

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

Date Issued: May 5, 2006

IBA Report Number: 06-20

City Council Agenda Date: May 10, 2006 (Rules Committee)

Item Number: 1-A

Item: Independence of the City Auditor and Comptroller

OVERVIEW:

Under the new Mayor-Council trial form of government, the Mayor is granted the authority to appoint and dismiss the City Auditor and Comptroller. This structure represents a significant change from the prior form of government, when the Auditor and Comptroller was appointed by, and reported to, the City Council. Concerns have been raised about the ability of the Auditor and Comptroller to maintain independence under the current structure. This report discusses several options regarding the appointing authority and reporting relationship of a city auditor.

FISCAL/POLICY DISCUSSION

As discussed in the City Auditor's Annual Report on Internal Controls dated January 1, 2006, the concept of auditor independence is an essential element of both the accounting and auditing professions. The Report states:

The value of the auditor's opinion is rooted in the auditor's *objectivity*. The auditor's objectivity is rooted in the auditor's *independence* within the organization. To the extent that an auditor's opinion is less than objective, the value (and reliability) of that opinion is diminished.

The Report continues:

The concept of 'checks and balances' and the controls inherent therein, are diminished at least perceptively, and often in reality, when the auditor is hired by and reports to the Chief Executive Officer of the organization.

Under the city's prior form of government, the City Manager was the chief executive officer, responsible for the day-to-day operation of the city, while the Auditor and Comptroller was appointed by, and reported to, the city's legislative body – the City Council. Under this form, the Auditor and Comptroller could not be appointed or dismissed by the executive in order to maintain independence.

With the transition to the Mayor-Council form of government, and the concurrent amendments to the City Charter, the office of City Auditor and Comptroller has been transferred to the executive branch. The amended Charter expressly grants the Mayor the authority to appoint and dismiss the Auditor and Comptroller, although appointment is subject to Council approval and dismissal may be appealed to Council. Given the powers of appointment and dismissal accorded to the executive under the current structure, it is presumed that the Auditor and Comptroller reports directly to the Mayor; however, the amended Charter does not expressly state to whom the Auditor and Comptroller is required to report. Despite these structural changes, the functions and responsibilities of the Auditor and Comptroller remain unaltered.

The current structure implemented with the transition to the Mayor-Council form of government has raised concerns pertaining to the independence of the Auditor and Comptroller. The primary concern that has been expressed is that the current structure may subject the Auditor to undue political influence, undermining the objectivity of the Auditor's opinion. Furthermore, an auditor's opinion is effective only if it can be transmitted directly in original form, unfettered by any other source. The current organizational structure raises questions about the viability of unfiltered communication. However, a City Attorney memorandum dated January 23, 2006 opined that the current structure provides "check and balances" by allowing the Auditor to appeal his or her dismissal to the City Council.

The Office of the IBA has performed a survey of other comparable cities across the nation that operate under the Mayor-Council form of governance. The survey results, combined with information acquired from other sources, suggest that the degree of independence accorded an auditor is dependent upon three factors: who has the power of appointment, who has the power of dismissal, and to whom the auditor reports. Under the current structure, all three of these factors are province of the Mayor

Several alternate models that are utilized in these survey cities are discussed below. It should be noted that each of these options would likely require additional amendments to the City Charter. These options are:

1. Make the Auditor and Comptroller an elected position;
2. Appoint the Auditor and Comptroller with a fixed contract for a specified amount of time;
3. Create an Audit Committee that appoints the Auditor and Comptroller, and to whom the Auditor and Comptroller reports.

These options are discussed in greater detail below.

Auditor and Comptroller as an Elected Position

Making the Auditor and Comptroller an elected position would change the appointing authority from the Mayor to the voters. The Auditor would be accountable to the voters, and would hold office for a fixed term. This scenario would likely secure the greatest degree of independence for the Auditor and Comptroller, as he or she could operate objectively without fear of dismissal. Mayor-Council cities such as Los Angeles, Portland, Houston, Oakland and Denver all have an elected city auditor. However, in several of these cases, the elected auditor is more akin to the chief financial officer in that the scope of duties includes Treasury functions such as issuing debt, investing funds, and collecting revenue; as well as management functions such as developing the annual budget. Los Angeles has the most comparable structure, with the duties of the elected auditor being largely similar to those of the Auditor and Comptroller in the City of San Diego.

The downfall of having an elected auditor is that the position could become highly political. The auditor would no longer be solely an administrator but also a politician, beholden to the electorate and any faction therein that exerts substantial influence. In addition, while the auditor certainly would still have to adhere to state and federal laws, governing generally accepted accounting practices (GAAP) and the required duties of a public auditor, being elected often entails establishing an agenda, and may lead to political competition with other elected officials. In addition, it is uncertain whether an elected auditor would possess the same high degree of experience and expertise as that of an appointed auditor.

