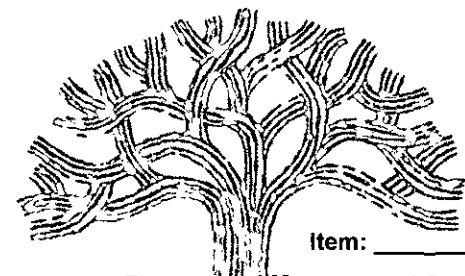


FILED
OFFICE OF THE CITY CLERK
OAKLAND

2009 JUL -9 PM 3: 53

**City of Oakland,
Office of the City Auditor**

**Measure K 2.5% Set-Aside
Performance Audit**



Item: _____

Finance and Management Committee

July 14, 2009

Background

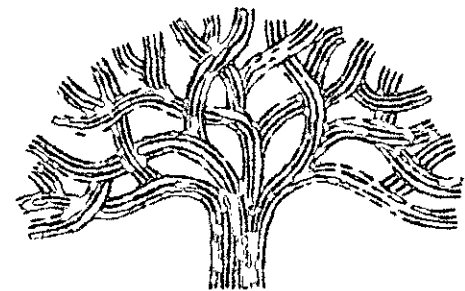
■ Oakland voters passed the Measure K ballot initiative in 1996.

- The City Charter requires the City to annually set aside 2.5% of unrestricted general fund revenues for the KIDS FIRST! Oakland Children's Fund (Kids First Fund or Fund).
- The Fund earns interest income on monies in the Fund.
- Monies set aside for the Fund are to be spent on services for children and youth below 21 years of age.



Audit Objectives

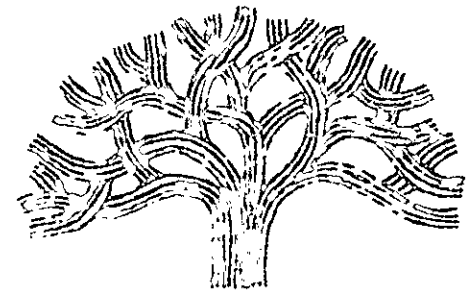
- To determine if the City Administration set aside the correct amount of money for the Kids First Fund:
 - set aside 2.5% of unrestricted general fund revenues
 - credit interest income earned on the monies in the Fund



Audit Scope

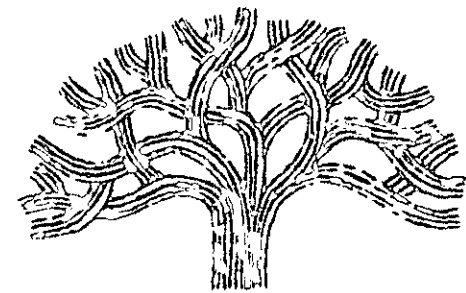
■ We audited:

- the City Administration's calculations of the 2.5% set-aside and allocations of interest income for fiscal years (FYs) 2005-06 and 2006-07; and
- the City Administration's 2006 true-up calculation for fiscal years 1997-98 through 2004-05.



Audit Results

- The audit found that the City:
 - underpaid the Fund by \$398,780 in FYs 2005-06 and 2006-07 as a result of not including certain unrestricted general fund revenues;
 - underpaid the Fund by \$248,640 in the true-up calculation for FYs 1997-98 through 2004-05 as a result of not classifying cable television franchise fees as unrestricted revenues;

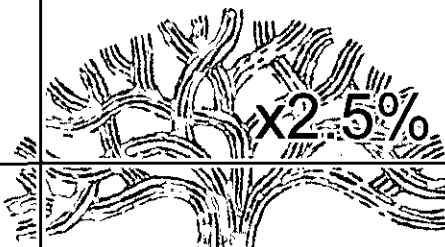


Audit Results (continued)

- The audit also found that the City:
 - lacks a formal policy and procedure for calculating the set-aside and reimbursing either the City or the Fund for any differences between the set-aside based on actual versus budgeted revenue; and
 - allocated interest income to the Fund in accordance with the process the City Administration uses to allocate interest to other City funds.



