CITY OF SAN DIEGO

Independent Accountant's Report on Agreed-Upon Procedures Applied to Wastewater Fund Transfers to Other Funds

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Independent Accountant's Report on Agreed-Upon Procedures
Applied to Wastewater Fund Transfers to Other Funds

We have applied the procedures enumerated below to the City of San Diego's transfers out and interfund charges (including Service Level Agreement charges) paid by the Wastewater Fund for the fiscal year ended June 30, 2003. These procedures, which were agreed to by the City of San Diego were performed solely to assist the City in determining whether or not interfund charges and transfers applied to the Wastewater Fund were in accordance with generally accepted accounting principles.

This engagement to apply agreed-upon procedures was performed in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of the specified users of the report. Consequently, we make no representations regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

The procedures performed and the results of those procedures were as follows:

1. We obtained a summary of expenses by account name for the Wastewater Fund. We identified accounts that were likely to include charges from other funds and transfers to other funds.

   Results: Interfund activities were recorded as either transfers or expenses of the Wastewater Fund. The expense charges can be further broken into Service Level Agreement (SLA) charges and other charges initiated by journal entries. The following summarizes the universe of interfund activities evaluated for the year ended June 30, 2003:

Service Level Agreements – Operating	$13,275,065
Service Level Agreements – Capital	21,575,156
Transfers to Other Funds	2,189,849
General Government Service Allocation	3,395,658
Total	$40,435,728

2. We obtained a list of the transfers out of the Wastewater Fund for the year ended June 30, 2003 totaling $2,189,849. We tested 100% of the transfers to determine whether the transfer resulted in a benefit to the Wastewater Fund and to determine whether the allocation methodology was reasonable in those instances where costs were allocated among various funds of the City.

Results: The transfers tested benefited the Wastewater Fund and were allocated equitably between the funds of the City for $1,761,157 or 80% of the transfers, with the exception of the following:

a. $254,302 Transfer to General Fund: This transfer allocated the cost of the Equal Opportunity Contracting Program. The program pays for compliance, research, and other costs associated with small capital improvement projects allowing an equal opportunity for small construction companies to participate. The Wastewater Fund paid 49% of the project costs for the year ended June 30, 2003. However, City personnel estimate that approximately 5% of these projects were Wastewater Fund projects (based on number of projects since inception of program). The 49% allocation was determined many years ago and has not been adjusted to reflect a more equitable allocation.

   Recommendation: We recommend that the City allocate costs of this program based on the number of participating project from each department. The allocation base should be reevaluated and adjusted annually.

b. $87,353 Transfer to General Fund: This transfer allocated 21.36% of the cost of lobbying contracts. The lobbying costs were allocated to the following City funds that are regularly engaged in lobbying activities: General Fund, Airport Fund, Environmental Services, Wastewater Fund, Development Services, and the Water Fund. The allocation was based on each participating fund's expenditure budget as a percentage of the whole. The allocation does not appear to align the benefits received by each fund with the cost of the program.

   Recommendation: The allocation should be based on specific lobbying activities based on information received from the lobbyist.

c. $73,407 transfer to the Special Training Fund: This was a budgeted transfer for reimbursement of the Career Development & Mentoring Program. Per discussions with City personnel, the program was specifically for "field employees" and is only charged to four enterprise funds (Wastewater, Water, Development Services, and Environmental Services). The four enterprise funds account for 46% of the transfers in to fund the program. These funds appear to have been overcharged for the benefits to the funds with other field employees. Additionally, the share of costs between the four funds does not appear to be supported by the number of field employees in each fund.

   Recommendation: We recommend that the City evaluate the current allocation methodology and modify it to better align with the benefits to the Wastewater Fund.

d. $13,630 Transfer to Special Training Fund: This transfer allocated certain costs of the Equal Employment Opportunity Program. These costs were only funded by six of the City's enterprise funds. The Wastewater Fund paid 37% of the

costs. The allocation does not appear to be reflective of the benefits provided to the Wastewater Fund since employees of non-enterprise funds were not charged for the cost of the program. The program is funded through user charges based on employee attendance at seminars. However, this additional charge (totaling $36,403 for all six enterprise funds), was intended to partially pay for the salary of the Human Resources' Director's assistant who provided training services.

