DSD has not developed controls to implement its policy for setting the MRB. As a result, deposit accounts frequently fall into deficit and City staff continue working on projects with deficit account balances, despite the requirement to stop working on projects with deficit balances. Continued work on projects with deficit balances increases the risk that money will go unpaid to the City. The lack of MRB and continued work on projects with deficit balances possibly creates a violation of the City Charter which prohibits extending credit to any individual, association or corporation. Lastly, the use of discretion creates inequity between what customers pay, with some paying more than others for the same level of service.

We also found that DSD does not effectively identify and pursue money owed to the City because it has not established an efficient and effective process to do so. The process for monitoring and invoicing deficit accounts is an informal, manual process that DSD staff performs as time allows. Without timely review, the invoicing process and referral to Office of the City Treasurer's (Treasurer) Delinquent Accounts Program (Collections), if applicable, is delayed - decreasing the chances for collection of past due amounts. As of July 2019, there were 1,384 deposit accounts with deficit balances totaling \$4.6 million. Although \$3.0 million has been invoiced and remains outstanding, we identified another \$1.4 million that should be invoiced immediately.

Additionally, untimely review and irregular invoicing creates inequity between the City services as some customers receive services without payment. There is also the risk that some customers receive permits or completion of their projects without payment.

To address the issues mentioned above, we made eleven recommendations. They include MRB policies and procedures revision, policy clarification, training and implementation of automated controls as well as procedures and controls for stopping work on projects with deficit balances. For monitoring and invoicing of deficit accounts, we recommended establishing review and invoicing procedures, direct invoicing of deposit accounts and immediate invoicing of past due accounts.

Management has agreed to implement all eleven recommendations.



# Background

In accordance with the Office of the City Auditor's Fiscal Year (FY) 2019 Audit Work Plan, we conducted a performance audit of the City of San Diego's (City) Development Services Department's (DSD) administration of deposit accounts. The overall objective of this audit was to determine the efficiency and effectiveness of DSD's billing process for deposit accounts.

## **Development Services Department**

DSD is a department within the City that provides review, permit, inspection, and code enforcement services for private and public development projects throughout the City. Its mission is to ensure quality development by delivering consistent, transparent, and effective customer service to all stakeholders. DSD's major functions include entitlements, building construction and safety, engineering mapping, current planning, and code enforcement which are organized in a manner to manage the development process for the City.

DSD operates largely as an Enterprise Fund, separate from the City's General Fund, charging fees in exchange for services. Because its development review and inspection services component are operated without General Fund subsidy, customers pay for the operating costs similar to most businesses. Service levels provided are directly related to the fees charged and the fees may not exceed the estimated reasonable cost of providing the service.

The Development Services Fund (non-General Fund) is \$81.7 million in the adopted FY20 budget (shown in **Exhibit 1**) with the following breakdown by expenditure and revenue.

**Exhibit 1:**

**Development Services Fund Expenditures, FY20**

**Department Expenditures**

	FY2018 Actual	FY2019 Budget	FY2020 Adopted	FY2019-2020 Change
Administration & Support Services	\$ 29,097,621	\$ 22,764,050	\$ 24,300,224	\$ 1,536,174
Building & Safety	19,675,257	19,887,301	23,575,206	3,687,905
Engineering	8,027,293	11,789,015	15,385,067	3,596,052
Land Development Review	5,539,618	8,324,210	8,794,406	470,196
Project Submittal & Management	8,155,840	9,680,594	9,671,578	(9,016)
<b>Total</b>	<b>\$ 70,495,630</b>	<b>\$ 72,445,170</b>	<b>\$ 81,726,481</b>	<b>\$ 9,281,311</b>

**Revenues by Category**

	FY2018 Actual	FY2019 Budget	FY2020 Adopted	FY2019-2020 Change
Charges for Services	\$ 8,928,990	\$ 9,482,173	\$ 8,785,141	\$(697,032)
Fines Forfeitures and Penalties	5,500	-	-	-
Licenses and Permits	54,024,570	53,427,616	68,040,456	14,612,840
Other Revenue	1,112,939	1,216,023	1,216,023	-
Rev from Money and Prop	354,938	110,072	110,072	-
Transfers In	1,513,921	243,439	200,000	\$(43,439)
<b>Total</b>	<b>\$ 65,940,859</b>	<b>\$ 64,479,323</b>	<b>\$ 78,351,692</b>	<b>\$ 13,872,369</b>

Source: DSD's FY20 Adopted Budget.

**User Fees vs Customer  
Deposit Accounts**

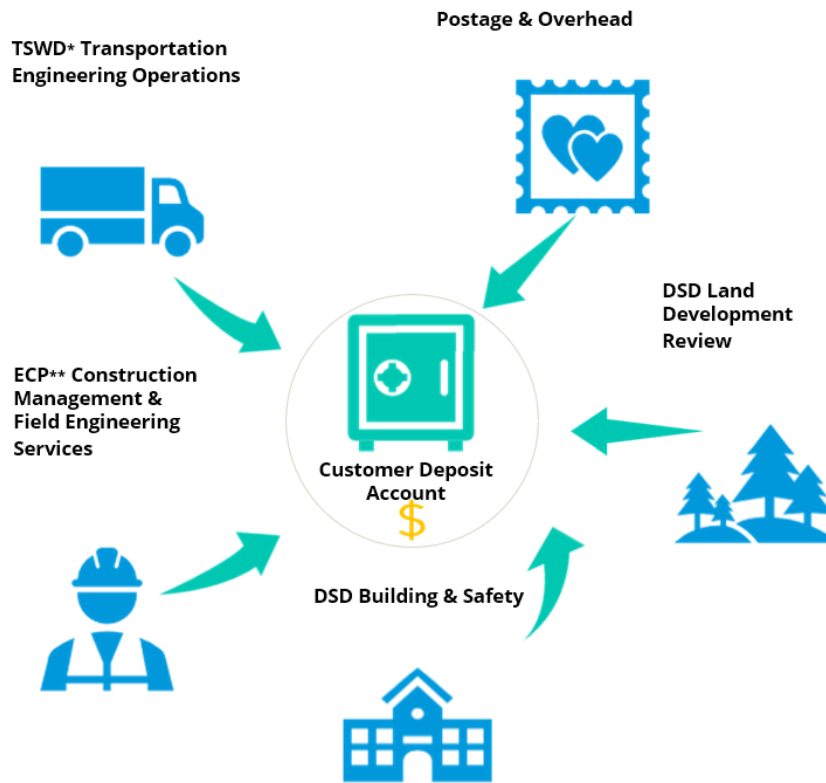
As required in City Council Policy 100-05, an in-depth user fee study should be undertaken at least every five years at the direction of DSD's director. DSD's last fee proposal was completed in May 2016. Most of the services can be priced on a fee for service basis. DSD, customers, and other stakeholders prefer that DSD use fees wherever possible to charge for services to make processing costs more predictable for customers. However, some projects with highly variable costs, if charged on a fee basis, would cause some customers to pay far more than the actual cost of processing their project while others would pay far less. In these cases, DSD requires customers to set up a deposit account to recover costs in some development projects that are less predictable on a single project basis in terms of costs. DSD has over 4,000 individual deposit accounts, together which compose the Subdivision Trust Fund. Deposit account revenue was \$12.4 million and \$12.6 million in FY18 and FY19, respectively.

A deposit account is created with an initial deposit, which City staff draw against to pay for time and materials associated with project reviews and/or inspections. The deposit amount depends on the size and type of project and is displayed in DSD’s fee schedules, also known as information bulletins (**see Appendix C**). Customers are required to make subsequent deposits to maintain a minimum required balance (MRB) to pay for all City staff labor charges and other expenses associated with ongoing review and/or inspections. **Exhibit 2** provides examples of services charged to deposit accounts.

**Exhibit 2:**

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**Examples of Services Charged to Deposit Accounts**



Source: OCA generated based on DSD’s descriptions of deposit accounts and review of customer statements.

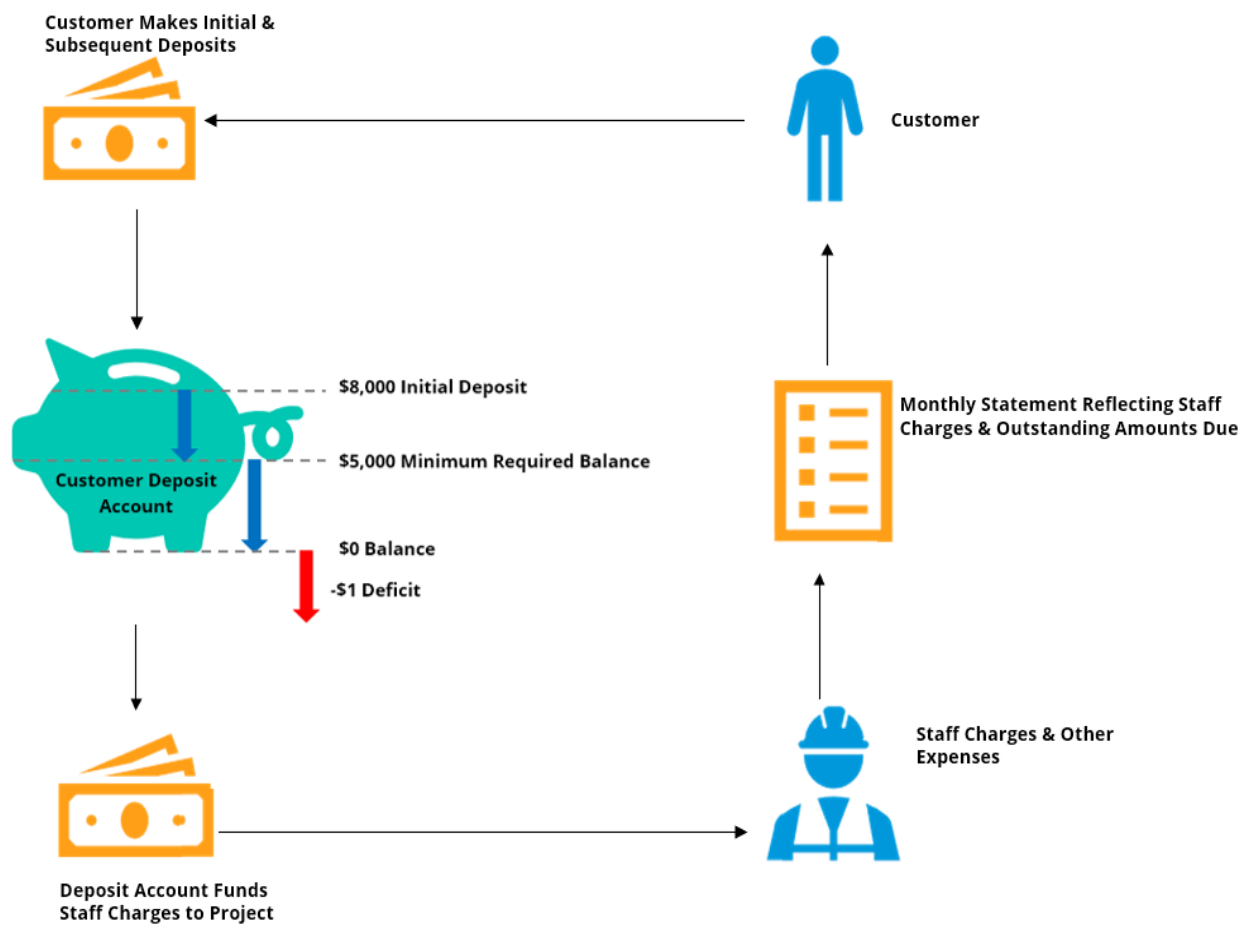
\*TSWD is an abbreviation for the Transportation and Storm Water Department

\*\*ECP is an abbreviation for the Public Works Department’s Engineering and Capital Projects Construction Management and Field Engineering Division. ECP staff typically perform inspections on ministerial projects that involve grading and public right-of-way permits.

