



Let us

Collaborate to Create Value

For the Great City of Los Angeles and the Angelenos



Table of contents

Let us Collaborate (Our message)2

Overview3

Chapters:

1. The Issue5

2. A Problem or Risk6

3. An Opportunity7

4. How Big is The Opportunity? 12

5. Contributing Factors13

6. Areas for Improvement16

7. It is All About Change19

8. Recommendations 20

9. Conclusion21

Appendices:

1 (a). History of Building and Safety Permit Fund23

1 (b). Building and Safety Fee Increase in 201023

1 (c). Could There be Another Reason for Such Huge Cash?24

2. How the City Does Accounting?25

3. Cost Allocation Plan26

4. What Went Wrong and Why?27

5. How Much is Owed to the General Fund and how was it Calculated?33

6. Other Considerations40



Stakeholders of Los Angeles

Let us Collaborate

As the second largest city in the nation, Los Angeles has a lot to be proud of. A melting pot of diversity, a caring citizenry, a committed leadership, a dedicated team, many opportunities and until last month a booming economy. However, we have our challenges as well. The ability to convert challenges into opportunities hinges on one desire “wish we had more money.”

This report “Collaborate to Create Value” presents hundreds of millions of dollars in much needed money that can be used for various programs and services. This report also identifies a need to change how the City does business, especially when it comes to accounting and budgeting processes. For reasons discussed in this report many of City's accounting and budget processes were established decades ago and need to be transformed to make them more transparent, efficient, effective and responsive to better meet the expectations of staff, customers and decision makers.

As you read through the following pages, you will be tempted, to ask questions such as; how could this happen? Whose fault is it? Why did someone not do anything about this? Even though these may be relevant questions, the primary focus of this report is to analyze the situation, diagnose the problems and recommend options to help the City implement necessary solutions.

Readers will most definitely ask; why should we trust this report and its contents? The short answer is “you should not.” We had no obligation to put in so much time and effort to research, analyze this issue or take unnecessary risks. Our only motivation is the hope that this may help the City and its constituents.

This report merely identifies and presents an opportunity. An opportunity of this magnitude requires careful due diligence, comprehensive analysis and independent evaluation of all potential pros and cons.

The report is therefore inviting all stakeholders to come together and collaborate to analyze, explore, evaluate all options and initiate a process to implement appropriate actions.

No one could have anticipated the current pandemic and its impacts. We are very hopeful that this crisis that has impacted the whole world will soon be a distant memory and the good times, booming economy and hope will return. But these difficult times have created a sense of urgency and the opportunity identified in this report has become even more valuable. We hope the opportunity outlined here will not only allow the City to assist those who need help in these dire times but also give it some options to better deal with the long term impacts of the crisis.

This report is motivated by Controller's passion and vision of improving City's performance. We are thankful to the Controller for his support and confidence in our efforts and to the members of the team **who dare to care to make a difference**, and have influenced this project.

We hope that the City supports an effective and strong collaboration of various stakeholders to promptly implement necessary actions to make the City of Angeles a better and more responsive organization and to make a difference in the lives of those we all have chosen to serve, “**The Angelenos**”.

Respectfully,

Vijay Singhal
Principal Deputy Controller
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Overview



This report starts its journey by identifying that the City's Building and Safety Permit Fund has hundreds of millions in cash, which is the result of substantial annual surpluses that the fund has been generating for years (chapter 1).

This huge accumulation of cash could create a very substantial financial and reputational risk for the City. The risk arises from potential non-compliance with State law (chapter 2).

The report then digs deeper and discovers that the risks may be transformed into a substantial opportunity for the City.

It appears that the opportunity arises out of problems that have been in the making for more than a decade. Even though the Building and Safety Permit Fund was charging customers full cost for providing services it was not paying the General Fund (GF) for all the costs incurred by the GF. This chapter also provides a story to facilitate an understanding of this complex issue.

Upon detailed analysis and research, it was identified that there are opportunities to improve how the City does accounting business. The various accounting and budget processes were established long time ago, many of them are manual and consequently produce inconsistent outcomes.

These processes resulted in the General Fund losing hundreds of millions of dollars that it should have received from the Building and Safety Permit Fund. Further appropriate fiscal oversight would have either prevented the problems from happening or identified them sooner (chapter 3).

The problems of the past have now become an opportunity. The General Fund may be able to recover \$200-\$300 million from the Building and Safety Permit Fund in one-time money and \$20- \$30 million annually. Once recovered this money can be added to General Fund reserves or spent on City programs and services. We are confident that there are many more opportunities that are waiting to be uncovered (chapter 4).

As a public agency we are held to a higher standard of trust, transparency and accountability. We often hear public has the right to know. Such issues also tend to become controversial especially in public domain.

If there is a problem, it needs to be acknowledged and discussed. It is important to understand what happened? What was supposed to happen and why did somethings not happen? Understanding the root cause of the problems is important to not only fix them but to prevent them from happening again.

The report also identifies the factors that contributed to the problems (chapter 5) and areas for improvements (chapter 6).

The City could benefit significantly by changing how it does business, Change is hard but not impossible (chapter 7). Chapter 8 provides some recommendations to facilitate successful outcomes. The conclusion in chapter 9 discusses how the current pandemic has created a sense of urgency and encourages the stakeholders to come together to help the City and its constituents.



The realization that hundreds of millions of dollars were hidden in plain sight, which could have been used for important programs and services, yet were not, could be frustrating and disappointing for many. At the same time to even suggest that processes and practices that have been in place for decades are flawed would be considered preposterous and will be met with great resistance and push back. A conflict between these two environments could derail or stall any efforts to capitalize on this opportunity and will adversely impact any resolution.

The success of this effort depends on an effective collaboration of all stakeholders

While the intention of this report is not to be critical about anything or anyone or point fingers, City cannot claim hundreds of millions of dollars without proving and justifying that it is doing the right thing. Therefore, we have in this report tried to analyze all potential aspects objectively to help stakeholders develop a very good understanding of the root causes of the problems so appropriate measures can be implemented.

We strongly believe that this is **not a people problem**. The problems were with processes and how we do business. It is not the fault of any individual or group of individuals. The problems have been in the making for over a decade and hundreds of people have come and gone in that time. Even if we are able to assign blame on someone, it will not serve any purpose as they are long gone.

City and its stakeholder's interests are best served by looking forward to the future, to the opportunities and by focusing on the outcomes and the value they will create.

We did not anticipate the current pandemic and the havoc it may create. Changing circumstances have created an urgency to release this report so the City leadership can expeditiously evaluate and implement necessary and appropriate measures/actions to help the suffering community and also take proactive steps to better prepare for financial challenges that it is likely to face.

As of yesterday, this report was still a work in progress, and we wish we had time to refine it. We apologize for typos, misspellings and other inconsistencies, but if this work can make even a little difference, we will readily accept any blame and criticism.