Fixed-Term Contract

Appointing the Auditor and Comptroller with a fixed-term contract would secure greater independence through the security and longevity of the term. The Auditor and Comptroller would be able to operate objectively without fear of dismissal. In this scenario, appointment could be made by either the Mayor or the City Council; however, the independence gained from a fixed-term contract would be reinforced by requiring the Auditor and Comptroller to report jointly to the Mayor and the City Council. The precedent for this model exists in San Francisco, which has a Mayor-appointed, Council-confirmed auditor that serves for a 10-year term. The Auditor reports to both the Mayor and Board of Supervisors and can be removed for cause by the Mayor and 2/3 vote of the Board.

The downside to this model is that the extended term of appointment could make it difficult to remove an auditor who is not performing. A clear procedure for removal short of the contract term would need to be established. In addition, a somewhat shorter term may be preferable, one that is more on par with other elected officials.

Audit Committee

Another model that could potentially secure greater independence would be to have the Auditor and Comptroller appointed by, and report to, an Audit Committee. The Audit Committee would be composed of several members, all or most of whom would be members of the public possessing sufficient experience and education. This model would not only change the appointment and removal authority, but would also institute greater accountability, as the Audit Committee would also act in an oversight capacity. This process could be made inclusive by having Committee members appointed by both the Mayor and the Council. A similar model exists in Seattle, where the Auditor is appointed by the chair of the City Council Finance Committee and confirmed by the full Council to a six year term of office. The Auditor reports to the Mayor and the City Council's Finance Committee and can be removed for cause by a majority vote of the Council. This model is different in that Seattle's Finance Committee is a Council Committee, which essentially amount to having a Council-appointed Auditor. The Seattle model also incorporates elements of the fixed-contract model, as well as a joint-reporting element.

San Diego Municipal Code provides for a similar audit advisory board. On October 11, 2004, the City Council established the Financial Reporting Oversight Board (FROB) to "serve as an advisory body to the Mayor, City Council and City Manager on matters that relate to achieving a high standard of quality in and efficacy of the City's financial reporting and disclosure practices..." (San Diego Municipal Code, Article 6, Division 17, § 26.1701(a)). The duties of the Board include advising on the "operations of the Office of the City Auditor and Comptroller." According to Municipal Code, this Board was scheduled to assume its duties no later than December 31, 2005, though to date it has not been commenced. While the FROB is currently granted an advisory role pertaining to the city's financial reporting policies, it is feasible that the Municipal Code could be amended to grant the FROB oversight on all of the functions of the Auditor and Comptroller. An option for consideration would be to have the Auditor and Comptroller report directly to the FROB.

QUESTIONS/COMMENTS

The following questions are designed to facilitate discussion regarding the placement of the Auditor function within the broader structure of the City's organization.

Does the current organizational structure provide independence for the Auditor and Comptroller? While concerns have been raised to this effect, it is unclear whether the current structure will actually result in abridgment of the Auditor's independence, or even result in a situation where such abridgment is likely or even possible. Given that this form of government is still relatively new in the City of San Diego, it may be argued that the best course of action is to take a "wait and see" approach.

Does the City Charter and Municipal Code require the Auditor to report jointly to the Mayor and the City Council? It is unclear whether the Auditor has the obligation to report directly to the City Council as well as to the Mayor. Regarding the Auditor and Comptroller, Section 39 of the City Charter states, “He shall submit to the City Manager *and to the Council* at least monthly a summary of revenues and expenses for the preceding accounting period...” (emphasis added). This clause suggests that the Auditor has a duty to report jointly to the executive and the legislative branches, while the Charter amendments that provide for the Mayor-Council form of government do not explicitly state to whom the Auditor reports.

Should the Auditor and Comptroller functions of the current Auditor be separated into different departments? The CFO has suggested that the option of separating the auditing and accounting functions into different departments should be explored. In this scenario, the audit function would attain independent status, while the accounting function would remain in the executive branch. However, there may be reason for both of these functions to secure independence, in which case they may be kept together in a single department. Some cities separate the auditing and accounting functions, while other cities maintain consolidation.

CONCLUSION

In order for the City Auditor and Comptroller to be effective, he or she needs to have an objective opinion, which in turn requires a certain degree of independence. Concerns have been raised regarding the degree to which independence can be secured under the current form of government, which places the Auditor and Comptroller beneath the chief executive. While the IBA agrees that the current organizational structure may not provide sufficient “checks and balances” regarding independence the Auditor and Comptroller, it should be noted that the Mayor-Council form of government was implemented on a trial basis for just this reason – to try it out.

Unless there is a clear, undeniable reason to make significant changes to the City Charter (i.e. if it is shown that the Auditor’s independence is currently being abridged), the IBA recommends deference to the Charter amendments and organizational structure approved by the voters. However, the IBA would support an effort to secure a greater degree of independence for the Auditor and Comptroller if it can be accomplished through minor amendment to the Municipal Code, such as granting the Financial Reporting Oversight Board the oversight capacity for all functions of the Auditor and Comptroller.

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