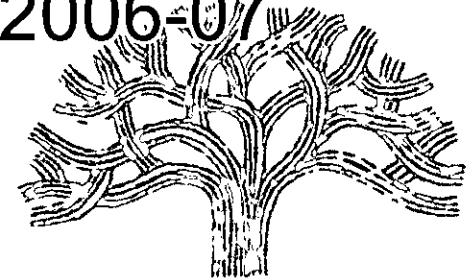
The City Administration's Calculation of the Set-Aside for FYs 2005-06 and 2006-07

	FY 2005-06	FY 2006-07
All General Purpose Fund (GPF) Revenues	\$476,458,416	\$471,416,768
Less: Restricted Revenues	(\$69,344,989)	(\$79,543,142)
Total Unrestricted GPF Revenues	\$407,113,427	\$391,873,626
Multiplied by Set-Aside Percentage	x2.5%	 x2.5%
Amount Due to the Kids First Fund	\$10,177,836	\$9,796,841

The City Administration's Calculation of the Set-Aside for FYs 2005-06 and 2006-07 (continued)

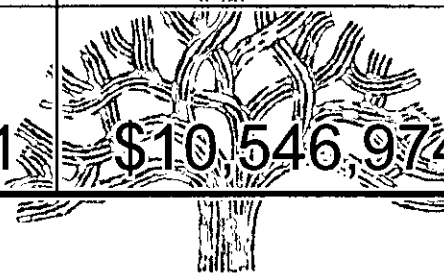
	FY 2005-06	FY 2006-07
Restricted Revenues	69,344,989	\$79,543,142

- Our audit found that:
 - \$5,404,251 of the \$69,344,989 were unrestricted revenues in FY 2005-06
 - \$10,546,974 of the \$79,543,142 were unrestricted revenues in FY 2006-07



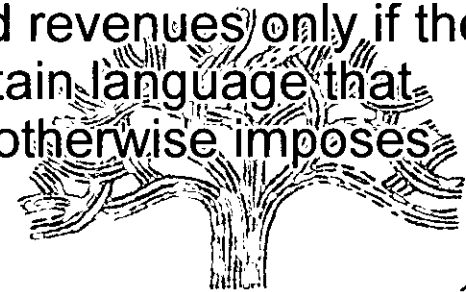
General Fund Revenues Misclassified as Restricted

	FY 2005-06	FY 2006-07
Cable television franchise fees	\$1,701,021	\$1,823,553
Proceeds from the sales of land, buildings and equipment	\$2,647,380	\$7,598,777
Rents	\$1,055,850	\$1,124,644
Total	\$5,404,251	\$10,546,974



City Attorney's opinions

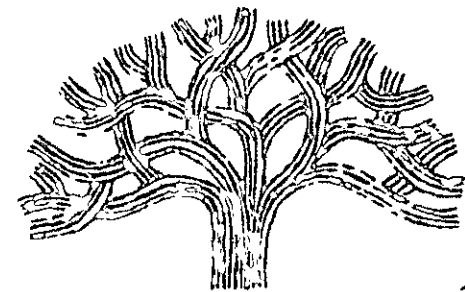
- City Attorney's 1997 opinion
 - Unrestricted general fund revenues are revenues in the general fund subject to appropriation at the discretion of the City Council.
 - Revenues excluded from unrestricted general fund revenues are:
 - revenues from taxes imposed for a special purpose
 - fees for services provided which are based on cost reimbursement
 - other dedicated revenues with restrictions upon their use
- City Attorney's 2006 opinion
 - The City could classify fees as restricted revenues only if the franchise agreements or legislation contain language that limits or restricts the use of the fees, or otherwise imposes restraints on the use of the fees.



General Fund Revenues Misclassified as Restricted (continued)

	FY 2005-06	FY 2006-07
Cable television franchise fees	\$1,701,021	\$1,823,553

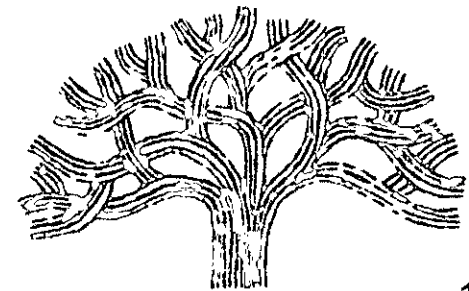
- These amounts represent the portion of cable franchise fees received that are not required to be placed in a separate Telecommunications Account.
- Use of these revenues are unrestricted per the City Attorney's 2006 opinion.