The City should bring everyone together to work together and collaborate to make a difference for Los Angeles and its stakeholders.



- Building and Safety Permit Fund had \$346 million in cash (on June 30, 2019)
- In contrast the fund had only \$21 million on July 1, 2011

\$325 million

or

15.5 times

increase in 8 years

2020 (Mar-31) - 400+ Million

2019 - 346 Million

2018 - 299 Million

2017 - 239 Million

2016 - 190 Million

2015 - 151 Million

2014 - 118 Million

2013 - 61 Million

2012 - 35 Million

July-1- 21 Million
2011

Some Financial Stats

Fiscal Year 2012 to 2019

Fund Revenues	\$1.39 Billion
Fund Expenses	\$1.07 Billion
Surplus Generated	316 Million

WOW! This is good?

NO! Los Angeles

We may have a problem

Cash Balance Trend

A Problem or Risk

So, what is the problem?

The City may be in violation of State Law

- This huge cash balance is the result of significant annual surpluses (revenues exceeding expenses) and may suggest that Building and Safety fees exceed costs
- By law the Building and Safety fees should not exceed the estimated costs of providing services
- This would make the City non-compliant with law and expose it to risks

Why do we think the City may have violated a law? (Appendix 1(a))

The Building and Safety Permit Fund (BSPF) was established in 2005 to ensure compliance with the provisions of California Government Code section 66014 (a), which requires that the Building and Safety fees should not exceed the estimated cost of providing services. We discuss in appendix 1(a) History of Building and Safety Fund, why it was created. Appendix 1(b) discusses how Building and Safety fees were updated in 2010.

As discussed in appendix 1(a), the fees do not have to match the costs on an annual basis. The intent of the law is to prevent cities from; imposing excessive fees or using the fees for purposes other than what they were collected for. However it is reasonable to use these fees to offset the impacts of economic downturns by taking shortfalls in one year and offsetting them against surpluses from another year. In an economic downturn such as the one experienced by the City between 2007 and 2012 the revenues declined right away, however, the City had limited ability to reduce costs immediately. Similarly should there be another economic downturn, the City should have some reserves to weather the storm without disrupting operations.

What are reasonable Reserves?

On June 30, 2019, the reserves of Building and Safety and Permit Fund were more than 200% of its annual spending. A cash balance of \$346 million appears to be unreasonable bringing the law into consideration. Given that the General Fund only maintains a reserve of about 6%. A reserve of about 20% for the BSPF should be considered reasonable. City may choose a different percentage or consult with the City Attorney regarding this matter.

Can this money be spent on something else to avoid the risk?

NO! This money can only be used for paying the costs of Building and Safety operations for which the fees were collected

Why should we worry now, no one has found it in the past?

As a public agency it is our responsibility to maintain highest standards of accountability and transparency and do the right thing irrespective of whether someone finds out or not.

A potential unintended consequence: A recent study conducted by University of Berkeley's Terner Center found that high fees imposed by cities contribute to the housing and affordability problem.

While it is not known what impacts if any these fees are causing on affordability of housing or homeless crisis in the City, such large cash balance, these kind of studies, and increasing focus on housing shortages and affordability problems are likely to result in greater scrutiny.

Not doing anything does not serve any purpose. Sooner or later someone is going to ask questions and may challenge the City.

From Risk to an Opportunity

We were not convinced that there is a risk, due to following reasons:

- In 2010 the City increased building and safety fees because they were not enough to recover full costs of building and safety operations appendix 1(b)
- In 2010 City's fees were found to be comparable or lower than other jurisdictions
- The fees have not been increased since 2010 even though the costs of providing services have increased significantly

The questions that bothered us were:

- How could the City then generate so much money?
- How did the City go from not charging enough to charging too much?
- Was the fee increase based on incorrect assumptions and was not warranted?
- Was something else wrong?

To find answers to these questions we dug deeper to challenge the obvious (that the money represents excess fees). We brought a different and outside perspective, conducted extensive research and analysis, combed through almost a decade worth of financial records, documents and information and analyzed millions of bytes of data. ***It appears that our efforts will pay off.***

So, there is another possibility? Yes!

We believe that a substantial portion of the cash belongs to the General Fund and not to the Building and Safety Permit Fund.

Why do we think that the money belongs to the General Fund?

Our analysis reveals that:

- All costs pertaining to the Building and Safety operations were not recorded in the Building and Safety Permit Fund (BSPF) where the fees collected were recorded
- Under City's current processes, most costs such as salary, overtime and benefits such as retirement, medical, workers compensation, utilities and many others are first recorded in the General Fund
- The General Fund is paid back for these costs by the BSPF through complicated manual accounting processes
- For reasons discussed later the BSPF paid the General Fund much lower amounts for these costs than it collected in fees. It kept the rest resulting in huge surpluses and cash balance
- Consequently the General Fund (GF) ended up paying for costs that should have been paid by BSPF. This impacted GF programs and services because the GF was using its own cash to pay for Building and Safety operations, and consequently had less money to use for public programs and services.

If the GF had received every year what was due to it, the BSPF would not have this cash

Could there be another reason for this huge stash of cash?

Yes, it is possible that if the City borrowed hundreds of millions of dollars or it collected hundreds of millions of dollars in advance fees, then that may explain such huge cash balance. However, our review does not support this hypothesis. Additional details on this issue are included in appendix 1 (c)

A Story

The subject matter of this report is a very complex and confusing accounting matter. To facilitate an understanding let us consider a story:

Let us blame it on confusing accounting

The residents of the town of “we care” wanted the town to build a sports complex and agreed to pay for it. The residents approved a ballot measure and agreed to pay a fee or tax to cover the actual costs relating to the sports complex construction, operations and maintenance. The ballot measure required that the fees cannot exceed the actual costs.

The town hired a management company Transparent and Trustworthy LLC. (T&T) to build, run and manage the complex. The town council established the fees that were determined to be sufficient to recover all costs for building, maintaining and running the sports complex including the repayment of principal and interest on bonds issued for construction. The management company produced annual budgets, prepared periodic reports and submitted them to the town council, which were reviewed by staff, council and auditors.

Few years later the residents found out that (T&T) the company, which was running the complex had \$10 million in the bank account over and above what was necessary to maintain operations. The residents were furious, when they learned that the management company had millions of dollars stashed away in a bank. They blamed the town for gouging them and wanted their money back. The town council made a commitment to find out what happened and started an investigation.

The investigation revealed that annually the company was collecting \$10 million in fees and spending only \$8 million thus generating a surplus of \$2 million each year, which over the next five years resulted in the \$10 million bank balance.

Neither the management company nor the town staff had any ulterior motives, except no one asked any questions such as why was there so much money? Where did it come from? What was it for? Why was the company collecting \$10 million each year but only spending \$8 million?