Each month, customers receive a monthly deposit account statement reflecting the charges made against their accounts and outstanding amounts due that are necessary to cover the charges accrued and to maintain their accounts' MRB. **Exhibit 3** shows the billing cycle for deposit accounts. If customers do not make subsequent deposits, these accounts go into deficit. According to DSD's procedure, City staff are to immediately suspend working on projects with deficit accounts to prevent extending City credit – possibly prohibited by the City Charter. Deposit accounts are typically required for two types of projects: discretionary and ministerial engineering projects.

**Exhibit 3:**

**Deposit Account Billing Cycle**



Source: OCA generated based on DSD's descriptions of deposit accounts.

**Discretionary  
Development Projects**

Discretionary projects involve requesting approval for land use entitlements. Common reasons for discretionary review include proposals to modify a previously conforming use, development proposing to deviate from zoning requirements, development projects located in environmentally sensitive lands, development involving historical resources, and development located in the Coastal Zone. Discretionary approvals are granted at the discretion of a City decision-maker and may require a public hearing. Depending on the type of permit, the decision maker may be City staff, the hearing officer, the Planning Commission or the City Council. If multiple discretionary permits are required for a project, they will be decided together by the highest-level decision maker. Approvals include everything from small single-family home additions to master planned communities of several hundred acres.

Discretionary approvals can take several months to years to process and can cost customers anywhere from a few thousand dollars to hundreds of thousands of dollars. There is no reliable way to forecast project time and costs because these elements are dependent upon several unpredictable factors, such as project complexity, quality of information received, and demand set by market conditions. While many discretionary projects with a single approval type require a flat fee, other projects, including those with multiple approvals, require a deposit account to pay for ongoing project costs. Deposit accounts for discretionary projects are set up in accordance with DSD's fee schedule, Information Bulletin 503 (see **Appendix C**).

DSD assigns project managers to oversee discretionary projects. According to DSD, project managers are expected to estimate near-term upcoming project costs and restrict workflow on projects that have deposit accounts in deficit. As sole points of contact for customers, project managers are responsible for checking deposit account balances regularly, including at various milestones: biweekly, during review, prior

to a hearing, or prior to recordation. Project managers are also responsible for identifying erroneous account charges, requesting additional deposits, collecting on past due balances, and stopping work on projects with negative balances. According to DSD, project managers typically manage a large volume of projects (30-40) at one time.

Once a discretionary approval is granted and a discretionary permit is issued and recorded, a development is considered "entitled" and may then enter the construction phase to process any required ministerial approvals associated with the project, including building permits, grading permits, right-of-way permits and final maps.

### **Ministerial Engineering Projects**

Ministerial engineering projects for grading and public right-of-way (ROW) permits and mapping actions may require the setup of deposit accounts. Once DSD issues the permits for these projects, it sets up a deposit account to pay for inspections of improvements in the ROW, grading, landscape and irrigation and drainage work. DSD collects the inspection fees and deposits on behalf of the Public Works Department (Public Works): the department that performs inspections on ROW permits and most grading permits. Deposit accounts for inspections are set up in accordance with DSD's fee schedule, Information Bulletin 502 (see **Appendix C**).

According to DSD's policy, a lead staff person is responsible for checking inspection account balances at various milestones in the inspection process. These milestones include, but are not limited to, upon completion of each review, prior to permit issuance, prior to recordation of maps, when a client applies for an extension of time prior to inspection, and prior to bond release. The lead reviewer may (or should) also request additional deposits from customers when necessary or suspend work on a project with a negative deposit account balance.

**Deposit Account  
Tracking and Billing  
Process**

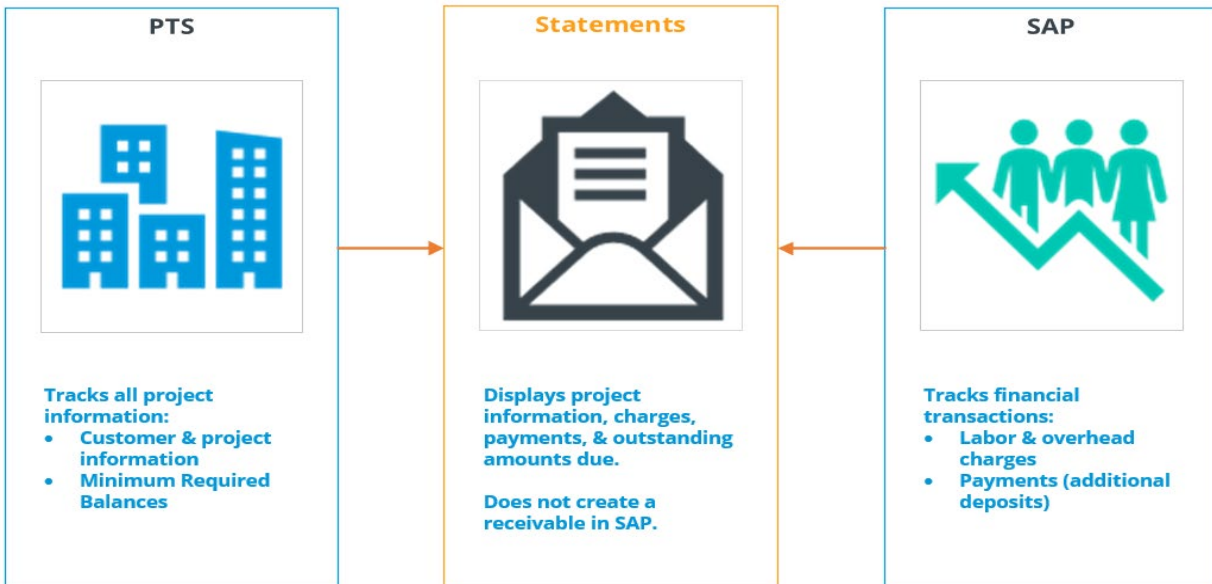
Two systems are used to track and manage project charges and workflow: SAP and DSD's Project Tracking System (PTS). SAP, the City's Enterprise Resource Planning system, tracks all financial transactions that are associated with a deposit account. Each project with a deposit account is assigned an internal order number (IO) in SAP. Initial deposits are posted to SAP the day after the deposit is made. While DSD is responsible for monitoring deposit accounts, staff from other authorized departments frequently contribute work on projects and therefore charge their labor to the IOs associated with a project. Other departments that charge and derive revenue from DSD's deposit accounts are as follows: Environmental Services, Parks & Recreation, Planning, Public Utilities, Public Works, and Transportation and Storm Water. Non-personnel expenses, such as overhead charges, are also charged to deposit accounts.

PTS manages the entire workflow related to processing development permits within the City. PTS contains information such as customer name and address, project scope and title, and project status. It also contains the financially responsible party information – the person who is responsible for receiving statements and making additional deposits when necessary. Importantly, project managers use PTS to set the MRB for projects.

Together, the information from SAP and PTS is combined to generate monthly statements that are mailed to customers. See **Exhibit 4:**

**Exhibit 4:**

**Information from PTS and SAP is Combined to Create Deposit Account Statements for Customers**



Source: OCA generated based on review of DSD's descriptions of the billing process and interviews with personnel from DSD and the Treasurer.

**Referral to Collections**

Some inherent delays within the billing system make it likely that charges will continue to accrue after statements are mailed. Therefore, it is important for accounts to maintain the MRB. These delays include:

- Payroll is charged in SAP in arrears on a biweekly basis;
- Overhead charges are posted to deposit accounts at the end of the month; and
- Labor charges continue to accrue on projects.

In **Exhibit 5**, we show an example of charges accrued in January that will not be billed and mailed to a customer until nearly the end of February. With payment due mid-March, a customer will pay for charges accrued nearly two months prior. Meanwhile, labor charges will continue to accrue.



**Exhibit 5:**

**Example of Delays in Billing Process for Deposit Accounts**

January						
S	M	T	W	TH	F	S
		1	2	3	4	5
6	7	8	9	10	11	12
13	14	15	16	17	18	19
20	21	22	23	24	25	26
27	28	29	30	31		

- Accounting period closes at month end for further transactions on deposit accounts.

February						
S	M	T	W	TH	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28		

- SAP and PTS data merged to create customer statements.
- Statements are prepared and mailed to customers in approx. 1 week.

March						
S	M	T	W	TH	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28	29	30
31						

- Payments for transactions occurring in January are typically due in mid-March.
- Customers typically have 2 weeks to pay.



Source: OCA generated based on interviews with DSD.

The statements show all account labor charges including previous balances and payments. They also show the MRB which is netted to the account balance. Although the statements contain a listing of staff charges, total amount due, and due date, they do not create an account receivable (AR) in SAP.<sup>1</sup> Therefore, the statements are not recorded in the City's financial system as an amount owed the City and are therefore not true invoices.