General Fund Revenues Misclassified as Restricted (continued)

	FY 2005-06	FY 2006-07
Proceeds from the sales of land, buildings and equipment	\$2,647,380	\$7,598,777

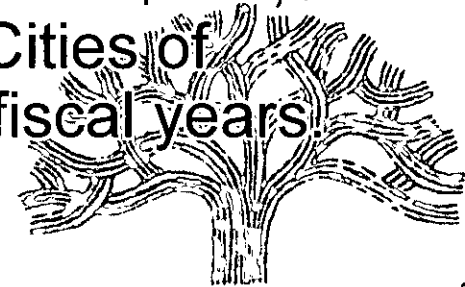
- No restrictions on how the amounts in the table above could be used.
- The City Council had discretion on how these revenues were spent.



General Fund Revenues Misclassified as Restricted (continued)

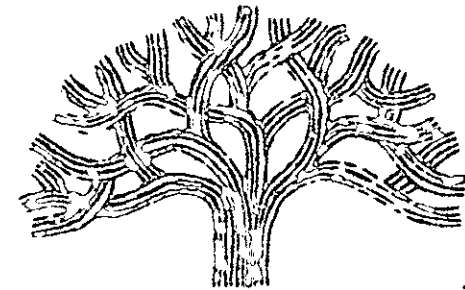
	FY 2005-06	FY 2006-07
Rents	\$1,055,850	\$1,124,644

- No restrictions on how the amounts in the table above could be used.
- Amounts in the table above include rents totaling approximately \$1,009,000 for the four Frank Ogawa Plaza leases we sampled over both fiscal years.
- Amounts in the table above also include \$756,814 in library payments received from the Cities of Emeryville and Piedmont over both fiscal years.



Revised Restricted Revenue Amounts

	FY 2005-06	FY 2006-07
Restricted Revenues per the City Administration	(\$69,344,989)	(\$79,543,142)
Unrestricted Revenues Misclassified as Restricted Revenues	5,404,251	10,546,974
Revised Restricted Revenues	(\$63,940,738)	(\$68,996,168)

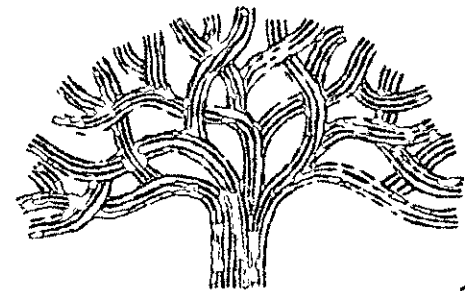


Revised Calculation of the Set-Aside Amounts for FYs 2005-06 and 2006-07

	FY 2005-06	FY 2006-07
All General Purpose Fund Revenues	\$476,458,416	\$471,416,768
Less: Revised Restricted Revenues	(\$63,940,738)	(\$68,996,168)
Total Revised Unrestricted GPF Revenues	\$412,517,678	\$402,420,600
Multiplied by: Set-Aside Percentage	x2.5%	x2.5%
Revised Amount Due to the Kids First Fund	\$10,312,942	\$10,060,515
Less: Amount Due to the Fund per the City Administration	(\$10,177,836)	(\$9,796,841)
Additional Amount Due to the Kids First Fund	\$135,106	\$263,674
Combined Amount Due for Both Fiscal Years		\$398,780

City Administration Needs to Develop and Implement Better Internal Controls

- We found that the City Administration has not established written policies and procedures for calculating the set-aside.



City Administration's 2006 True-Up Calculation

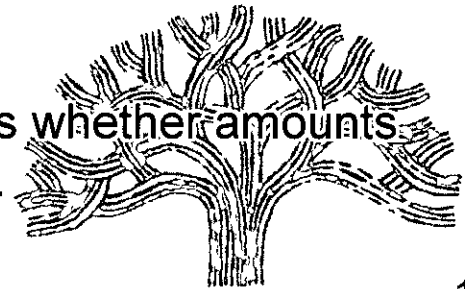
- The true-up calculation corrected the set-aside calculations for fiscal years 1997-98 through 2004-05.
- We found that the City Administration did not classify cable television franchise fees placed in the General Purpose Fund as unrestricted revenues in calculating the true-up.
 - There is no restriction on the use of these revenues per the City Attorney's 2006 opinion.
- The City Auditor's true-up calculation classifies cable television franchise fees as unrestricted revenues.