Everyone presumed it was somebody else's job. The budget and financial reports that the town was reviewing and approving were not complete in many ways. The town accountants did not charge the management company for several costs that were paid by the town such as:

- Retirement costs for town employees assigned to manage the sports complex
- Interest and principal on the loan that the town had taken to build the complex
- Utilities that were provided by the town owned utility company
- Cost of town vehicles and computer system used for the sports complex

Once the town realized its mistake it recovered almost all of the ten million, which was used by the town council to support programs and services in the town.

What happened at the City was exactly what is mentioned in the story and we hope this story will help readers develop a better understanding of the complex issues and concepts discussed in this report.

The Opportunity cont.

Earlier on page 7 we mentioned that even though the Building and Safety Permit Fund (BSPF) increased and collected fees to cover full costs it did not pay the General Fund (GF) full costs spent by the GF, just like in the story. This problem caused the GF Fund to lose substantial amounts of money.

Issues like these raise questions about accountability, transparency and trust in government and expect the following questions to be answered:

- Why did it happen?
- How will it be fixed?
- How will it be prevented?

Further one could argue:

- It sounds too good to be true
- It is like a rags to riches fiction
- How can we trust that the opportunity is real?
- How come nobody discovered it before?

These are all very valid concerns and questions. It is therefore important to explain and demonstrate that the arguments or hypothesis being promoted in this report are in fact true and supported by facts and figures.

To prove that the opportunity is real, we will discuss in this chapter and related appendices (2-4), why the GF did not receive the money it deserved and why the problem was not identified until now and will provide information to support what happened or did not happen and why?

Scope and time period covered by this report.

The period covered by this report is Fiscal years (FY) 2011 to 2019. In FY 2012 the City implemented a new financial system and therefore only limited information is readily available for FY 2011. We have used available information and trends for 2012 to arrive at estimates for FY 2011.

Problem with City's processes

Our review and analysis reveal that the City's budget and accounting processes did not deliver on the expectations of accuracy, accountability and transparency. For reasons discussed in chapter 5, (contributing factors); loss of knowledge and lack of resources caused these processes to become inefficient, ineffective and outdated. They produced inaccurate outcomes and lacked sufficient oversight and monitoring to prevent the problems or identify them in a timely manner (note1).

To fully comprehend the scope, reason and impacts of the problem it is important to develop an understanding of these processes, what role they played or failed to play and what errors and mistakes were caused. This chapter discusses the following issues:

1. How the City does accounting?
2. City's Cost Allocation Plan
3. City's Budget Process
4. Process of maintaining fiscal oversight
5. What impacts did these deficiencies create?

The following pages provide a brief summary of each process with details included in referenced appendices at the end of this report.

Note 1.

It is important to note that City has many very good and outstanding processes and functions and, the City and its staff do a very good job. The comments regarding processes are not intended to take away from this fact.

The comments are only with respect to this matter regarding Building and Safety operations and do not pertain to the budget, CAP and accounting or other processes as a whole.

The Opportunity cont.

1. How the City does accounting? (appendix 2)

The Building and Safety revenues and expenses are accounted for in different places, majority of revenues are recorded in the Building and Safety Permit Fund (BSPF). However, majority of costs are first spent from and recorded in the General Fund and later transferred or allocated to the BSPF using complex and manual processes, many of which are performed offline outside of City's financial system. Because of manual nature these processes are not consistent, are error prone and create risks of inaccuracies.

Details regarding City's accounting processes and practices are included in **appendix 2**.

2. Cost Allocation Plan (CAP) (appendix 3)

The full or total cost of a program, service or product should include all costs. Costs incurred by an organization can be grouped into two main categories (i) direct costs, which are easily identifiable with the product, program or service, for example the cost of iPhone that Apple pays to the manufacturer and (ii) indirect costs that include all other costs relating to an iPhone such as research development, cost of marketing, showrooms, support, after sales services, accounting etc. that cannot be easily identified with each iPhone.

CAP is a process to estimate and determine the amount of indirect costs that should be allocated to programs, services and products. The City's current CAP process resulted in lower than required recovery of General Fund indirect costs. Details regarding City's CAP process are included in appendix 3.

3. City's Budget Process

An organization's budget is a policy document. It establishes expectations and standards for performance, if these standards or expectations are incorrect then the actual performance may also be impacted.

The annual budgets determined how much money the Building and Safety Permit Fund was supposed to pay to the General Fund for indirect costs (referred to as reimbursement of General Fund costs in the budget).

As discussed in appendix 4 (page 31) the amounts included in the annual budget were not based on annual CAP rates but instead on some unknown basis, which appears to be inconsistent and resulted in significantly lower amounts being paid to the GF than required. The (BSPF) paid to the GF, the lower amounts that the budget told it to. There was no review or audit and the problems persisted costing the GF all this money.

4. Process to maintain fiscal oversight

Every organization needs processes to provide appropriate fiscal oversight and monitoring. Failure to do so results in errors, mistakes and incorrect information.

Effective fiscal analysis and monitoring processes help identify anomalies and unusual trends and prompt questions to identify and prevent problems.

The City's fiscal oversight, analysis and monitoring processes were not effective in identifying the problems or to stop or prevent them.

The Opportunity cont.

5. What impacts did the deficiencies in these processes cause? (appendix 4)

Following are the reasons, why the GF did not get paid for all the costs it had spent for Building and Safety operations. Each item is discussed in detail in appendix 4.

- a. All direct costs relating to the Building and Safety operations recorded in the General Fund were not allocated to the BSPF
- b. The CAP rates applied were lower than required
- c. CAP rates were applied to a smaller base
- d. The CAP rates as calculated were not appropriate for the purposes of calculating indirect costs for the Building and Safety operations
- e. The annual budgets established much lower amounts for indirect costs than the General Fund should have recovered
- f. There was not enough oversight, monitoring and analysis, which prevented the problem from being discovered

Chapter Summary:

- **The General Fund has an opportunity to recover substantial amounts of money from the Building and Safety Permit Fund**
- **The reason for this opportunity is that City's accounting, CAP and budget processes caused the GF to not recover all the costs it had spent for Building and Safety operations.**
- **The details are included in appendices:**
 - Appendix 2-How the City does Accounting**
 - Appendix 3-Cost Allocation Plan**
 - Appendix 4-What went wrong and why?**

Warning:

Very complex and confusing turns ahead:

In appendices 2-4 related to this chapter and appendix 5 under chapter 4, we discuss some very complex, complicated and confusing accounting concepts,

This report is not an audit and the objective of the report is not to promote one view, hypothesis or to present conclusions. The report simply identifies and opportunity for City's consideration.

This report should be viewed as a guide or diagnostic tool. The primary intent of this report is to evaluate the problem, analyze symptoms, conduct testing, identify potential causes of the problem and provide options and recommendations including a framework that the City can use to calculate the amount that should be paid to the General Fund.