**Invoicing for Deficit Deposit Accounts and the Collections Process**

Because the statements do not create an AR in SAP, DSD staff manually reviews accounts that have been in deficit for three months and invoice them in SAP to pursue collections on outstanding amounts. The SAP invoice creates the AR in SAP. Staff reviews two reports in SAP to obtain deposit account balances:

<sup>1</sup> Accounts receivable is the balance of money due to a firm for goods or services delivered or used but not yet paid for by customers. Accounts receivables are listed on the balance sheet as a current asset. Accounts receivable is any amount of money owed by customers for purchases made on credit. <https://www.investopedia.com/terms/a/accountsreceivable.asp>

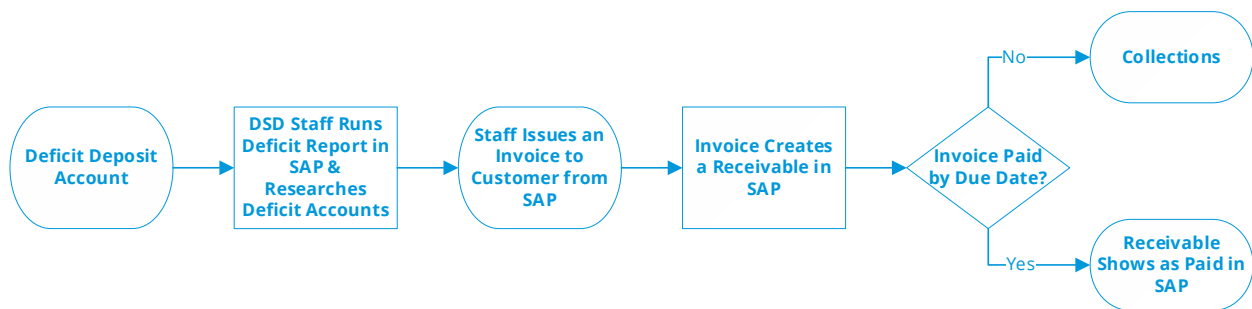
- 1) DSD IO Report – which shows balances for all deposit accounts; and
- 2) DSD Deficit IO Report – which shows only accounts with deficit balances.

After reviewing deficit deposit accounts, DSD staff is responsible for generating an invoice in SAP that creates a receivable in SAP. According to SAP’s dunning procedure, SAP automatically refers invoices to the Office of the City Treasurer’s (Treasurer) Delinquent Accounts Program (Collections) if they remain outstanding after the due date - 30 days for non-government accounts and 90 days for government accounts. Once the customer pays the invoice, the receivable shows as paid in SAP. **Exhibit 6** shows the invoice generation and collections process.

**Exhibit 6:**

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**Invoicing and Collections Process in SAP**



Source: OCA generated based on review of City billing process narratives and interviews with personnel from DSD and the Treasurer.

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Timely invoicing and referral to Collections is the most important element to increasing collectability on deficit accounts. The collection rate of invoiced deficit deposit accounts has been 59 percent between FY11 – FY19. Cumulatively, \$7.4 million has been invoiced with \$4.4 million paid, leaving an outstanding invoiced amount of \$3.0 million due the City.

Soon, DSD anticipates implementation of its new permitting software, Accela. Accela is a tracking system that DSD has procured to manage its permitting, code enforcement, and invoicing activities. Accela may simplify the billing and invoicing process.

**Previous Review of the  
Administration of  
Deposit Accounts**

We previously reviewed the administration of deposit accounts in our *Performance Audit of the City Treasurer's Delinquent Accounts Program*, issued December 9, 2009. To identify opportunities to improve the collection process of past due accounts, we reviewed the billing and collection practices of several City departments, including DSD, that refer past due amounts to the Collections. We observed significant weaknesses in the City's billing process and in DSD's collection practices, many of which persist today and will be discussed in this report. Some of the findings from the December 2009 report were:

- DSD has a decentralized and mostly manual billing process for deposit accounts;
  - Customers' monthly statements do not create receivables in the City's billing system, SAP;
  - PTS does not suspend all work on a project with a deficit deposit account;
  - Billing and collections efforts primarily fall upon the discretion of staff at DSD;
- Customers with deficit deposit accounts continue to receive City services – in violation of the City Charter – without paying for these services; and
- DSD does not invoice deficit accounts in a timely manner, resulting in millions of uncollected fees.

One issue previously affecting DSD staff's review and collection on deficit deposit accounts included the difficulty in obtaining accurate account balances – a time-consuming task that required checking two systems and performing calculations. In response to our previous recommendations, the Treasurer created the DSD Deficit IO Report in SAP for DSD's use to show the balances of deficit deposit accounts.

## Audit Results

### ***Finding 1: Deposit Accounts' Minimum Required Balances are Insufficient to Cover Ongoing Project Expenses Leading to Deficit Amounts that May Not be Paid to the City***

The City of San Diego's (City) Development Services Department (DSD) does not follow its own policy in setting the minimum required balance (MRB) for ministerial and discretionary projects with deposit accounts. Accurately setting and enforcing the MRB is essential to ensure that projects have enough money to cover ongoing project expenses incurred by City staff who review projects. However, DSD management permits its project managers to use discretion when setting the MRB during project milestones as they estimate upcoming project costs. DSD management views the use of discretion as a necessary aspect of providing good customer service. DSD has not developed controls to implement its policy for setting the MRB. As a result, deposit accounts frequently fall into deficit and City staff continue working on projects with deficit account balances, despite the requirement to stop working on projects with deficit balances. Continued work on projects with deficit balances increases the risk that money will go unpaid to the City.

The lack of MRB and continued work on projects with deficit balances possibly creates a violation of the City Charter which prohibits extending credit to any individual, association or corporation. Lastly, the use of discretion creates inequity between what customers pay, with some paying more than others for the same level of service. We made seven recommendations that include MRB policies and procedures

revision, policy clarification, training and implementation of automated controls as well as procedures and controls for stopping work on projects with deficit balances.

**DSD Does Not Follow  
Its Policy When Setting  
the MRB for Deposit  
Accounts**

DSD does not set the MRB for deposit accounts in accordance with its policy. Setting the MRB in accordance with DSD's information bulletins 502 and 503 is important to ensure that projects have the money to support ongoing project costs (see **Appendix C** for the bulletins). Although the MRB varies depending on the project type, the lowest MRB for ministerial projects is \$700 and for discretionary projects it is \$1,200. Deposit accounts must maintain a positive minimum balance in accordance with the information bulletins to ensure available funds to cover ongoing project costs.

We reviewed the MRB amounts as shown in DSD's project tracking system (PTS) as of July 2019, for all DSD's 4,012 deposit accounts that were created from FY02 – present. We found that 61 percent of the deposit accounts for ministerial and discretionary projects have an MRB of \$0 as shown in **Exhibit 7**. It is important to note that the information bulletins do not show any instances where the MRB should be zero.

**Exhibit 7:**

**Most Deposit Accounts Among the Two Project Types Have a Minimum Required Balance of \$0**

Minimum Required Balance Range	Deposit Accounts by Project Type FY02-Present		
	Ministerial	Discretionary	Total
\$0	1,628	836	2,464
\$1 - \$1,000	34	4	38
\$1,001 - \$2,000	953	22	975
\$2,001 - \$3,000	99	26	125
\$3,001 - \$4,000	138	16	154
\$4,001 - \$5,000	8	178	186
\$5,001 and up	9	61	70
<b>Total</b>	<b>2,869</b>	<b>1,143</b>	<b>4,012</b>

Source: DSD's Project Tracking System (PTS).

Additionally, we reviewed DSD's Deficit IO Report, a report showing 1,384 accounts in deficit as of July 2019, and found that 75 percent of deficit accounts have an MRB of \$0.

In our testing of 87 discretionary projects created in FY19, we combined the MRB amounts for projects with multiple approvals and found that the DSD could have collected an additional \$410,200 had it correctly set the MRB for these projects. With approximately 40 percent of discretionary projects having two or more approvals, combining the MRB is essential to ensuring that projects have adequate funds to pay for ongoing project costs.

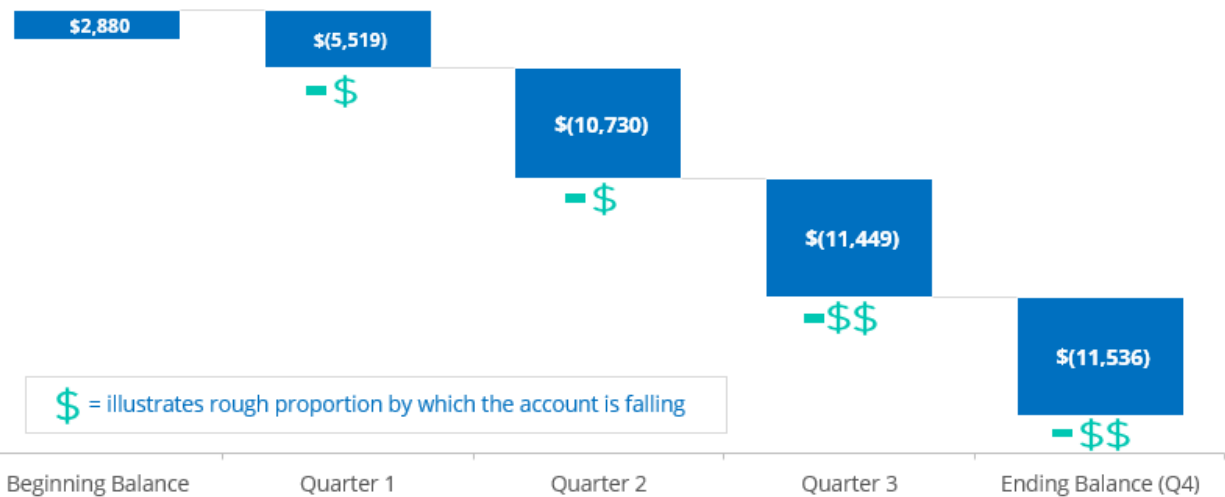
We reviewed the MRB for 475 deposit accounts for ministerial projects that were created between FY17-FY19 and found that 370 (77 percent) had a \$0 MRB in PTS. Substituting the lowest MRB of \$700 for the 370 deposit accounts that had a \$0 MRB in PTS, we calculated that the City could have collected at least an additional \$259,000 for these accounts as a cushion for non-payment.

**City Staff Continue Working on Projects with Deficit Balances which Extends Credit and Creates Greater Exposure to Loss of Unpaid Labor Costs**

In our review of deficit accounts for FY19, we found that staff continues working on projects with negative balances. For instance, we found 20 projects that began the year with a total deficit balance of \$184,262 and ended the year with a total deficit of \$316,931, suggesting that these projects had ongoing charges (and growing deficits) during the year. In a second example (shown in **Exhibit 8**), one project began the year with a surplus balance of \$2,880 and quickly fell into deficit after 1 month while charges continued to accrue for 11 months and ended the year with a deficit balance of \$11,536.