Recommendation: Since the program is already funded through user charges based on employee attendance, additional transfers should not be made to cover other unfunded portions of the program. Instead, the City should change the user rates to cover the costs of the program

3. We obtained a list of all SLA agreements for the year ended June 30, 2003 and selected the three largest agreements for testing (amounting to over 55% of total expenditures for all SLA's). We obtained a copy of the three SLA agreements, met with personnel responsible for development of the SLA, and determined whether the benefit received by the Wastewater Department was sufficient to justify the costs of the SLA's.

Cities utilize fund accounting to track specific functions or activities of the government. It is common for an employee's payroll costs to be charged to multiple funds based on the benefits received by each fund. There are several ways to allocate employee costs to various funds of the City. An employee's costs could be recorded in one fund of the City and a journal entry could be generated to charge another fund a portion of that employee's payroll costs based on an estimate of time spent benefiting the other fund. A more accurate way to allocate employee costs is to have employees keep track of their time on a daily basis and directly charge the benefiting fund based on the employee's timesheet entries.

Results: The City of San Diego utilizes the timesheet method for allocating labor between funds which conforms to the "best practices" method of documentation of allocation of personnel costs. The three SLA agreements selected and the results of our testwork are as follows:

<u>General Services / Facilities Maintenance</u>

Budgeted expenditures -	$1,398,121
Actual expenditures -	2,106,783

The SLA provides fourteen full-time positions to provide preventative maintenance, general repair and maintenance, and improvements as required and necessary for the efficient operation of City facilities and related equipment (elevators, heating, air conditioning systems, boilers, etc.). All of the charges to the Wastewater Fund were based on employee timesheet charges. Employees working on specified projects covered by the SLA tracked actual time spent on the project on their timesheets. The payroll

system allocates a percentage of the employees' payroll costs based on the employee timesheets.

We selected two employees who charged their time through this SLA. We selected a pay period and tested the two employee's time cards. We traced the labor charge under the SLA to the employee time cards.

Recommendation: City documentation policies conform to accepted methodologies. In response to community concerns, we recommend that the Facilities Maintenance Division augment this standard level of documentation with monthly reports describing in detail the benefits provided to the Metropolitan Wastewater Department.

Engineering & Capital Projects / Water & Sewer Design

Budgeted expenditures -	$19,331,769
Actual expenditures -	15,451,134

The purpose of the SLA is to establish collaborative supportive roles of each division for different phases of capital improvement projects including sewer main replacements, trunk sewers, sewer pump stations, and unscheduled accelerated projects. The Water & Sewer Design division provided project management, engineering and design, construction management, and contract support services to the Metropolitan Wastewater Department. The SLA budgeted costs are divided into 72% timesheet driven labor costs and 28% non-labor charges (totaling $5,413,858). The Water & Sewer Design division was 100% reimbursable by the Water and Wastewater SLAs. All costs of the division were allocated to Water and Wastewater based on the percentage of capital expenditures related to the managed projects. For the year ended June 30, 2003, the Wastewater Fund paid 67% of the costs of this division.

The SLA agreement covers the following non-labor costs: training, transportation, workstations, computers, printers, office space, supplies, telephone, mainframe usage, network access, hardware/software purchases, computer maintenance, and San Deigo Data Processing labor charges. When reviewing the types of charges covered by the SLA, we noted that additional expenses were charged that were not specifically covered in the SLA such as the general government indirect cost allocation of approximately $518,000 and legal fees of almost $390,000. While we found no evidence that these costs were inappropriately charged to the Wastewater Fund, these particular cost categories were not specifically set forth in the service level agreement as authorized costs to be charged to the Wastewater Fund.

We selected twenty transactions accounting for over $800,000 of the total non-labor charges for additional testing. Each of these twenty transactions were allowable non-labor costs under the SLA agreement.

We selected four employees who charged their time through this SLA. We selected a pay period and tested the four employee's time cards. We traced the labor charge under the SLA to the employee time cards.

We interviewed two employees who charged their time to the SLA. We inquired with each employee if they were encouraged to overcharge time on their time cards for time spent on Wastewater projects. In each interview, the employee stated that only actual hours spent on each Wastewater project were charged, and that they were unaware of any other employee or department that was encouraged to overcharge Wastewater projects.