If the City finds merit in the subject matter of the report then the City should allocate resources and engage independent subject matter experts to verify and validate the report, its approach, methodology, assumptions and numbers to determine appropriate actions if any.

How Big is the Opportunity?

So how much money are we talking about?

Table 2 on page 39 of this report shows an estimated amount of \$290 million that may be available to the General Fund in one-time money for the past nine fiscal years (FY 2011 to 2019) including interest. However, there are several factors and policy issues as discussed in appendix 5 and 6 that may impact the exact amount available. Some may increase the amount, some may decrease it.

The final amount available to the General Fund will depend on the validation and resolution of all issues discussed in this report. We are confident that the final amount owed to the General Fund would be in the range of \$200-\$300 million. We also estimate that the General Fund could get between \$20 to \$25 million annually, if not more.

Details of our methodology, approach, calculations are provided in appendix 5. A review of the information provided in appendix will reveal that it is a very complex issue. Further because of manual and offline processes some relevant information is not readily available. Due to this reason and limited resources we had to use some estimates and assumptions but we were conservative in our estimates.

We are confident that except issues identified in appendix 6 the final amount would not change significantly. Our methodology returned a higher amount but to be conservative we rounded it down by \$10 million to arrive at \$290 million.

Our estimate was arrived by using the alternate methodology and alternate CAP rates as discussed in appendix 5. This amount is made up of two components; (1) amount available in respective fiscal years and (2) amount to be recovered from other years.

Due to the recession in 2007, the Building and Safety revenues declined significantly however, the City had to maintain operations and the General Fund was spending money every year on Building and Safety operations. Due to lower revenues there is not enough money in fiscal years 2011 to 2013 to recover the entire amount owed to the GF. There is about \$57 million, which should be recovered from the surpluses in the future years as discussed in chapter 2 and appendix 1(a), The City may want to confer with the City Attorney's Office in this regard. Based on table-2, even if recovery of this \$57 million is deferred, \$233 million is still available.

We hope that, these estimates will confirm that the opportunity is real and substantial and the City finds the analysis and framework useful to determine the amount owed to the General Fund and to make appropriate decisions.

The General Fund has an opportunity to obtain \$200-\$300 million in onetime money

The General Fund can also benefit to the tune of \$20-\$30 million annually

Contributing Factors

From the preceding discussion, four main questions emerge:

1. Why did this happen?
2. Why did it stay undetected?
3. What can be done to prevent this from happening again?
4. Are there opportunities that we do not know about?

In this chapter we will discuss the first two which will provide the reasons that caused the various accounting processes to not deliver the expected outcomes and why the resulting problems were never identified? The other two will be discussed in the next chapter, areas for improvement.

Following are the major factors that contributed to the problems. These are the root causes why the various processes got out of sync, delivered incorrect outcomes and why the problem was never identified?



Complex and decentralized structure and processes



Loss of Knowledge and subject matter expertise and lack of staff training



No one asked the questions

These factors created an environment that inhibited, engagement, empowerment, ownership and transparency, resulted in stifling creativity and innovation and promoted a culture of “this is how we have always done it”. “Just do it as was done in the past”. Each of these factors are discussed in the following pages

Contributing Factors cont.

1. Complex and decentralized structure and Processes

The City is a very large, organization, with complex and very diverse lines of business. City's accounting processes are complex, complicated, decentralized and many are manual and were established decades ago based on tools and expectations available at that time.

A quick glance at City's financial documents and reports would reveal that even though the outside world has evolved into something totally unrecognizable these documents and processes have not changed in the past 15-20 years. They have the same format, provide same type of information and take too much effort and time (several months in many cases) to prepare. Any changes and updates need to be made manually, and take a long time. Fiscal monitoring is very sporadic, complex and manual as well. The documents have too much detail and redundant information and not much of relevant information to facilitate effective decision making.

Unlike most other organizations private or public the City does not have a centralized accounting function or oversight. There is no one office, department or person responsible for maintaining oversight on overall fiscal performance. For example, CAO's team prepares the budget, money is collected by Finance and/or departments, departments spend the money, Controller pays the bills, CAO is supposed to maintain budgetary oversight. Everyone does what they have been doing for a long time and how they have done it, with no one looking over the whole.

Further City's organization is also quite bureaucratic, stifles creativity and innovation. Resources for improvements are hard to come by. The City could benefit from greater trust and engagement.

For example, the budget process is controlled by CAO team. Due to limited staffing and too many things to do there is not much focus on long term financial planning, fiscal analysis or oversight.

Due to complexity of processes, and need to get things done with limited resources, the general perception is that the process is not collaborative and transparent and decisions are made in isolation with not much regard to the departmental business needs and performance.

Generally, one size fits all policies and directives, inhibit creativity. Departments rush to fill positions and spend money fearful of the fact that if they don't use it, they will lose it, which results in waste and lack of trust to the detriment of the City.

The current environment, culture and structure dilutes consistency, ownership, transparency, accountability, trust, engagement and oversight, and adversely impacts performance, outcomes and quality and reliability of financial decision making.

Question?

Do we have processes that would provide necessary budgetary and fiscal oversight or is there a need to improve them?

Do current processes ensure responsible and responsive fiscal decision making?

Do we have effective and efficient long-term budgeting, financial planning, analysis and reporting processes which serve as guides, standards and controls to preserve and maintain effectiveness of these functions and guide the City in the long term?

Is there a need to implement sophisticated and more robust processes and oversight functions?

Contributing Factors cont.

2. Loss of Knowledge and Expertise and Lack of Training

During recession the City lost many experienced staff members, resulting in loss of decades of institutional knowledge and experience, which adversely impacted City's performance in many areas. The remaining people performed the various tasks how they were told to do or how they believed it should be done.

The critical component or knowledge of why it is being done? And why it is done this way was lost? This is how we have done it gained preponderance inhibiting change and improvement. Additionally, due to hiring freeze the departments had to contend with fewer resources. Further because of fiscal constraints the training budgets were eliminated.

Not only the City lost knowledge, had fewer resources but was not able to train the remaining staff to develop necessary knowledge and subject matter expertise. The fewer remaining staff had too much to deal with. Staff had to figure out a way to manage workload with outdated processes and complex systems forcing them to just get things done (just get the budget out, just get the report out, just get the MOU's approved) with no time for qualitative or analytical aspects to fully comprehend the long term impacts of financial decisions or to explore options for improvements.

Good long term fiscal performance depends on effective fiscal stewardship. The City needs to develop expertise in areas such as budgeting, financial analysis, long term financial planning and might explore bringing relevant skills from outside to train its team.

Question?

How well does the City's structure and culture help it develop its team members and enable and empower them to take ownership and initiative to change what needs to be changed?