**Exhibit 8:**

**Over 12 months, a Deposit Account Began with a Positive Balance and Subsequently Accrued \$14,416 in Project Charges and Ended with a Deficit Balance of \$11,536**



Source: OCA based on DSD's Deficit IO Report as of July 2019.

Continued work on projects with deficit balances extends credit to customers, allows unpaid labor charges to grow and increases the risk that money will go unpaid to the City.



**DSD Management  
Allows Project  
Managers Discretion  
to Set the MRB for  
Discretionary Projects  
with Deposit Accounts**

DSD management allows staff to use discretion when setting the MRB for discretionary projects with deposit accounts in a variety of ways, viewing its information bulletins as merely guidelines rather than official policy and as a way of providing good customer service.

**Information Bulletin is  
Unclear on Setting  
MRB for Discretionary  
Projects with Multiple  
Approval Types**

Although DSD's Information Bulletin 503 requires combining the initial deposit amounts for each approval within a project that has multiple approvals (e.g., Coastal Development Permit with a Site Development Permit), it is less clear as to whether this requirement also applies to the subsequent MRB. Calculating the subsequent MRB using the same method, however, is appropriate because the level of service the department can provide is directly related to the fees charged. A discretionary project with three approvals requiring an initial deposit of \$30,000, for instance, would require a subsequent MRB of \$24,000 – not \$8,000 as required for one approval type. Without clear direction for projects with multiple approval types, project managers can choose a lower MRB as applicable to the project which may not reflect the project costs incurred by the City.

**MRB Adjusted Based  
on Perceived Customer  
Access to Funds**

Project managers must request additional deposits from customers when account balances are below the MRB. Although customers should make additional deposits when requested by their account statements, the statements do not create a receivable in the system (SAP). According to project managers, they are reluctant to ask a customer to pay the current outstanding amount (as shown in SAP) because it may be higher than what is shown on a customer's statement.<sup>2</sup> Project managers stated that they prefer that customers have access to all funds necessary to keep projects moving rather than risk "overcharging" them. According to

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<sup>2</sup> Statement balances are usually 2 months old by the time the customer receives the statement. Charges have likely accrued to a customer's deposit account by the time of statement receipt.

DSD management, refunds can take up to several months which may in turn delay projects because customers potentially have access to fewer funds. However, this process increases the risk that City staff will continue working on projects that are in deficit without assurance of payment, especially if the customer's payment is not sufficient to meet the MRB.

**MRB Changed  
According to Project  
Milestones**

Project managers can change the MRB based on agreement with the customer, during project milestones (e.g., prior to a hearing or prior to permit recordation), or during project close. While project managers stated that this is a common practice, we did not find any evidence outlining circumstances where the MRB can be adjusted. Project managers must manually check account balances on a regular basis (e.g., biweekly, during review, etc.). In practice, project managers perform this task as time allows, typically focusing on active projects during project milestones (e.g., prior to a hearing or prior to permit recordation). As a result, overlooked accounts may fall below the MRB or become negative while staff continue working on the projects.

**DSD Project Managers  
do Not Follow Policy  
and Stop Work on  
Projects with Deficit  
Account Balances**

DSD project managers are also responsible for stopping work on projects with negative account balances. However, identifying projects with deficit accounts is unreliable due to project managers' inconsistent process and sole responsibility for monitoring deposit account balances. Once project managers identify accounts with negative balances, they may send courtesy collection letters (via mail or email) to customers and email project staff to discontinue working on these projects. PTS also does not have controls to notify or prevent staff from continuing to work on projects with negative deposit account balances. Therefore, stopping work on projects is contingent upon several manual processes initiated by project managers: identification of deficit accounts, notification to customers for additional deposits,

issuance of emails to staff to stop work, and staff's receipt of and compliance with these emails. Absent supervisory oversight and controls in PTS, there is little assurance that this process is carried out. As a result, staff continue working on projects with negative deposit account balances.

**DSD Project Managers  
are not Actively  
Managing Deposit  
Accounts for  
Ministerial Projects**

DSD policy and Information Bulletin 502, governing ministerial engineering projects with deposit accounts, give DSD the responsibility for managing these deposit accounts: setting the MRB, collecting initial and subsequent deposits, and assigning a lead staff person to check account balances during project milestones. DSD issues the permits for ministerial engineering projects - typically involving grading and right-of-way permits (ROW) - and sets up a deposit account to cover the cost of subsequent inspections that are conducted by the Public Works Department (Public Works). However, we found that DSD and Public Works management dispute this responsibility. According to DSD, Public Works' staff can set the MRB in PTS or it can contact DSD staff to request additional deposits from the account's financially responsible party (FRP). Public Works management, in response, reiterated that DSD is responsible for managing deposit accounts for ministerial engineering projects which includes setting up the accounts, ensuring sufficient positive balances and requesting additional deposits when necessary.

As a result, Public Works continues inspections regardless of account balances for public safety reasons. In addition, although policy states that a lead staff person is responsible for setting the MRB and requesting additional deposits from customers when necessary, we found that the MRB for 370 of 475 deposit accounts for ministerial projects that were created between FY17 - FY19 had a \$0 MRB in PTS. Ministerial project deposit accounts comprise 64 percent of accounts in deficit as of July 2019. Low MRBs and Public Works' practice of continuing inspections in the public ROW regardless of deposit account balances likely contributes to this high percentage. The lack of administration of deposit

accounts for ministerial projects creates the risk that these accounts will end up in deficit – and risks the City's loss of unpaid labor costs.

**DSD Lacks Internal and System Controls to Maintain Account Balances and Prevent Accounts from Becoming Deficit**

PTS does not have key controls to ensure that the MRB is correctly calculated and maintained for ministerial and discretionary projects with deposit accounts. Specifically, PTS does not automatically calculate the MRB by tying it to the appropriate approval types or disallow incorrect entries. PTS also does not contain the construction cost estimate that is used to calculate the MRB for ministerial projects with deposit accounts. As a result, project managers and/or other staff directly enter the MRB into PTS without assurance of accuracy.

The absence of several factors – controls on who can change the MRB, and external documentation showing supervisory approval of MRB – makes it nearly impossible to determine why the MRB was set at the specified amount and by whom. It also makes it difficult to determine and address errors, either amongst specific staff persons or in each department. Identifying errors can lead to training opportunities for staff on how to correctly calculate the MRB for deposit accounts.

There is a computer glitch in PTS that is erroneously setting the MRB to \$0 for some active projects when administrative staff enter the FRP information. The FRP is the person or entity responsible for maintaining the deposit account. While this glitch may explain why some of the accounts in our sample have a \$0 MRB, it does not account for other cases where the MRB is incorrect and how discretion is used to change the MRB (see discussion above). DSD discovered the glitch after our office informed DSD of the large number of accounts with a \$0 MRB. DSD has instructed staff to manually re-enter the MRB after the FRP input. However, the absence of system controls or documentation with supervisory approval showing the original MRB makes it difficult to guarantee that the new MRB

will be set in accordance with policy. Additionally, DSD is not making system changes to prevent the glitch from occurring because it anticipates the implementation of its new system, Accela, in FY20 as a replacement for PTS. According to a former deputy director, Accela supports the elements for which the City has traditionally used trust accounts and it has stronger mechanisms to restrict workflow on deficit accounts than available in PTS. Therefore, Accela may address many of the system internal controls issues we've identified in this section.

Lastly, PTS does not have any automated controls preventing staff from continuing to work on projects with deficit deposit accounts. Consequently, stopping work is almost entirely contingent upon project managers or others to notice the deficits and to alert appropriate staff to discontinue work.

**Using Discretion When  
Setting the MRB  
Creates Inequity  
Between Customers**

Allowing project managers to use discretion when enforcing the MRB creates inequity between what customers pay for the same services. In the example shown in **Exhibit 9**, two customers with the same development project containing the same approvals should have been assessed an MRB of \$10,000 each in accordance with policy. However, because the project managers used discretion to set the MRB, one customer had an MRB of \$0 while the other had an MRB of \$8,000, resulting in an \$8,000 inequity between the two. Ultimately, neither customer was required to maintain the MRB of \$10,000 per department policy.

**Exhibit 9:**

**Example of Inequity Between Two Customers**



**EXAMPLE OF INEQUITY**

\*Two customers each have a discretionary project with the same approval types.

\*Project managers use discretion to set the minimum required balance.

<u>Development Project</u>	<u>Customer A</u>	<u>Customer B</u>
Coastal Development Permit		
Site Development Permit		
<b>Minimum Required Balance (MRB)</b>	<b>\$0.00</b>	<b>\$8,000</b>

*Difference of \$8,000 - Inequity between Customers*

Source: OCA generated based on two actual occurrences.

**Recommendation #1:** We recommend Development Services Department establish formal written policies establishing the authority and approvals for setting and changing the minimum required balance in project tracking system or Accela. This policy should describe the project managers roles, responsibilities, level of authority, required documentation and supervisory review and approval. (Priority 2)

**Recommendation #2:** We recommend Development Services Department (DSD) automate minimum required balance (MRB) calculation in project tracking system or Accela. Specifically, the approval types should be tied to specific MRB amounts as set forth in DSD’s information bulletins, 502 and 503. (Priority 2)

**Recommendation #3:** We recommend Development Services Department revise Information Bulletin 503 to clearly state that the specific minimum required balance (MRB) amounts for discretionary projects with multiple approval/policy types will be combined to calculate total required MRB. This process should also be automated in project tracking system and/or Accela. (Priority 2)

- Recommendation #4:** We recommend Development Services Department train project managers on the new policy for establishing the authority and approvals for setting and changing the MRB in project tracking system or Accela. (Priority 2)
- Recommendation #5:** We recommend Development Services Department work with the Public Works Department to develop procedures that clearly define roles and responsibilities for setting the MRB in applicable ministerial deposit accounts and stopping work on projects with deficit deposit account balances. (Priority 2)
- Recommendation #6:** We recommend Development Services Department develop policies and procedures to suspend work on projects with a negative balance until a positive balance has been reestablished for projects with deficit deposit accounts. (Priority 2)
- Recommendation #7:** We recommend Development Services Department automate the following information technology controls in project tracking system (PTS) and/or Accela to:
- a. Fix the glitch in the PTS that causes the minimum required balance (MRB) to revert to \$0;
  - b. Calculate the MRB automatically – e.g., tie approvals to the appropriate dollar amounts; and
  - c. Notify staff to stop working on projects with deficit deposit account balances. (Priority 2)

## ***Finding 2: Deposit Accounts with Deficit Balances are Not Reviewed, Researched, and Invoiced in a Timely Manner***

While Finding 1 demonstrates the importance of enforcing minimum required balance (MRB) and stopping work on projects with deficits, we also found that Development Services Department (DSD) does not effectively identify and pursue money owed to the City because it has not established an efficient and effective process to do so. The process for monitoring and invoicing deficit accounts is an informal, manual process that DSD staff performs as time allows. Without timely review, the invoicing process and referral to Office of the City Treasurer's (Treasurer) Delinquent Accounts Program (Collections), if applicable, is delayed - decreasing the chances for collection of past due amounts. As of July 2019, there were 1,384 deposit accounts with deficit balances totaling \$4.6 million. Although \$3.0 million has been invoiced and remains outstanding, we identified another \$1.4 million that should be invoiced immediately. Additionally, untimely review and irregular invoicing creates inequity between the City services as some customers receive services without payment. There is also the risk that some customers receive permits or completion of their projects without payment. We made four recommendations that include establishing review and invoicing procedures, direct invoicing of deposit accounts and immediate invoicing of past due accounts.