	Total True-Up Amount for FY 1997-98 through FY 2004-05
City Administrator's True-Up Calculation	\$3,288,032
City Auditor's True-Up Calculation	\$3,536,672
Difference	\$248,640

City Administration Lacks Clear Reimbursement Policy

Fiscal Year	Set-aside based on budgeted revenues	Set-aside based on actual revenues	Amount owed to the Kids First Fund	Amount owed to the General Fund
2005-06	\$9,263,564	\$10,177,836	\$914,272	
2006-07	\$10,058,181	\$9,796,840		\$261,341
Net Total			\$652,931	

- The City Administration lacks a clear policy on when adjustments should be repaid to the respective fund. The General Fund did not reimburse the Kids First Fund for the amount owed after FY 2005-06 and FY 2006-07 until FY 2008-09.
- Previous City Attorney's opinions did not address whether amounts owed to the Kids First Fund should earn interest.



City Administration Correctly Credited Interest Income

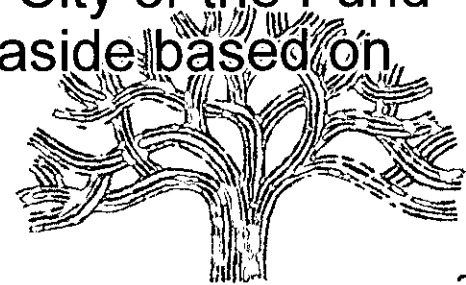
Fiscal Year	Amount Credited to the Kids First Fund
2005-06	\$320,466
2006-07	\$355,745
Total	\$676,211

- City Administration allocated interest to the Kids First Fund in accordance with the process used to allocate interest income to all funds participating in the City's investment pool.



Conclusion

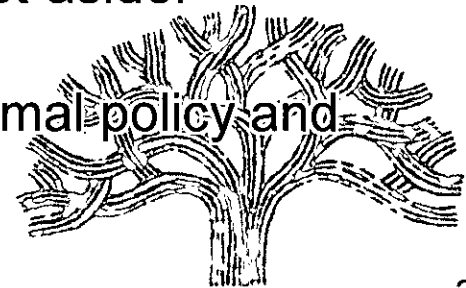
- The audit found that the City:
 - underpaid the Fund by \$398,780 in FYs 2005-06 and 2006-07;
 - underpaid the Fund by \$248,640 in the true-up calculation for FYs 1997-98 through 2004-05; and
 - lacks a formal policy and procedure for calculating the set-aside and reimbursing either the City or the Fund for any differences between the set-aside based on actual versus budgeted revenue.



Recommendations

The City Administration should:

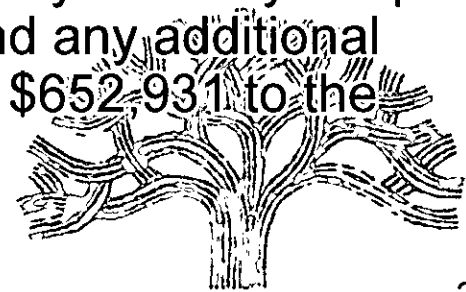
- RECOMMENDATION No. 1: Pay the Kids First Fund \$398,780 to correct the set-aside calculation for fiscal years 2005-06 and 2006-07.
- RECOMMENDATION No. 2: Include the cable television franchise fees in the unrestricted general fund revenue total when calculating the set-aside for fiscal year 2007-08 based on actual revenues. Furthermore, the City Administration should review the revenues from rents and the sales of land, buildings, and equipment to identify those revenues that are unrestricted and include them in the calculation of the set-aside.
- RECOMMENDATION No. 3: Develop a formal policy and procedure for calculating the set-aside.



Recommendations (continued)

The City Administration also should:

- RECOMMENDATION No. 4: Pay the Kids First Fund \$248,640 to correct the true-up calculation for fiscal years 1997-98 through 2004-05.
- RECOMMENDATION No. 5: Develop a written policy and procedure that clarifies when the City Administration should calculate and repay any monies owed to the Fund.
- RECOMMENDATION No. 6: Request the City Attorney to opine on whether the City owes the Kids First Fund any additional interest resulting from the delay in crediting \$652,931 to the Fund.