3. Why was the problem not discovered until now?

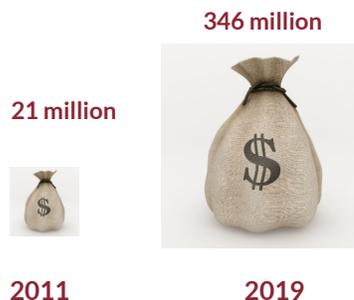
No one asked any questions

Asking the right and relevant questions is important. Subject matter expertise and sophisticated processes help organizations appropriately measure and evaluate financial performance by analyzing trends, comparing actual performance with expectations and prompting questions. No one asked the right questions.

\$300+ million fund balance

No Questions asked

Unreasonable Cash Growth



No Questions asked

The Building and Safety Permit Fund was accumulating cash at a significant rate. Following questions should have been asked:

- Why is there so much money?
- Why is it growing so much?
- What will it be spent on?
- When will it be spent?

Just asking WHY? Would have identified the problem

Subject matter experts would have asked questions
Sophisticated processes would have prompted why?

We asked why?

Hence this opportunity.

Areas for Improvement cont.

What can be done to prevent this from happening again?

Following areas will offer significant opportunities



Leverage
Technology
to improve
performance



Hire the right
skills and
talent



More
effectively
manage
generational
challenges
and
opportunities



Simplify,
streamline,
automate
and improve
current
processes

1. Leverage Technology to improve performance

Today, customer and constituent expectations have changed, we now live in an age of instant gratification especially when it comes to information.

In the last decade, quite inexpensive and efficient technologies have become available to simplify and automate complex repetitive tasks, provide information in an expeditious and simple manner while also improving oversight and performance. Today when one can access any information on their mobile devices anytime anywhere, the City still operates in a very different world.

Many of our financial processes are antiquated. It takes several months to prepare and update financial documents such as budget and financial reports.

The processes to obtain information necessary for effective decision making are overly complex, staff has to use manual and offline processes to compile, verify and present information. Many of the processes involve manually getting data from different systems, putting it in offline databases or spreadsheets, a rather complex, tedious, time consuming and error prone undertaking, which takes a long time and the information is outdated even before it comes out.

In a world of data driven decision making with real time information, the City has a long way to go. The City could benefit both operationally and financially through a digital transformation.

Don't take our word for it!

We recommend that the City conduct a survey of its team members and just look around to see how others are using technology to change how they do business.

We are confident that the results would be eye opening.

Questions?

Are we happy with where we are?
Should the City explore and implement technological solutions to improve its performance, be at the leading edge and bring its processes into the 21st century?

As the second largest City in the country, are we the leaders? If not isn't it time we try to be?

Areas for Improvement_{cont.}

2. Hire the right skills and talent

Highly restrictive budget and hiring practices continue to stifle initiative, growth and progress. Today technology intensive skills and jobs such as data analysts, data scientists, application and AI developers are the top sought after skills by high performing organizations. City's job classifications were developed decades ago and have not kept pace with the changing business needs and customer expectations and severely limit City's ability to hire necessary skills to perform much needed tasks and jobs in the current business environment.

Compared to the thousands of employees that the City has in accounting and administrative classifications there are very few data analysts and financial analysts.

The City has very good people, however, it has not really invested in either acquiring current skills or in training existing staff.

As a multi-billion dollar organization, serving millions of customers, we need to complement our existing team with talent and skills necessary to move the City forward.

Question?

Does the City have the right skills and talent to operate in the 21st century?

Do our job classifications and positions represent the current needs and environment?

If not then what should we do? Do we need to reevaluate and realign our priorities and practices with the expectations?

3. More effectively manage generational challenges and opportunities

The City is also at the crossroads of generational transformation of its workforce.

The City is bringing millennials into its workforce and they seem to be driven by different motivations, they are more technology savvy and more open to changing everything that appears to be at odds with their perceptions and expectations. They are more likely to challenge status quo, bureaucracy and how we do business. They do not really have much patience for slow and manual ways of doing business,

The City has many good and dedicated staff who have been here for a long time. They take great pride in what they do. However, their perception of what should be done and how it should be done is many times at odds with the expectations of the new generation.

However, in the current environment the boss (the past) often prevails. Being forced to do as the boss wants, which many times is not the best way is disheartening to the future generations. City Offices that have successfully integrated the new generation have demonstrated outstanding successes in many areas.

Capitalizing on the maturity of seasoned workforce with the enthusiasm of millennials and greater integration of the new generation in the decision-making process will yield surprising outcomes.

Question?

How do we develop a structure, culture and team for the future? Is there a need to promote better cross generational understanding and integration?

Should we evaluate our structure? Is the current vertical hierarchical structure with future at the bottom what we want or should we start transitioning towards a more tech- team culture?

Areas for Improvement cont.

4. Processes that could use some help

Based on preceding discussion it appears that the City may need to reevaluate, reassess, reform, re-engineer and improve many things including:

- Accounting, Budget and CAP process
- Fiscal oversight, monitoring and financial analysis processes
- Financial planning including long term planning process
- Internal controls over internal financial processes
- Investment in staff training and development
- Building a team for the future through improved hiring retention and succession planning process
- Implementing sophisticated management information systems and dynamic tools that can provide relevant and useful information in real time to facilitate prompt and effective decision making
- Embrace and implement new emerging technologies to improve performance

An investment in these processes will not only improve performance but also save the City substantial amounts of money, which the City desperately needs and would yield a very high return on investment.

Are there additional opportunities?

Yes Absolutely!

We estimate that in the past decade the General Fund has lost hundreds of millions of dollars in addition to the subject matter of this report due to the problems discussed in this report. We believe that the GF can still recover some of that money and generate \$20-\$30 million annually in the future if not more.

The issues and challenges discussed earlier had a much widespread impact and created a perfect storm that has buried numerous other opportunities that are waiting to be discovered.

It is all about Change



Need for Change

The City is a very large and complex organization, and it operates in a certain way that has not changed or evolved with time. City (who is the City?) may want to ask itself the question; is there a need to evaluate how the City does business and implement necessary improvements?

What to Change?

There is a lot that would need to be re-aligned with priorities. The City should evaluate where it wants to start and what it wants to do differently? Developing a strong and engaged team and leveraging technology should be the easiest ones to implement.

How to Change? .

When the City has determined that it needs to do things differently, it will find that change is very hard, changing so many things, is very daunting and might even be considered impossible or may take years or even decades.

A well thought out change initiative, which is; gradual and incremental, promotes ownership and initiative, is supported by leadership and engages the team is likely to generate greater buy-in and eventually deliver desired outcomes.

Change is difficult but not impossible.

We believe that change may not be as difficult as it may appear. Our observations and recommendations are not just our opinion, their foundation is based on what has already been accomplished in the City.

There are people in the City who have changed many things for the better, created outstanding opportunities. Our small team has also made significant strides in changing how we do business. Their passion and commitment to make a difference has enabled them to disrupt status quo and implement innovative solutions and new approach to decision making. Better use of technology has resulted in; greater oversight and accountability, improved access to information, efficiencies, substantial cost savings, improved performance and a customer centric culture that creates much greater value for the City.