### **Deficit Deposit Accounts are Not Invoiced Timely**

Timely invoicing is the most important element to increasing collectability. However, DSD does not invoice deficit accounts in a timely manner. According to DSD and the Treasurer, DSD should research and then invoice deficit accounts when they have been in deficit for three months. However, DSD does not have formal policies and procedures on the frequency and



methodology for researching and invoicing deficit deposit accounts.

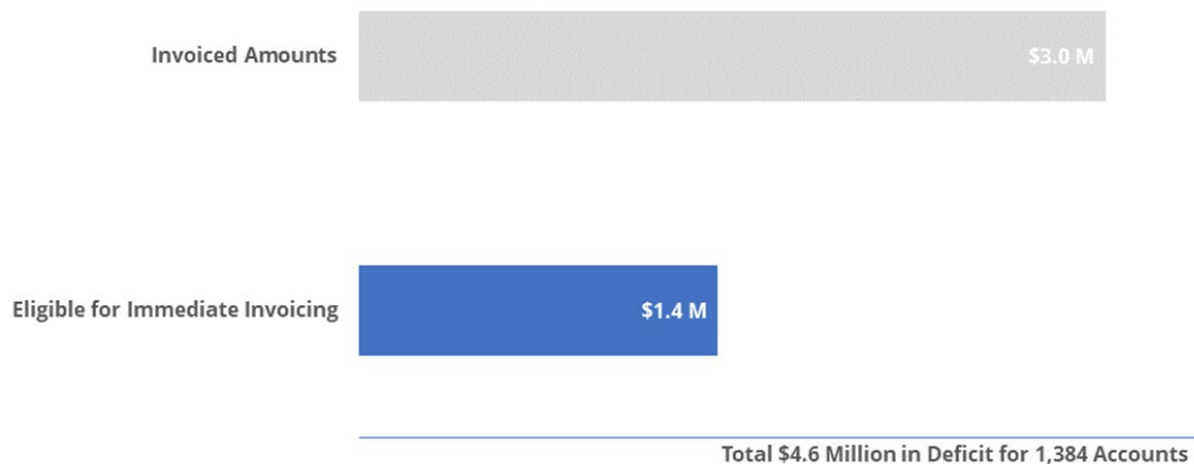
Using the three-month deficit criterion, we found that approximately \$1.4 million is eligible to be invoiced immediately; many of these accounts have been in deficit for up to 12 months.

See **Exhibit 10**.

**Exhibit 10:**

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**\$1.4 Million in Deficit was Eligible to Be Invoiced as of July 2019**



Source: OCA generated based on review of DSD's Deficit IO Report for July 2019.

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Timely invoicing is dependent upon DSD staff because the monthly customer statements do not create an account receivable in SAP. In the absence of an automated process to create receivables in SAP, staff must research and review deficit accounts to determine invoice amounts and to create an invoice in SAP. According to the Government Finance Officers Association (GFOA), an account receivable should be established for services provided in advance of payment.

**Review of Deficit  
Deposit Accounts  
Performed as Time  
Allows**

DSD staff does not have a systematic process to review, research, and invoice deficit accounts. The process for identifying and reviewing deficit accounts is discretionary, manual, and time consuming. Although staff have access to the DSD Deficit IO Report which provides up-to-date account balances, they review deficit accounts as time allows. Additionally, they must research deficit accounts - an activity that can take considerable time - by reviewing statements, payments and charges to determine which accounts to invoice and what amount to invoice. The research falls primarily into two categories:

1. Deficit accounts that have no activity for three months; and
2. Deficit accounts with some activity in three months, including payments that may not be sufficient to bring the accounts to a positive balance.

Accounts in the first category should be relatively easy to research because of the prolonged absence of activity. Although the SAP report identifies deficit accounts with three months of no activity, we found that as of July 2019, 90 accounts totaling \$378,000 had been in deficit for 12 months and should have been invoiced in October 2018. In total, there are 138 accounts totaling approximately \$462,000 that have been in deficit over three months and should have been invoiced by July 2019 and therefore subject to collection efforts if not paid within the prescribed timeline. The accounts in this category could be reviewed and invoiced monthly.

Research is more complicated for accounts in the second category: staff must review documentation to determine whether these accounts should be invoiced and for how much. We found 95 of 208 accounts totaling nearly \$1 million that had been in deficit from 4 - 12 months and should be invoiced. That activity includes project charges and customer

payments, but the payment did not result in a positive balance.

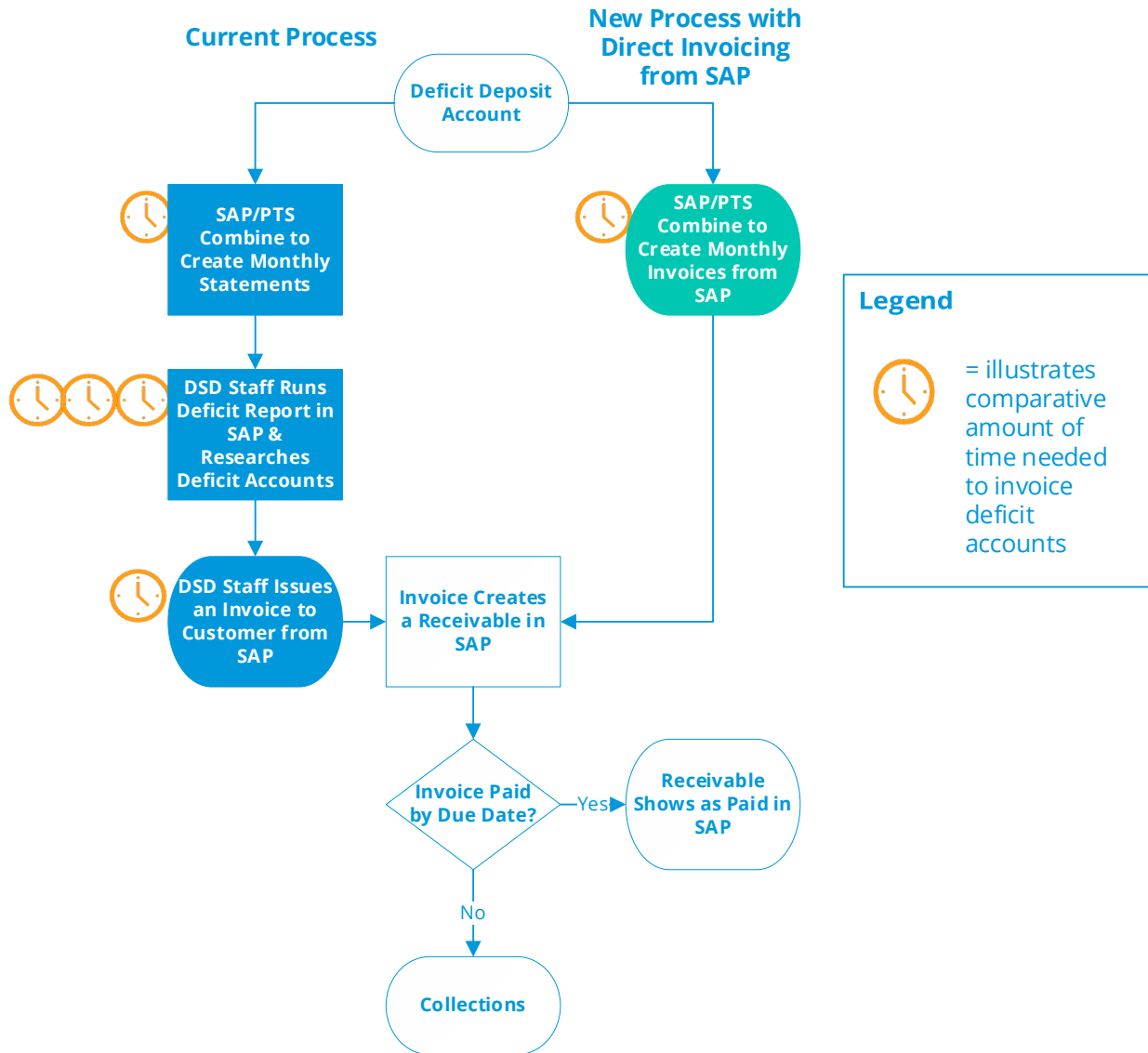
For instance, we found a deposit account that started the year with a surplus amount of approximately \$10,000 and ended the with a deficit of roughly \$25,000. Two payments were made, totaling about \$8,000, but these were not near enough to offset staff charges of approximately \$43,000 posted to the account during the year. Another example of the research and the need for decision-making in this category is an account that began with a deficit of roughly \$2,300, incurred staff charges of approximately \$54,000 and had 6 payments made during the year totaling \$56,000. The account ended the year with a deficit amount of \$522. The account only had a positive balance in two months out of the year and went 8 straight months with a deficit balance. This account could have been invoiced during that 8-month period and is also an example of the City extending credit.

**Direct Invoicing  
through SAP Can  
Simplify the Billing  
Process**

Direct invoicing – invoicing from SAP in lieu of monthly statements - of deficit accounts can simplify the billing and collections process. Currently, as discussed in the background, statements are created using a data merge between SAP and PTS, merging financial transactions with project information, respectively. Invoicing from SAP in lieu of monthly statements will eliminate this data merge process and the need for DSD staff review while also creating a receivable in SAP. Importantly, direct invoicing from SAP will remove discretion from the invoicing process and reduce inequity between how customers are invoiced. Therefore, all customers with deficit balances who do not pay by the cutoff date will be automatically referred to Collections. We provide an example of this process in **Exhibit 11**.

**Exhibit 11:**

**Directly Invoicing Deficit Deposit Accounts from SAP Will Reduce the Time-Consuming Current Process for Invoicing**



Source: OCA based on interviews with DSD staff regarding their invoicing process.

