

## **OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT**

**Date Issued:** March 1, 2007

**IBA Report Number:** 07-27

**City Council Docket Date:** March 5, 2007

**Item Number:** 201

**Subject:** Remediation Status Report Number 4 and Related Action.

### **OVERVIEW**

This item includes an informational update on the status of implementation of items on the City's Remediation Plan as well as one action item for the City Council. The Mayor is requesting that the City Council direct the City Attorney to draft an ordinance amending the Municipal Code to modify the Disclosure Practices Working Group (DPWG) in accordance with the City's Remediation Plan.

### **FISCAL/POLICY DISCUSSION**

This Status Report Number 4 shows that much progress has been made on the implementation of the City's Remediation Plan. The Mayor reports that nearly half of the items in the Plan are complete or substantially complete and another two dozen are in-process. This is a significant accomplishment for the short five months since the Plan was presented to the City Council and the IBA applauds the efforts of all staff and elected officials that have moved the City so quickly in this positive direction. The Mayor's Status Report is a thorough and valuable tool in charting this progress.

The IBA has a few comments for the record as well as one recommendation for modification of the DPWG. The IBA is supportive of the efforts to refine the DPWG, but must firmly recommend that both the IBA and the Auditor be ex-officio members of the DPWG, as opposed to voting members. The DPWG is a tool for management to establish and monitor disclosure controls and review documents prepared as part of the City's public disclosure. The IBA is not a part of management and this office should not participate in management decisions. As an ex-officio member, the IBA will be able to offer perspective and expertise where appropriate, but will retain the independence to offer insight to the Council and the public after the DPWG has finalized their work.

Similarly, the Auditor must not serve as a voting member of a group that designs disclosure controls, as articulated by best practices in the industry. As we have reported on many times, it is critical that the Auditor be independent, in both appearance and in fact. Specifically, it is acknowledged that participating in management decision-making may compromise the independence of the Auditor. The Government Accountability Office (GAO) gives the following as an example of personal impairment to auditor independence:

“...responsibility for managing an entity or decision making that could affect operations of the entity or program being audited...”

Both the GAO and SEC agree that auditors may not function in the role of management through making management decisions or performing management functions. Finally, the Institute of Internal Auditors specifically states that “an internal auditor should not develop and install procedures, prepare records, or engage in any other activity which he would normally review and appraise...” Thus, we encourage the City Council to modify the proposed ordinance to ensure that both the IBA and Auditor are ex-officio members of this group in order to retain independence. As an additional note, we encourage the City Council to direct the Attorney to draft this ordinance to refer to the Auditor as the City Auditor & Comptroller, not the Auditor General, since no such position exists in the City at this time.

The IBA also would suggest that, while designees of the COO, CFO, and City Attorney are acceptable to serve on the DPWG, each party should take pains to ensure that the designee for a given project or document review should not have a conflict in serving on the DPWG. For instance, if the item is a Water bond offering, it would not be appropriate for the COO to designate the Water Department Director to serve as her designee at that time.

With respect to other updates provided throughout the informational report, the IBA has the following comments:

This report was finalized and printed on February 21, 2007 and it notes that the City’s Audit Committee is in the process of establishing a written Charter (#20, p. 13). On February 26, the Audit Committee did approve a Charter, as well as Standing Rules for the Municipal Code and a Statement of Operating Principles from the Mayor, and forwarded them to the full City Council for consideration. We would also note that the Audit Committee should in no way be referred to as “temporary” or “interim.” We recognize that a different construction of the Audit Committee may be developed in future years based on a revision to the City Charter and in accordance with the long-term plan the Mayor proposes in his previous reports. However, while the City’s current Audit Committee is a part of the short-term plan to comply with the City’s Remediation Plan, it is not designated as temporary in any rules and, in fact, is permanent unless or until the City Charter is revised, which is not a given. We recommend that the City’s Audit Committee not be referred to as “temporary.”

Finally, with regard to item #87 (p. 14) on developing realistic retirement plan parameters, the IBA suggests that the City Council formally add the IBA's report 06-51 and 06-52 to the list of items that will further this goal and be reported to the SEC as compliance efforts. These two IBA Reports provide information on obligations to the City's current Retirement System and reform measures that must be undertaken as well as significant research, not provided in any other venue in the City, on options for new or revised retirement plans that the City could employ to be fiscally prudent as well as meet the City's recruitment needs. This is exactly what is called for in Item #87 of the Remediation Plan and we believe the City should report these efforts to the SEC as well.

## **CONCLUSION**

The IBA recommends that the City Council approve the report and direct the City Attorney to draft the ordinance as requested, with the following modifications:

1. For the DPWG, make the following modifications to the proposed ordinance:
  - a. References to Auditor General shall be replaced with City Auditor & Comptroller.
  - b. The IBA and City Auditor & Comptroller shall serve as ex-officio members.
  - c. Voting members shall be encouraged to designate staff with no conflict of interest for the particular project.
2. Update the Status Report to reflect actions taken by the Audit Committee on February 26, 2007 to establish a written Charter. Item #20 should be reflected as complete.
3. Strike references to the City's Audit Committee as "temporary" or "interim."
4. For Item #87, on developing a realistic retirement plan, IBA Reports 06-51 and 06-52 shall be reported to the SEC as efforts toward this goal, along with the three other items reported by the Mayor's Office.

The IBA applauds the work of staff and officials in the progress made toward the implementation of the City's Remediation Plan. The collaborative work to execute this plan should be a strong positive signal to the citizens, the financial community and the nation.

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