Did we face resistance and push-back? Absolutely and some projects took 3-4 years, but we were able to establish strong collaborations and partnerships to move things forward.

The City as a whole is more resourceful and has many more committed and dedicated team members. We are very confident that by embracing an entrepreneurial mindset, appropriate support and resources and right skills and encouragement, the City can create success on a large scale. These efforts will transform the City into an agile and high performing organization where such problems will not happen and even if some slip through will be detected promptly.

Recommendations

Whether something should be done or not? What should be done? How it should be done? When it should be done are all policy decisions to be made by the City leadership? Here are some recommendations for consideration, which we hope will facilitate an expeditious action to capitalize on this tremendous opportunity:

- Confer with the City attorney regarding any legal issues
- Invest appropriate resources, engage outside subject matter experts and expeditiously investigate this issue and confirm, verify, validate or disprove the assertions made in this report
- If the City sees merit in this report, consider transferring \$200-\$250 million as the City deems appropriate into a holding account (Fund), pending research and analysis
- Based on the outcome develop a strategy and plan to use this money for appropriate projects, programs and services
- Explore, discuss, evaluate, strategize, plan and implement appropriate actions to improve various City processes
- Simplify City's current manual, offline, and paper-based processes, invest in new technologies to automate them and implement more robust processes to improve fiscal oversight, monitoring and financial planning
- Invest in staff training and succession planning initiatives (not just a plan)
- Acquire the right skills and talent
- Allocate resources to help our team continue our work to identify additional opportunities



Conclusion

The General Fund has an opportunity to obtain \$200-\$300 million.

The issue discussed in this report is a very complex issue that has been in the making for a very long time and may sound too good to be true. Tremendous amount of time, efforts and work has been put in this project to uncover the problems and develop recommendations. We are not looking for any personal gain nor do we have any personal agenda or motivation. Our work is driven by only one goal, that as a public entity and as public servants we have an obligation to do the right thing and to make a difference for those we are committed to serve.

Why should anyone trust this report?

It is understandable that some people will be apprehensive, doubtful, and defensive. Some may even be critical. Our goal is to present information to stakeholders so they can make well informed decisions as they deem appropriate. For those who still have doubts we encourage them to ask the questions:

- Why was there \$346 million (June 2019) cash in Building and Safety Permit Fund?
- How did the fund accumulate so much cash? or What is this money for?

We are very confident that the only place where one will find answers to these questions is in this report.

What would it take to capitalize on the opportunity?

The success of a team does not depend on one individual or group of individuals; it depends on every member of the team working together and in unison for the common goal of team's success. Similarly, in this case, value can only be created through an effective collaboration of all stakeholders.

What is the rush to do anything?

Under normal circumstances, there would be no rush to do anything. However, we believe that the current pandemic has created a sense of urgency. No one anticipated this crisis that has shaken the core of humanity. While the top priority right now is to prevent risk to human lives, that risk will eventually subside. However, the crisis will leave another long-term impact, a potential fiscal turmoil of unprecedented proportions.

Depending on the duration of the crisis, severity of its impacts and speed of recovery it is possible that it may significantly deplete the City's meager reserves or safety net. It may also cause significant long term financial impacts that may affect the City's ability to effectively serve its residents. Raising taxes would not be an option.

Besides meeting its budgetary needs with limited resources, it is also very likely that the City may be looked upon to help assist and provide relief in the form of tax deferrals or holidays to suffering businesses.

Let us Collaborate!

Not an end but a new beginning

The City may also be expected to create an environment to help businesses flourish again by relaxing regulations and reducing fines and fees.

Our intention is not to paint a gloom and doom situation, but these are unprecedented times. Who would have imagined just a month ago that we all will feel so unprepared and helpless. In a matter of weeks, the Country has gone from full employment to more than 22 million unemployed and many other severe financial impacts are likely to follow.

It is possible that everything will go back to being what it was a month ago and happy times and booming economy will return. No one has a crystal ball, and no one knows what will happen, but prudence dictates that one should hope for the best and plan for the worst.

We have tremendous confidence in the resilience, leadership, compassion, care, concern that people have demonstrated and hope that everyone will come together and make sacrifices to help each other. However, we need to be pragmatic and must have a plan. Depending on how quickly the City can mobilize support, the opportunity could provide some respite and offer benefits for both short term and long term needs.

In the short term, it offers money, which the City leadership may be able to use to help its residents and businesses in this crisis, to protect them and create some positive impacts on the vulnerable and offer some relief to lessen their suffering.

In the long term it can help the City better prepare for what might be a long term financial turmoil. The City would not only need money but would also need to reinvent itself, become lean and agile. If the crisis is extended the City would need to find ways to serve its residents and customers with fewer resources.

If the City is proactive it may be able to blunt some of the financial impacts of this crisis, position itself for a speedy recovery and emerge a stronger and renewed organization.

But the City must act fast and bring together various stakeholders. As we have shared anything is possible, the City already has many dedicated and committed soldiers, all the City needs is an entrepreneurial mindset, bring people together and facilitate a journey to capitalize on this opportunity and explore additional opportunities.

We are very thankful to Controller Galperin for his support and to those who have influenced this project. We are proud and grateful to be part of this exciting adventure and to have an opportunity to make a difference and to better serve the **Great City of Los Angeles**, its stakeholders and the **Angelenos**.

Thank you,

There is also an opportunity for the City to transform itself into an agile and high performing organization of the future.

To Help the Angelenos!



Appendix 1 (a)

History of Building and Safety Permit Fund, its need, purpose and legal requirements

- The Building and Safety Permit Fund was established in 2005
- It was established to ensure compliance with State Law (California Government Code section 66014(a)), which requires that when a local agency charges fees for --- building inspections; building permit..... those fees may not exceed the estimated reasonable costs of providing the service for which the fees is charged. This view is further confirmed by CAO Report 0220-0394 7-0000, March 2, 2005, page 1, paragraph 3, which states, " "State law requires that building permit fees collected be spent on providing the services for which the fees were collected (Government Code Section 66014). Currently, showing compliance with this law would be very difficult for the City,"
- This action was prompted by a 4.5 million verdict against Orange County, which ruled that "The Planning Department overcharged for building fees....."

\$4.5-Million Ruling Goes Against O.C.

The planning department overcharged for building fees and then misspent the money, a judge says.

The fund was established as an enterprise fund, even though under GAAP it is considered a special revenue fund and reflected accordingly in City's annual audited financial statements (CAFR), The intent was to separate the fees from the General Fund so the City could demonstrate compliance with the State law.

As discussed in chapter 2 and also eluded in CAO report referenced here the fees do not have to match the costs on an annual basis. It is reasonable for the fees collected in one year to be used to offset costs in one year as long as they relate to Building and Safety operations.