In the near future, DSD anticipates implementation of its new permitting software, Accela. With Accela, the billing process may be simplified and direct invoicing possible. According to a former deputy director, Accela allows for staff to track their labor time in the system. Accela then passes this information to the City's accounting system through an interface. These features in Accela will help the City to create statements (which are invoices) from SAP that contain project information and associated labor charges, effectively eliminating the data merge between PTS and SAP, reducing billing lag time, and creating a receivable in SAP. According to the GFOA, establishing accounts receivable for services in advance payment and establishing terms for collection are key components for effective fiscal administration for the City. Effort should be made to ensure that receivables are collected in a timely fashion. In the City, establishing a receivable in SAP through the initiation of an SAP invoice begins the automatic referral process to Collections. According to SAP's dunning procedure, invoiced accounts are automatically referred to Collections if they remain outstanding after the due date - 30 days for non-government accounts and 90 days for government accounts. Without timely invoicing, the City cannot pursue collections efforts on deficit deposit accounts. Additionally, the absence of formal review of deficit deposit accounts allows the City to extend credit to customers - credit which may go unreimbursed.

**Untimely Invoicing  
Creates Inequity  
Among Customers**

DSD extends credit to customers with deposit accounts in deficit - possibly prohibited by the City Charter. Untimely invoicing creates inequity between customers, some of whom receive more City services than others without payment. In some cases, customers receive continued inspections or issued permits for ministerial and discretionary projects, respectively. For example, in our review of 27 discretionary projects with deposit accounts we found that the City issued permits to 15 projects while their deposit accounts were in deficit. Once permits are issued, the City has little collateral

with which to ensure that it is paid for project costs. Similarly, as discussed in Finding 1, the Public Works Department continues inspections for ministerial projects with deposit accounts, regardless of whether the accounts are in deficit. Therefore, some customers may receive work for project completion, without payment.

**The City has Invoiced and Collected for Deficit Accounts, but Anticipates Losses**

Timely invoicing and referral to Collections is key to recouping amounts due to the City. DSD's lack of timely invoicing has led to a \$4.6 million deficit for deposit accounts with \$3.0 million due and \$1.4 million eligible for invoicing. Cumulatively, since FY10, \$7.3 million has been invoiced with \$4.3 million collected. Of the \$3.0 million balance owed the City, \$1.8 million is over a year past due and all these accounts are in the collections process.

There have been issues with deposit accounts for years and the City anticipates non-payment on many of these accounts as evidenced by an allowance for doubtful accounts currently at \$2.8 million. An allowance for doubtful accounts, sometimes called a bad debt reserve, represents management's estimate of the amount of accounts receivable that will not be paid by customers. An allowance for doubtful accounts is typically used when goods or services are provided on credit. However, according to City Charter, the City does not extend credit.

**Recommendation #8:**

We recommend Development Service Department review current deposit accounts with deficit balances and immediately invoice past due amounts. (Priority 1)

**Recommendation #9:**

We recommend Development Service Department establish written procedures for monthly review and invoicing of deficit deposit accounts that includes criteria for number of months the account has been in deficit and whether to invoice for accounts where payments made have not resulted in a positive balance. (Priority 2)

**Recommendation #10:** We recommend Development Service Department work with the Office of the City Treasurer, Department of Finance, and Department of Information Technology to implement direct invoicing of all deposit accounts through SAP to establish receivables for customers with outstanding balances. (Priority 2)

**Recommendation #11:** We recommend Development Service Department (DSD) automate the information technology controls in project tracking system and/or Accela to stop DSD permit issuance and/or Public Works Department completion of work for projects with deficit balances. (Priority 2)

## Conclusion

The Development Services Department (DSD) recovers costs for complex projects with unpredictable costs through the administration of deposit accounts. Customers make an initial and subsequent deposits to pay for ongoing project costs. Maintaining a minimum required balance (MRB) within the deposit account is critical to ensuring that funds are sufficient to pay for upcoming project charges and to prevent the City of San Diego (City) from extending credit to customers for unpaid services – possibly a violation of the City Charter. Without a sufficient MRB, accounts can quickly go into deficit. In addition, City staff continuing to work on projects with deficit account balances increases the risk that money will go unpaid to the City as deficit amounts increase. There is also the need for timely invoicing of deficit accounts to minimize the risk to the City that services will go unpaid and to increase the collectability of these amounts. Once deficit accounts are invoiced, the Office of the City Treasurer (Treasurer) can pursue collections efforts if not paid in the specified time frame.

We found that DSD does not enforce MRBs for deposit accounts. Specifically, DSD allows project managers discretion to set and change the MRB for discretionary projects with deposit accounts – projects that involve changing land use entitlements. Furthermore, there are no system controls in DSD's project tracking system (PTS) or documentation controls (e.g., supervisory sign-off) governing the setting of the MRB. As a result, deposit accounts for these projects are likely to become deficit.

While project managers oversee discretionary projects with deposit accounts, ministerial projects with deposit accounts are not actively managed, thus increasing the likelihood that these accounts will fall into deficit. We found that MRBs for



these accounts are inaccurate and the Public Works Department's practice of continuing to perform inspections regardless of account balances contributes to the high percentage (64 percent) of these accounts in deficit as of July 2019.

Enforcing the MRB in accordance with policy has several effects. First, it prevents inequity between customers. When two customers with the same project type have to maintain different MRBs, one customer pays more while the other pays less. Second, enforcing the MRB ensures that customers have enough funds to pay for upcoming project charges, thus preventing the City from extending credit. And third, enforcing the MRB mitigates the risk that accounts will become deficit and services that will go unpaid.

DSD project managers are also responsible for stopping work on projects with negative account balances. However, identifying projects with deficit accounts is unreliable due to project managers' inconsistent process and sole responsibility for monitoring deposit account balances. PTS also does not have controls to notify or prevent staff from continuing to work on projects with negative deposit account balances. Therefore, stopping work on projects is contingent upon several manual processes initiated by project managers. As a result, staff continue working on projects with negative deposit account balances. City staff continue working on projects with deficit balances which extends credit and creates greater exposure to loss of unpaid labor costs.

We also found that deficit accounts are not consistently reviewed, researched, and invoiced in a timely manner. As of July 2019, there were 1,384 deposit accounts with deficit balances totaling \$4.6 million. Although \$3.0 million has been invoiced and remains outstanding, we identified another \$1.4 million that should be invoiced immediately. Timely invoicing increases collectability on accounts, ensures that services rendered will be paid, and decreases inequity between

customers. Indeed, we found some cases where the City issued permits to discretionary projects with deposit accounts that were in deficit at the time of permit issuance. In these cases, some customers received permits for which the City may never receive full payment while other customers did not.

To address these issues, we made a total of eleven recommendations to DSD.

## Recommendations

- Recommendation #1:** We recommend Development Services Department establish formal written policies establishing the authority and approvals for setting and changing the minimum required balance in project tracking system or Accela. This policy should describe the project managers roles, responsibilities, level of authority, required documentation and supervisory review and approval. (Priority 2)
- Recommendation #2:** We recommend Development Services Department (DSD) automate minimum required balance (MRB) calculation in project tracking system or Accela. Specifically, the approval types should be tied to specific MRB amounts as set forth in DSD's information bulletins, 502 and 503. (Priority 2)
- Recommendation #3:** We recommend Development Services Department revise Information Bulletin 503 to clearly state that the specific minimum required balance (MRB) amounts for discretionary projects with multiple approval/policy types will be combined to calculate total required MRB. This process should also be automated in project tracking system and/or Accela. (Priority 2)
- Recommendation #4:** We recommend Development Services Department train project managers on the new policy for establishing the authority and approvals for setting and changing the MRB in project tracking system or Accela. (Priority 2)
- Recommendation #5:** We recommend Development Services Department work with the Public Works Department to develop procedures that clearly define roles and responsibilities for setting the MRB in applicable ministerial deposit accounts and stopping work on projects with deficit deposit account balances. (Priority 2)

- Recommendation #6:** We recommend Development Services Department develop policies and procedures to suspend work on projects with a negative balance until a positive balance has been reestablished for projects with deficit deposit accounts. (Priority 2)
- Recommendation #7:** We recommend Development Services Department automate the following information technology controls in project tracking system (PTS) and/or Accela to:
- a. Fix the glitch in the PTS that causes the minimum required balance (MRB) to revert to \$0;
  - b. Calculate the MRB automatically – e.g., tie approvals to the appropriate dollar amounts; and
  - c. Notify staff to stop working on projects with deficit deposit account balances. (Priority 2)
- Recommendation #8:** We recommend Development Service Department review current deposit accounts with deficit balances and immediately invoice past due amounts. (Priority 1)
- Recommendation #9:** We recommend Development Service Department establish written procedures for monthly review and invoicing of deficit deposit accounts that includes criteria for number of months the account has been in deficit and whether to invoice for accounts where payments made have not resulted in a positive balance. (Priority 2)
- Recommendation #10:** We recommend Development Service Department work with the Office of the City Treasurer, Department of Finance, and Department of Information Technology to implement direct invoicing of all deposit accounts through SAP to establish receivables for customers with outstanding balances. (Priority 2)

**Recommendation #11:** We recommend Development Service Department (DSD) automate the information technology controls in project tracking system and/or Accela to stop DSD permit issuance and/or Public Works Department completion of work for projects with deficit balances. (Priority 2)

# Appendix A: Definition of Audit Recommendation Priorities

## DEFINITIONS OF PRIORITY 1, 2, AND 3

### AUDIT RECOMMENDATIONS

The Office of the City Auditor maintains a priority classification scheme for audit recommendations based on the importance of each recommendation to the City, as described in the table below. While the City Auditor is responsible for providing a priority classification for recommendations, it is the City Administration's responsibility to establish a target date to implement each recommendation taking into consideration its priority. The City Auditor requests that target dates be included in the Administration's official response to the audit findings and recommendations.

<b>Priority Class<sup>3</sup></b>	<b>Description</b>
1	Fraud or serious violations are being committed. Significant fiscal and/or equivalent non-fiscal losses are occurring. Costly and/or detrimental operational inefficiencies are taking place. A significant internal control weakness has been identified.
2	The potential for incurring significant fiscal and/or equivalent non-fiscal losses exists. The potential for costly and/or detrimental operational inefficiencies exists. The potential for strengthening or improving internal controls exists.
3	Operation or administrative process will be improved.

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<sup>3</sup>The City Auditor is responsible for assigning audit recommendation priority class numbers. A recommendation which clearly fits the description for more than one priority class shall be assigned the higher priority.