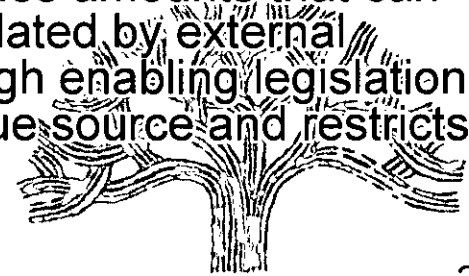
City Administrator's Response

- Concurs with Recommendation Nos. 2, 3, 4, 5, and 6.
- Recommendation No. 1 – Maintains the following were restricted revenues:
 - proceeds from the Oakland Marriott transaction
 - rents received from tenants of building space at Frank Ogawa Plaza
 - payments from Cities of Emeryville and Piedmont for Oakland library services



City Auditor's Response to the City Administrator's Response

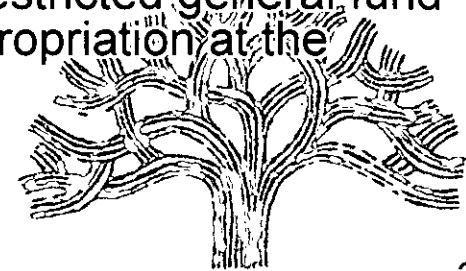
- City Attorney's 1997 opinion
 - Unrestricted general fund revenues are revenues in the general fund subject to appropriation at the discretion of the City Council
 - Revenues excluded from unrestricted general fund revenues are:
 - revenues from taxes imposed for a special purpose
 - fees for services provided which are based on cost reimbursement
 - other dedicated revenues with restrictions upon their use
- City Attorney's 2006 opinion
 - The City could classify fees as restricted revenues only if the franchise agreements or legislation contain language that limits or restricts the use of the fees, or otherwise imposes restraints on the use of the fees
- Governmental Accounting Standards Board, Statement 54
 - States that the restricted fund balance includes amounts that can be spent only for the specific purposes stipulated by external resource providers, constitutionally, or through enabling legislation (that is, legislation that creates a new revenue source and restricts its use).



City Auditor's Response to the City Administrator's Response (continued)

■ \$7.3 million in revenues from the Oakland Marriott transaction

- The City Administrator notes the proceeds were used to pay off debt related to the Marriott property.
- The City deposited these proceeds in the General Purpose Fund and the proceeds were subject to appropriation by the City Council.
- In fact, the City Council funded various projects with the proceeds received from the sale of the City's interest in the Marriott Hotel.
- The City Attorney's 1997 opinion stated unrestricted general fund revenues are those revenues subject to appropriation at the discretion of the City Council.



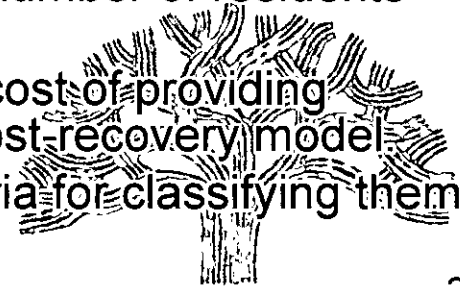
City Auditor's Response to the City Administrator's Response (continued)

- \$1,358,018 in rents received from leasing building space that the City owns in Frank Ogawa Plaza
 - The City Administrator states that rent revenues are restricted because they pay for costs necessary to maintain the building space, related debt service, and other necessary expenses.
 - The City Attorney's 1997 opinion allows fees to be classified as restricted if they are cost-reimbursable.
 - Fees set based on the cost of municipal services are contrasted by charging rents to tenants at Frank Ogawa Plaza.
 - Rents charged at fair-market value are subject to market fluctuations and are not set according to the cost of providing building space maintenance and debt service coverage as a fee would be.
 - We also have not been provided with any documentation that precludes the City Council from using Frank Ogawa Plaza rent revenue at its discretion.



City Auditor's Response to the City Administrator's Response (continued)

- \$756,814 in library service payments from the Cities of Emeryville and Piedmont
 - The City Administrator states that library service revenues should be restricted since it is a fee for providing services to residents of these other cities.
 - Municipal governments set fees based on the cost of providing service, where the fees cannot exceed the cost of providing the service.
 - However, the City negotiated the price of these agreements with the two jurisdictions
 - Emeryville – paid a negotiated fixed amount
 - Piedmont – paid amount based on total number of residents rather than actual use per patron
 - Since these revenues are not based on the cost of providing service, the library payments do not fit the cost-recovery model.
 - Therefore, these revenues do not meet criteria for classifying them as restricted revenues.



City of Oakland, Office of the City Auditor

Measure K 2.5% Set-Aside Performance Audit

Questions