Appendix 1 (b)

Building and Safety fee increase in 2010

In 2010 after much analysis and deliberations the City Council approved ordinance 180868, which increased various Building and Safety fees effective July 1, 2010.

The fees were increased because it was determined that the fees at that time were not sufficient to recover the full costs of providing services. Staff also compared the City fees with other jurisdictions and found that the City fees were lower than many other jurisdictions.

The City increased almost 400 different fees. The average rate increase was more than 30%

The new fees were considered to be in compliance with California Government Code section 66016(a) no local agency shall levy a new fee or service charge or increase an existing fee or service charge to an amount which exceeds the estimated amount required to provide the service for which the fees or service charge is levied. (Relevant reports, analysis, motions and ordinance relating to fees increases can be found in Council File CF 09-600-S130

Appendix 1 (b) cont.

How the new fees were determined?

The new fees were supposed to recover full costs for providing various services and included:

- All direct costs such as salary, overtime etc.
- All indirect costs. The City decided to use Cost Allocation Plan (CAP) rates for Fiscal year 2008-09 also referred to as CAP 31, which was 74.88% (75%)
- The new fees went in effect on July 1, 2010 and the Building and Safety Permit Fund started collecting the new increased fees
- The fee adjustment resulted in significant increase in Building and Safety revenues over the years, but the costs recorded in the Building and Safety Permit Fund did not increase at the same rate, suggesting that the fees collected exceeded the costs of providing services recorded in the fund.
- The ordinance also directed the Superintendent of Building and Safety Operations to adjust the fees annually in July every year based on inflation. Any fees adjustments exceeding the inflation adjustment required Council approval. **(No fee adjustments have been made since 2010)**

Appendix 1 (c)

Could there be another reason for this huge stash of cash?

If the City borrowed hundreds of millions of dollars or it collected hundreds of millions of dollars in advance fees, then that may explain such huge cash balance. However, we checked for these two possibilities and our review does not support this hypothesis.

- Building and Safety Permit Fund's financials included in the City's Comprehensive Annual Financial report (CAFR) for Fiscal Year 2019 show a fund balance of \$340 million
- According to Generally Accepted Accounting Principles (GAAP) Fund Balance represents the difference between assets and liabilities or accumulated surplus, (balance of revenues over expenses) and is similar to equity or capital
- Based on performance measures included in the budget 80%-100% of the various tasks are completed within 15-20 days. This would suggest that amount of fees collected for which, services have not yet been provided should not be significant. The June 30, 2019 CAFR shows unearned revenues (revenues received for which service is yet to be provided) at \$7.4 million only
- Further Building and Safety department maintains another fund Building and Safety Trust Fund, which is supposed to record amounts collected as deposits, advances or other liabilities. There was a cash balance of \$41 million in that fund on June 30, 2019
- City's 2020 adopted budget identifies \$313 million in cash on July 1, 2019 and shows 93% of this cash or \$292 million as a reserve for future costs. There is no information in the budget to justify what future costs would the \$292 million be spent on. Building and Safety is a service operation and the fees are supposed to be for the costs of providing services for which the fees were collected, and any future costs should be paid from future fees. As discussed in chapter 2, if it was supposed to be a reserve, then \$292 million would be very substantial and unreasonable reserve

Unless it is argued and proven that the City's financial records, reports, budgets and financial statements are inaccurate the only reasonable conclusion appears to be that the City has been charging more in fees than it should.

City's accounting process of recording/allocating revenues and costs

City is a very large and decentralized organization collecting and disbursing billions of dollars every year. Depending on their nature, the revenues and costs are recorded in hundreds of funds, The General Fund is the chief operating fund. While many of the accounting practices are similar, some differ based on the department and the fund. This discussion is with reference to the Building and Safety operations only.

Accounting for Revenues (Fees)

The fees and charges for various Building and Safety services that are subject to the provision of California Government Code section 66014(a) are collected and kept in the Building and Safety Permit Fund. There are some revenues such as fines that are recorded and accounted in the General Fund.

Accounting for Costs

The costs are spent from different sources: (1) General Fund (2) Building and Safety Permit Fund and (3) indirect costs are spent from various departments in the General Fund.

Types of Costs

For the purpose of this discussion the costs are grouped into two broad categories (1) direct costs and (2) indirect costs. Whether a cost is direct cost or an indirect cost depends on many factors. A cost may be direct in one situation and indirect in another. Direct costs and their accounting is discussed in this appendix and indirect costs and their accounting is discussed in appendix 3.

Direct Costs

Direct costs are costs that can be easily identified with projects, programs, services or activities. For example if the City assigns ten police officers at Dodgers stadium. It is easy to determine their salary and overtime costs based on the time they spend there.

Direct costs (cont.)

Similarly, if a building inspector spends 100 hours on inspection of a building then the salary for 100 hours can be easily determined and is considered direct cost. For Building and Safety operations the direct costs are paid from two sources (1) General Fund and (2) Building and Safety Permit Fund as discussed here:

1. Costs spent General Fund

Costs such as salary for regular and part time employees and overtime. Costs for printing, office and administrative expenses and transportation costs for employees are considered direct costs and recorded in Building and Safety department in the General Fund.

These costs are subsequently transferred or allocated to the Building and Safety Permit Fund (BSPF).

2. Costs spent from the Building and Safety Permit Fund (BSPF)

Costs such as equipment, training as well as costs for special direct services provided by departments such as ITA, City Attorney, Personnel, and others are paid directly from BSPF.

The City should record all costs directly in one place namely the Building and Safety Permit Fund.

The current practice to first record costs in the General Fund and then move them to BSPF, if changed would make the process more efficient, reduce errors, improve oversight, accountability and transparency and annually the City would save significant amount of time and resources.

It is understandable that this has been a long standing practice. Maybe it is time to change.

What is a Cost Allocation Plan? Why is it needed and what is its purpose?

Cost Allocation Plan (CAP) is a process, to determine indirect costs or overhead. The City receives numerous grants from Federal and State governments and provides services to many public and private organizations including other funds and departments. The City uses CAP rates to recover its costs. As discussed in appendix 2, it is easy to determine direct costs as they may be easily identified or associated with a program project or activity. However, it is not that easy to identify and allocate indirect costs.

What are Indirect Costs?

As we discussed earlier, in case of Apple, the cost of the iPhone that Apple buys from the manufacturer is a direct cost. Costs for marketing, sales, advertising etc. are considered indirect costs because they cannot be easily identified with a specific iPhone.

Similarly, for the City, in case of police officers assigned to Dodgers stadium or building inspector, in addition to their salary there are many other costs that the City spends. These costs include, retirement and medical costs, workers compensation costs, the cost of their vehicles. Equipment, recruitment and training costs and the cost of processing their paychecks, office and administrative expenses, cost of building and equipment maintenance, utilities and cost of support functions such as personnel, accounting, ITA and much more.