Recommendation: City documentation policies conform to accepted methodologies. In response to community concerns, we recommend that the Water & Sewer Design division augment this standard level of documentation with monthly reports describing in detail the benefits provided to the Wastewater Department. The SLA agreement should also be modified to include all allowable non-labor costs that are intended to be charged through the SLA.

Development Services Department

Budgeted expenditures -	$2,511,895
Actual expenditures -	1,558,123

The SLA provides for the coordination of environmental requirements resulting from Wastewater emergencies and urgent repairs, environmental reviews to support Wastewater projects, and ensuring that any new development is meeting the Wastewater design guide minimums. All of the charges to the Wastewater Fund were generated by direct personnel charges.

We selected three employees who charged their time through this SLA. We selected a pay period and tested the three employee's time cards. We traced the labor charge under the SLA to the employee time cards.

We interviewed two employees who charged their time to the SLA. We inquired with each employee if they were encouraged to overcharge time on their time cards for time spent on Wastewater projects. In each interview, the employee stated that only actual hours spent on each Wastewater project were charged, and that they were unaware of any other employee or department that was encouraged to overcharge Wastewater projects.

Recommendation: City documentation policies conform to accepted methodologies. In response to community concerns, we recommend that the Development Services Department augment this standard level of documentation with monthly reports describing in detail the benefits provided to the Wastewater Department.

City Attorney's Office

While the service level agreement between the City Attorney's Office and the Wastewater Fund was not one of the top three service level agreements impacting the Wastewater Fund in 2002-03 (in terms of dollars charged) and therefore was not selected for testing for the purposes of testing charges to the Wastewater Fund, the reader is referred to issues of inaccurate timekeeping practiced by the City Attorney's Office during fiscal 2002-03 that are described further in our report concerning interfund charges to the Water Fund.

4. For other charges to the Wastewater Fund that were neither a Transfer nor a SLA, we selected a sample of transactions and obtained the journal entry for testing. We determined whether the transaction resulted in a benefit to the Wastewater Fund and determined whether the allocation methodology was reasonable in those instances where costs are allocated amongst various funds of the City.

   Results: The City allocates indirect costs of the General Fund to other City Funds through the General Government Services Charge. For the year ended June 30, 2003, the charge to the Wastewater Fund was $3,395,658. The charge is broken into General Fund departments. We selected the largest departmental charges to the Wastewater Fund, Auditor-Comptroller's Office and City Treasurer's Office, and evaluated the allocation base and methodology as noted below.

   Auditor-Comptroller's Office

   The Auditor-Comptroller's indirect costs charged to the Wastewater Fund were $656,718 for the year ended June 30, 2003. We obtained the *Departmental Allocable Costs* report from the accounting system that details the Auditor-Comptroller's costs by department and expense type. This report includes all costs of the Auditor-Comptroller's office. To determine the allocation base, the total of the report is reduced by the SLA charges. The remaining costs not funded through SLA's were totaled and allocated to other City Funds based on each Fund's personnel costs as a percentage of budgeted expenditures, excluding capital expenditures. This methodology is an acceptable practice under generally accepted accounting principles. We recalculated the SLA charges noted on the *Departmental Allocable Costs* report for the Wastewater Fund and agreed them to the SLA charges per the accounting system, without material exception, to test that the Auditor-Comptroller's Office costs were not double charged both through the SLA and the general government services allocation.

   City Treasurer's Office

   The City Treasurer's indirect costs charged to the Wastewater Fund were $521,220 for the year ended June 30, 2003. We obtained the *Departmental Allocable Costs* report from the accounting system that details the City Treasurer's costs by department and expense type. This report includes all costs of the City Treasurer's Office. To determine the allocation base, the total of the report is reduced by the SLA charges. The remaining

costs not funded through SLA's were totaled and allocated to other City Funds based on each Fund's cash receipts as a percentage of total cash receipts. This methodology is an acceptable practice under generally accepted accounting principles. The City Treasurer's Office costs associated with the general government services allocation are not also associated with an SLA.

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We were not engaged to, and did not, perform an audit, the objective of which would be the expression of an opinion on the subject matter. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the use of the City of San Diego, California and is not intended to be and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of the procedures for their purposes.

Mayer Hoffman McCann P.C.

Irvine, California
August 2, 2006