## Appendix B: Objectives, Scope, and Methodology

In accordance with the Office of the City Auditor's Fiscal Year (FY) 2019 Audit Work Plan, we conducted a performance audit of the City of San Diego's (City) Development Services Department's (DSD) administration of deposit accounts. The overall objective of this audit was to determine the efficiency and effectiveness of DSD's billing process for deposit accounts.

To achieve our objectives, we reviewed the sufficiency of DSD's accounting and reconciliation procedures. We also reviewed whether deposit accounts are closed in a timely manner.

The internal controls were evaluated to determine if DSD exercised oversight responsibility, established structure authority and responsibility, enforced accountability, selected and developed control activities, developed controls over technology, used relevant information, and conducted ongoing and/or separate evaluations pertaining to the administration of deposit accounts. Our findings, conclusions and recommendations are included in the audit report.

AUDIT OBJECTIVE	METHOD
<p>Determine if deposit accounts have sufficient project accounting and reconciliation procedures.</p>	<ul style="list-style-type: none"> <li>• Reviewed relevant City and DSD policies and procedures related to the opening of deposit accounts, setting the minimum balances for these accounts, and monitoring deficit accounts.</li> <li>• Interviewed DSD staff about procedures for opening accounts, setting minimum balances, and monitoring deficit accounts.</li> <li>• Interviewed project managers at DSD about their responsibilities for overseeing projects with deposit accounts, including monitoring account balances.</li> <li>• Interviewed Public Works Department (Public Works) staff regarding their oversight of deposit accounts.</li> <li>• Evaluated DSD’s process for stopping work on projects with deficit deposit accounts.</li> <li>• Assessed DSD’s Project Tracking System’s (PTS) controls for setting the minimum balance for deposit accounts and stopping work on projects with deficit accounts.</li> <li>• Reviewed journal entries and cash receipts to determine whether deposit amounts are accurately posted to SAP.</li> <li>• Used data from PTS and DSD deficit reports to quantify minimum required balance (MRB) amounts by project type.</li> <li>• Tabulated MRBs for all deposit accounts by project type to determine number of accounts per \$1,000 increment.</li> <li>• From a population of 208 deposit accounts with ongoing payments or city charges, we reviewed a judgmental sample of 20 projects that were in deficit for twelve months to determine if work continued on projects with deficit balances. We did not extrapolate these results to the entire population of deficit deposit accounts.</li> <li>• From a population of 2,869 deposit accounts, we reviewed a judgmental sample of 475 Ministerial projects created between FY17 - FY19 to determine the number of accounts with a minimum balance of zero dollars. We used this sample to evaluate more recent projects. We did not extrapolate these results to the entire population of deficit deposit accounts.</li> </ul>



Determine if the deposit accounts are closed in a timely manner with any outstanding dollar amounts collected by DSD.

- Reviewed relevant City and DSD policies and procedures for closing deposit accounts.
- Interviewed staff from DSD and the Office of the City Treasurer to determine each department's responsibility in invoicing and closing deposit accounts.
- To ensure that accounts were invoiced in a timely manner, we reviewed deficit accounts not invoiced to determine whether they were invoiced within the department's 3-month time-frame.
- From a population of 226 deficit deposit accounts we reviewed a judgmental sample of 27 discretionary projects created from FY15 - FY17 to determine if their associated projects received permits while in deficit. We did not extrapolate the results.
- Reviewed the applicable accounts receivable reports for invoiced deposit accounts to determine amounts billed/collected.

We conducted this performance audit in accordance with generally accepted government auditing standards. 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 the audit objectives.

## Appendix C: Relevant City of San Diego Criteria

***Overall Relevant  
Criteria***

**City Charter, Section 93, Loans and Advances** states that the City Council may from time to time authorize the advance of moneys in the treasury as a temporary loan to any tax-supported fund, which loan shall be repaid from the first property taxes received thereafter; provided, however, that such temporary loans shall not exceed the current property taxes receivable. It shall be lawful from time to time to advance money in the General Fund to any bond fund or to use any money in the General Fund for any purpose for which a loan shall have been authorized and bonds actually voted but not yet issued and sold, and the City officials need not sell said bonds until it is necessary to repay the General Fund advances or to replenish such loan fund or funds. The credit of the City shall not be given or loaned to or in aid of any individual, association or corporation; except that suitable provision may be made for the aid and support of the poor. (Amendment voted 11-06-1962; effective 01-21-1963.)

***Relevant Criteria for  
Maintaining the  
Minimum Required  
Balance***

**DSD Information Bulletin 503, Fee/Deposit Schedules for Development & Policy Approvals/Permits** states that applicants [for discretionary approvals] are required to maintain a positive minimum balance within that deposit account, and when the balance goes into deficit, City staff are not allowed to work on the project resulting in project delays. See **Exhibit 12** for the initial deposit and subsequent minimum balance amounts for discretionary projects.

**Exhibit 12:**

**Initial Deposit and Subsequent Minimum Balance Amounts for  
Discretionary Approvals**

<b>APPROVAL TYPE</b>	<b>INITIAL DEPOSIT</b>	<b>SUBSEQUENT REVIEW AND MINIMUM BALANCE</b>
Amendment to Prior Discretionary Permit	Same as permit/approval	Same as permit/approval
Coastal Development Permit	\$8,000	\$5,000
Conditional Use Permit	\$8,000	\$5,000
Development Agreement	\$10,000	\$8,000
Easement Vacation	\$6,200	\$3,700
Land Use Plan (new or amendment)	\$12,000	\$8,000
Local Coastal Program (new or amendment)	\$10,000	\$8,000
Map Waiver	\$5,000	\$3,000
Neighborhood Development Permit	\$8,000	\$5,000
Neighborhood Use Permit	\$5,000	\$3,000
Planned Development Permit	\$10,000	\$8,000
Public Right of Way Vacation	\$6,200	\$3,700
Rezone	\$12,000	\$8,000
Site Development Permit	\$8,000	\$5,000
Street Name Change (Process 5)	\$2,500	\$1,200
Tentative Map/Vesting Tentative Map	\$10,000	\$8,000
Variance	\$8,000	\$5,000

Source: DSD Information Bulletin 503, Fee/Deposit Schedules for Development & Policy Approvals/Permits, Table 503B, July 2019.

**DSD Information Bulletin 502, Fee/Deposit Schedules for Grading/Right-of-Way Permits & Mapping Actions, dated July 2019** states DSD collects inspection fees/deposits at the time of permit issuance on behalf of the Public Works Department—the department that performs inspections of public right-of-way permits and most grading permits. The financially responsible party (FRP) will receive a monthly deposit statement reflecting the charges made against the account. The FRP may receive invoices for additional deposits to maintain the subsequent minimum balance. The payment of this invoice will be required to continue inspections of the project. **Exhibit 13** shows the initial deposit and subsequent minimum balance for ministerial projects based on their construction cost estimate.

**Exhibit 13:**

**Initial Deposit and Subsequent Minimum Balance Amounts for Grading/Right-of-Way Permits & Mapping Actions (Ministerial Projects)**

CONSTRUCTION COST ESTIMATE*	INITIAL DEPOSIT	INCREMENT	MINIMUM BALANCE REQUIRED
\$0 to \$15,000	\$1,500		\$700
\$15,001 to \$35,000	\$2,700		\$1,000
\$35,001 to \$50,000	\$3,700		\$1,500
\$50,001 to \$100,000	\$4,800	2% of amount over \$50,000	\$1,800
\$100,001 and over	\$6,000	1% of amount over \$100,000	\$2,100

\*The inspection deposit is established from the approved Construction Cost Estimate of the public right-of-way improvement work, grading, landscape and irrigation and drainage improvements being done. The estimate must be prepared by a registered civil engineer.

Source: DSD Information Bulletin 502, Fee/Deposit Schedules for Grading/Right-of-Way Permits & Mapping Actions, Table 502C, July 2019.

***Relevant Criteria for  
Managing Deposit  
Accounts***

**DSD Policy 9.05, Deposit Account Administration** states that a departmental project manager or lead staff person, for discretionary projects and ministerial projects, respectively, is responsible for checking deposit account balances on a regular basis or during project milestones (e.g., biweekly, during review, prior to hearing, prior to permit issuance, etc.). The project manager or lead staff person is responsible for requesting additional deposits from the FRP to ensure that the deposit account maintains the subsequent minimum balance as outlined in the fee/deposit schedule.

***Relevant Criteria for  
Stopping Work on  
Development Projects  
with Negative Deposit  
Account Balances***

**San Diego Municipal Code, Article 6: Development Permits** states that the development permit application file shall be closed if the applicant fails to submit or resubmit requested materials, information, fees, or deposits 90 calendar days from the date the application was deemed complete or the last written request by the City, whichever is later.

**DSD Policy 9.05, Deposit Account Administration** states that continued work effort by City staff on deposit accounts with a deficit balance is considered “granting credit.” Staff must suspend all work on discretionary and ministerial engineering projects that have negative deposit account balances until a positive balance is reestablished.

**DSD Information Bulletin 503, Fee/Deposit Schedules for Development & Policy Approvals/Permits** states that if the applicant fails to respond to the deposit account statement’s request for additional funds in a timely manner (90 days), the project will be closed and the account will be referred to Office of the City Treasurer’s (Treasurer) Delinquent Accounts Program (Collections).

**DSD Deposit Account Statement** contains the clause that Article VII, Section 93, of the City Charter prohibits the extension of credit by City staff when an account is approaching deficit.

***Relevant Criteria for  
Invoicing Deficit Deposit  
Accounts***

**Administrative Regulation 63.30** states that all City departments involved in the process of billing, invoicing, and collection of monies must issue an invoice to the customer in a timely manner using the correct accounting.

**Process Narrative 0227** states that City departments involved in the process of billing, invoicing, and collection of monies must create an invoice in SAP when monies are owed to the City.

**ONESD (SAP) Collections Referral Specification** states that SAP invoices will automatically be referred to Collections if they remain outstanding after the due date – 30 days for non-government accounts and 90 days for government accounts.

**DSD Policy 9.05, Deposit Account Administration** states that if an account is in deficit prior to or after permit issuance the account must be closed and sent to Collections.

**DSD Policy 9.10, Deposit Account Collection Referrals** states that DSD administrative staff refer deficit accounts to the Treasurer. Administrative staff will identify accounts to be referred, research account information, remove permissions for labor charges, and generate an invoice in SAP.



