



THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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Item Number: 3

Amending Council Policy 700-10 to Implement City Auditor Recommendation Regarding Audit Authority for City Leases

OVERVIEW

City Council Policy 700-10 (Attachment 1), entitled Disposition of City-Owned Real Property, establishes procedures for the management of City-owned real estate. More than half of Council Policy 700-10 is devoted to establishing policies that govern most of the City's property leases. On page 11 of the Policy, Section P addresses audits for City leases specifying that "All percentage leases shall be audited by the City Auditor and Comptroller in the first year of operation to establish proper reporting procedures and at least once every three (3) years thereafter." The Policy was last amended on October 17, 2008.

In Fiscal Year 2008, management restructured/moved the positions responsible for performing revenue compliance audits of City leases, hotels and franchises from the City Auditor and Comptroller Department to the Office of the City Treasurer. The City Treasurer established a Revenue Audit Program (RAP) within her department with these positions. In Fiscal Year 2009, the City Auditor and Comptroller Department was renamed to become the City Comptroller's Department and a separate, independent Office of the City Auditor was established.

The aforementioned restructuring (the creation of an independent Office of the City Auditor) was part of Proposition C, approved by the voters in June of 2008. The reorganization resulted in Council Policy 700-10 referring to a department (City Auditor and Comptroller Department) that ceased to exist in Fiscal Year 2009. The Office of the City Auditor audited lease revenues as part of its comprehensive Citywide Revenue Audit (March 2010) and raised the following question with regard to the City's revenue compliance auditing:

“The question that arises from Council Policy 700-10 is where auditing authority lies now that the City Auditor’s Office and the City Comptroller’s Office are separate entities. Moreover, while lease agreements do not generally state which entity within the City is responsible for auditing the lessee, the Revenue Audit Division does not lie within the City Auditor’s Office or the City Comptroller’s Office.”

In developing its audit recommendations relating to City leases, the City Auditor suggested the IBA work with the Real Estate Assets Department (READ) to revise Policy 700-10 and clarify auditing authority. More specifically, recommendation #16 from the Citywide Revenue Audit indicates:

“The Office of the Independent Budget Analyst (IBA) should work in consultation with the Real Estate Assets Department to revise Council Policy 700-10 to clarify who has the appropriate auditing authority.”

FISCAL/POLICY DISCUSSION

The delay in addressing recommendation #16 was in part the result of ongoing discussion at Council Committees and with the Office of the City Attorney about whether RAP functions are appropriately located in the Office of the City Treasurer or whether they should/could be moved to the Office of the City Auditor. On March 17, 2010, the Budget and Finance Committee requested the IBA analyze considerations surrounding a proposal to transfer RAP to the Office of the City Auditor and report back to the Audit Committee. The Audit Committee also requested this analysis at its meeting on April 12, 2010. In performing the analysis, the IBA discussed the matter extensively with the City Treasurer, City Auditor and the City Attorney’s Office, analyzed RAP revenue recovery data over several years and contacted 11 cities to determine where this function resided in their organizations.

IBA Report #10-39 (Attachment 2) was subsequently presented to the Audit Committee on May 10, 2010. While our research did not identify a single best practice as to where this function should be located, we ultimately concluded:

“The IBA believes that a determination as to where the revenue compliance audit function is located within the organization should be based solely on operating efficiency and effectiveness. The City’s current organizational structure for this function is similar to that of almost all major cities. We would suggest a recommendation to transfer the RAP only be made if the Audit Committee is convinced that the City Auditor can develop and realize significant operating efficiencies that could not otherwise be achieved by the Office of the City Treasurer.”

Our report further recommended that the Audit Committee request an opinion from the Office of the City Attorney regarding any legal implications related to such a transfer. At its meeting on May 10, 2010, the Audit Committee requested analysis from the Office of the City Attorney related to the legality of the City Council transferring the RAP functions from the Office of the City Treasurer to the Office of the City Auditor. On June 10, 2010, the Office of the City

Attorney issued a Memorandum of Law dated June 10, 2010 (within Attachment 3) in response to this matter and presented it to the Audit Committee. With respect to the contemplated transfer of the RAP, the City Attorney's Memorandum of Law concluded:

“The City Council may not legally transfer the functions of the Revenue Audit Division of the City Treasurer (Treasurer) to the City Auditor's Office. San Diego Charter section 45 places an express duty on the Treasurer to maintain a continuous inspection over special revenues she must collect from businesses, in order to effectuate collection of the revenue. The Treasurer meets this Charter duty through the Revenue Audit Division, which conducts periodic inspections of the records of businesses which remit the special revenues to the City, to ensure the revenues remitted are correct. The Treasurer is part of the City's financial management and reporting structure. The collection of revenue is a management function.

The independent City Auditor was established in 2008 by Charter section 39.2. The City Auditor is tasked with auditing City departments and offices to provide the public and City officials with objective, nonpartisan assessment of the stewardship, performance, or cost of the City's policies, programs and operations. To ensure independence from management, the City Auditor reports to the Audit Committee. A transfer to the City Auditor of a management (collection-of-revenue) function, which the Auditor must audit, conflicts with the Charter and Government Auditing Standards' requirements for Auditor independence.”


In 2011, the City Auditor asked the Office of the City Attorney to revisit the analysis contained in its June 10, 2010 Memorandum of Law. The Office of the City Attorney obliged and issued memoranda dated August 12, 2011 (within Attachment 3) and September 15, 2011 (Attachment 3). In the memorandum to the Audit Committee dated September 15, 2011, the Office of the City Attorney provided:

“A few months ago, the Auditor asked us to revisit our 2010 analysis and conclusions in that MOL. In response, we prepared a memorandum dated August 12, 2011, which concluded that our 2010 opinion remained the same. The Revenue Audit Division of the City Treasurer may not be transferred to the City Auditor. However, the memo further provided that the Auditor does have the authority to audit the Revenue Audit Division of the Treasurer's Office.”


CONCLUSION

Considering the recently reaffirmed June 10, 2010 Memorandum of Law and requests from the Real Estate Assets Department to address outstanding Citywide Revenue Audit recommendation #16, the IBA is recommending a simple amendment to Section P of Council Policy 700-10. The proposed amendment (shown in a strikeout/underline format on page 11 of Attachment 1) substitutes "City Treasurer" for "City Auditor and Comptroller". The proposed change addresses Citywide Revenue Audit recommendation #16 and reflects current City practices.

The Real Estate Assets Department has informed the IBA that the rest of Council Policy 700-10 requires no further amendment at this time.



Jeff Kavar
Fiscal & Policy Analyst



APPROVED: Andrea Tevlin
Independent Budget Analyst

Attachments: 1. Council Policy 700-10 (proposed amendment in strikeout/underline format)
2. IBA Report #10-39 dated May 7, 2010
3. Office of the City Attorney Memorandum dated September 15, 2011