**THE CITY OF SAN DIEGO**

**M E M O R A N D U M**

**DATE:** February 5, 2020

**TO:** Kyle Elser, Interim City Auditor, Office of the City Auditor

**FROM:** Elyse W. Lowe, Development Services Department Director

**SUBJECT:** Management's Response to the Performance Audit of the Development Services Department Administration of Deposit Accounts

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The purpose of this memorandum is to provide Management's response to the recommendations in the Performance Audit of the Development Services Department (DSD) Administration of Deposit Accounts conducted by the Office of the City Auditor.

DSD would like to take this opportunity to provide a response to the report findings and also present operational updates related information included in the audit report.

During calendar year 2019, Development Services issued approximately 60,000 permits in its mission to ensure quality development of projects. A portion of the work performed by City employees, mostly DSD employees, that charge time to deposit accounts represents less than 10% of revenues generated for DSD as the majority of revenues collected for permitting services are flat fee based<sup>1</sup>.

Upon a recent internal look at balances required on deposit accounts based off discussions with the Office of the City Auditor, it became apparent that the internal policies that set the required balances need to be revised to reflect a positive working solution that provides excellent customer considerations while maintaining appropriate funding levels when providing services to a client on a discretionary permit or engineering ministerial permit. For example, when a discretionary permit is nearing its end of reviews and costs will be lower, the Minimally Required Balance (MRB), should be reduced to reflect a percentage completion of the permit process so that the client is not expected to pay thousands of dollars to comply with a static minimum balance when very little is projected to be expended.

DSD is already evaluating and will revise MRBs designed to adjust when certain milestones of a project are achieved. This will result in full adherence to an internal policy rather than a guide that allows for varied discretion when establishing MRBs and will be included as automated values in Accela, DSD's new permit tracking software program.

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<sup>1</sup> It is important to note that other City Departments charge and derive revenues from these deposit accounts, such as Public Works Department for engineering inspection services.

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February 5, 2020

## **AUDITOR'S RECOMMENDATIONS**

### **Recommendation 1**

Establish formal policies establishing the authority and approvals for setting and changing the MRB in PTS or Accela.

#### **Management Response**

Agree with recommendation.

DSD is will add additional segregation of duties to improve supervisory oversight and internal controls for setting or adjusting the Minimum Required Balance (MRBs) in PTS or Accela. DSD will revise all related Department Instruction (DI) procedures to address the setting and changing of the MRB requirements. These updated procedures will establish approvals by the appointing authority over fiscal operations and remove current roles that allow direct MRB adjustments by non-fiscal operations employees.

#### **Anticipated Completion**

Spring 2020 for Discretionary permits and Fall 2020 for Ministerial Permits, in conjunction with finalization of the Accela Implementation Project

### **Recommendation 2**

Automate MRB calculation in PTS or Accela.

#### **Management Response**

Agree with recommendation.

Implementation of this recommendation will occur along with implementation of DSD's new Accela permit tracking program for discretionary permits in Spring 2020. Accela will be designed to automatically calculate MRBs for projects based on the number of required permits, providing a more accurate and consistent calculation for establishing MRBs.

Currently, PTS does not perform a calculation of the MRBs automatically and are instead calculated manually by Development Project Managers. These manual discretionary calculations will be reviewed and approved by DSD fiscal employees to vet accuracy and consistencies with policies in place while PTS remains in use. DSD does not believe it is feasible to invest in additional programming of automated calculations in PTS while the replacement software, Accela, is scheduled to go into production in the upcoming months.

#### **Anticipated Completion**

Spring 2020 for Discretionary permits and Fall 2020 for Ministerial Permits, in conjunction with finalization of the Accela Implementation Project.

### **Recommendation 3**

Revise current policy to clearly state that the specific MRB amounts for discretionary projects with multiple approval/policy types will be combined to calculate total required MRB.

#### **Management Response**

Agree with recommendation.



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This recommendation will be implemented at the same time as Recommendation No. 1. While DSD's Information Bulletin (IB) 503 contains a table for calculating all deposit amounts, it is implied and not directly stated to do so. The updated IB will address this policy more clearly in that multiple permits are to have a combined value MRB.<sup>2</sup>

**Anticipated Completion**

Spring 2020 for Discretionary permits and Fall 2020 for Ministerial Permits, in conjunction with finalization of the Accela Implementation Project.

**Recommendation 4**

Train project managers on the new policy for establishing the authority and approvals for setting and changing the MRB in PTS or Accela.

**Management Response**

Agree with recommendation.

Once updates and revisions are finalized, employees will be trained on procedures and provide a refresher training every six months. Training will include roles and responsibilities of managing Deposit Accounts for all job classifications (Development Project Managers, Plan Review Specialists, engineers, supervisors, fiscal analysts, etc.) involved in establishing and maintaining these accounts.

**Anticipated Completion**

October 2020

**Recommendation 5**

Work with the Public Works Department to develop procedures that clearly define roles and responsibilities for setting the MRB in applicable ministerial deposit accounts and stopping work on projects with deficit deposit account balances.

**Management Response**

Agree with recommendation.

DSD and PWD will create a new Administrative Regulation regarding Deposit Account Administration of Ministerial Engineering Permits to clarify roles and responsibilities in establishing and maintaining the MRB and procedures for internal control alerts of projects with deposit accounts that are or are projected to be in deficit.

Suspension of work on projects with negative balances require stopping any further work, however, due to the nature of construction, there may be certain circumstances where the immediate suspension of work places the public's safety at risk as determined by the City Engineer. Other circumstances have involved assessing a severe impact to the client's project and reviewing documented field conditions. In that case, a safe stopping point would be determined and maintained until the account funding level is satisfied.

**Anticipated Completion**

October 2020

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<sup>2</sup> MRB's of Deposit Accounts for inspections (per IB 502) are incrementally based upon the estimated construction cost of the project and do not require multiple items to be chosen.

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### **Recommendation 6**

Develop policies and procedures to suspend work on projects with a negative balance until a positive balance has been reestablished for projects with deficit deposit accounts.

#### **Management Response**

Agree with recommendation.

The policies and procedures for the suspension of work on projects with deposit accounts in deficit are documented in DSD's DI manual 9.05 "Deposit Account Administration". DSD will develop a more in-depth process and determine appropriate enforcement of these policies and procedures that will include more direct management-level oversight.

#### **Anticipated Completion**

October 2020

### **Recommendation 7**

Automate the following information technology (IT) controls in PTS and/or Accela to:

- a. Fix the glitch in the PTS that causes the MRB to revert to \$0;
- b. Calculate the MRB automatically; and
- c. Notify staff to stop working on projects with deficit deposit account balances.

#### **Management Response**

Agree with recommendation.

- A. PTS and Accela will be running in parallel as final implementation of Accela is in progress. Upon completion of Accela, PTS will become obsolete. DSD has a procedure allowing for MRBs being maintained in PTS in the event balances are reverted to a \$0 balance performed by fiscal analysts upon creation of a billable Internal Order. DSD has since gone back to all accounts with \$0 MRB values and corrected them in PTS. This will continue to be monitored until PTS closes.

#### **Anticipated Completion**

Completed

- B. Currently, PTS does not perform a calculation of the MRBs and is calculated by Development Project Managers. MRB values will be reviewed by DSD fiscal analysts while PTS remains in use. DSD does not believe it is feasible to invest in additional programming of automated calculations in PTS while the replacement software, Accela, is scheduled to go into production this in the fall of this year.

#### **Anticipated Completion**

PTS- Completed (Segregation of duties applied)

Accela- Spring 2020 for Discretionary permits and Fall 2020 for Ministerial Permits, in conjunction with finalization of the Accela Implementation Project

- C. The Accela permit tracking program, currently under phased development and will replace PTS, will provide an alert automatically on a project when a deposit account balance has gone into deficit or fallen below the MRB. Accela will assign

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an alert placing a condition rule to the project so that no further work, charges, permit issuance, or completion of work can be performed until the deficit has been resolved. The programmed condition in Accela will be based on coded rules driven by the required and actual balance values of the deposit accounts and will not allow for any discretionary manual adjustments.

**Anticipated Completion**

Spring 2020 for Discretionary permits and Fall 2020 for Ministerial Permits, in conjunction with finalization of the Accela Implementation Project

**Recommendation 8**

Review current deposit accounts with deficit balances and immediately invoice past due amounts.

**Management Response**

Agree with recommendation.

DSD has reviewed deposit accounts with negative balances as of September 1, 2019 and invoiced all of them in SAP that same month.

**Anticipated Completion**

Completed

**Recommendation 9**

Establish procedures for monthly review and invoicing of deficit deposit accounts that includes criteria for number of months the account has been in deficit and whether to invoice for accounts where payments made have not resulted in a positive balance.

**Management Response**

Agree with recommendation.

DSD will establish procedures to include monthly reviews by fiscal analysts and develop criteria that includes which accounts have fallen into deficit in the past 30, 60, 90 days. A review of all newly created Deposit Accounts will be conducted by DSD fiscal teams to ensure consistency and compliance of MRBs.

**Anticipated Completion**

July 2020

**Recommendation 10**

Work with Department of Finance, Department of IT and Treasury office to implement direct invoicing of all deposit accounts through SAP to establish receivables for customers with outstanding balances.

**Management Response**

Agree with recommendation.

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DSD will work with the Department of Finance (DoF), Department of IT (DoIT), and Office of the City Treasurer to implement direct invoicing of deposit accounts within SAP so that receivables, and their subsequent payments, and are more easily tracked.

**Anticipated Completion**

September 2020

**Recommendation 11**

Automate the information technology (IT) controls in PTS and/or Accela to stop DSD permit issuance and/or PWD completion of work for projects with deficit balances.

**Management Response**

Agree with recommendation.

DSD recognizes the needs and anticipates implementation of this recommendation in two phases, occurring in conjunction with the related phases of implementation of Accela (Spring 2020 for Phase 2 related to discretionary projects and Fall 2020 for Phase 3 related to ministerial and engineering projects).

**Anticipated Completion**

Spring 2020 for Discretionary permits and Fall 2020 for Ministerial Permits, in conjunction with finalization of the Accela Implementation Project.

If there are any additional questions, please feel free to contact me at 619-446-5423.

Sincerely,



Elyse W. Lowe

Development Services Department Director

cc: Kris Michell, Chief Operating Officer  
Aimee Faucett, Chief of Staff, Office of the Mayor  
Andrea Tevlin, Independent Budget Analyst, Office of the IBA  
Ron Villa, Assistant Chief Operating Officer  
Rolando Charvel, Chief Financial Officer  
Erik Caldwell, Deputy Chief Operating Officer, Smart & Sustainable Communities  
Johnnie Perkins, Deputy Chief Operating Officer, Infrastructure/Public Works  
Elizabeth Correia, City Treasurer  
James Nagelvoort, Director, Public Works Department  
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