All these costs are considered indirect costs and must be added to the salary of the police officers or building inspector to determine full cost and should be collected or recovered from recipients of service. If not done tax payers would end up subsidizing private enterprise and this could constitute gift of public funds in certain cases.

Cost Allocation Plan

There are numerous indirect costs and they are paid for and recorded in various cost centers or departments in the General Fund. CAP is a process that helps identify, accumulate and allocate all these indirect costs to various programs, projects, activities or funds.

CAP provides a rate that is applied to the direct salary (in our case) to calculate the amount to be billed to the respective agencies whether it be Dodgers stadium for police officers, or for building inspection or from Federal or State governments for various grant funded projects or other City funds.

City's Cost Allocation Plan rates have three main components a separate rate is calculated for each component?

- **Fringe Benefits**, which includes costs such as employee retirement costs, medical costs, workers compensation costs and payroll taxes
- **Central Services**, which includes costs such as utilities, rent, maintenance and cost of support departments such as ITA, City Attorney, Controller, Personnel, CAO etc.
- **Department Administration and Support**, which includes administrative and overhead costs for the department for which the rate is being developed (Building and Safety in this case)

City's CAP rates are prepared pursuant to Federal guidelines, which limit how much overhead costs can be allocated to Federal grants. These guidelines are restrictive and limit the types of costs and amounts that are eligible to be collected and are generally lower than what should be applied to determine costs to be charged against the fees for Building Safety services.

The City should developed a separate CAP process and rates for allocating General Fund costs to the Building and Safety Permit and even other funds.

What went wrong and why?

Why did the General Fund not get paid what it spent? What went wrong?

In chapter 3 we discussed that the General Fund did not get paid what was due to it. This appendix discusses the why? Further on page 11, we identified the following as the main reasons why the General Fund was not paid for full costs it had spent:

- a. All direct costs spent by the General Fund relating to the Building and Safety operations were not allocated to the Building and Safety Permit Fund
- b. The CAP rates applied by the department to pay General Fund were lower than required
- c. CAP rates were applied to a smaller base or salary
- d. The CAP rates were not appropriate for the purposes of calculating indirect costs to be charged against the fees collected for the Building and Safety operations
- e. The annual budgets established a lower than required expectation for indirect costs to be paid to the General Fund
- f. Lack of sufficient oversight and monitoring prevented the problem from being discovered until now

In the following sections we discuss these items in greater detail:

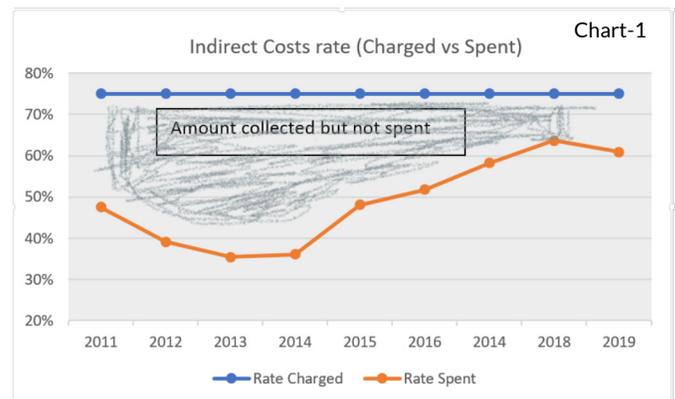
(a.) Lower than required direct costs

Annually the General Fund was only allocating or recovering only about 90% of the costs it incurred for Building and Safety Operations. This resulted in lower allocation of both direct and indirect cost.

The appropriate process would have been to allocate 100% of the costs to BSPF and if the fund provided any services to the GF then bill and recover them separately.

(b.) Lower than required indirect costs

Even though the indirect costs included in the fees were 75% of salary appendix 1(b) the actual indirect costs paid to the General Fund were much lower as shown in the following chart



The average rate used to pay the General Fund (rate spent-Note 2) for Fiscal Years 2011 to 2019 was only 49% compared to the 75% collected as part of the fees. The shaded area represents the amount collected by the Building and Safety permit Fund (BSPF) which was never spent and constitutes a significant portion of the cash sitting in the BSPF.

It appears that even though the fees were increased to ensure full cost recovery the accounting and budgeting processes did not change to incorporate the new expectations.

Note 2: The "rate spent" in the above charts is a derived rate. The calculation of amount payable to the GF were performed by the Building and Safety departmental staff based on offline manual documents. The actual salary allocated to the Building and Safety Permit Fund is not readily available in either annual budgets or City's financial system. We had to use the ratio of total GF costs for Building and Safety Operations transferred or allocated to the Building and Safety Permit Fund vs. the total costs incurred by the General Fund, which is about 88%. For fiscal years 2018 and 2019 we obtained the offline documents from the department and calculated the actual ratio of salaries allocated vs actual salaries spent. And the rate was close to the 90% rate. The above chart is only to demonstrate the existence of the problem and not to calculate the amount owed to the General Fund.

What went wrong and why?

Why did the department use lower rates?

The Building and Safety accounting staff calculates the amount of indirect costs to be paid to the General Fund by applying the CAP rates to the salary. We looked at the calculations of the indirect costs done by the department and noticed the following:

The department was not applying the total CAP rates, they were only applying the Fringe Benefit and Central Service rates, which is much lower than the total rate included in the fees.

Department staff was then further reducing the rates (it appears that this exclusion was for certain direct billed costs by certain departments such as ITA, City Attorney and Personnel from the allocable indirect costs. We believe that this exclusion is incorrect and should not have been made.

(c.) CAP rates applied to incorrect base

As discussed under item (a) earlier the General Fund only recovered about (90%) of the direct costs incurred by it and about 10% remained in the General Fund. The CAP rates were only applied to the salaries allocated to the Building and Safety Permit Fund, namely 90% when they should have been applied to 100%. For example if the total salary is \$100 the indirect costs @75% would be \$75. In this scenario the indirect costs allocated were only \$68 (90% of 75). This resulted in lower recovery of indirect costs.

(d.) CAP rates as calculated are not appropriate for the purposes of calculating indirect costs for the Building and Safety Operations

As discussed in appendix 3, the City's CAP process follows Federal guidelines, which are restrictive and place limitations on what costs are allowable and how much? As a result, the CAP rates are lower than the rates that are needed to ensure full cost recovery.

Use of these lower rates resulted in less than full cost recovery and consequently the General Fund did not recover all the costs it had spent on Building and Safety operations.

We also noticed several other issues with the CAP rates. It is not known if they are the result of following restrictive Federal guidelines or something else. CAP rates are reviewed and approved by the Federal Government suggesting that they accepted the rates and considered them appropriate for their purposes.

We have not audited the CAP rates and it is not our intent to establish if they are correct or not. Our intent is to determine if they are appropriate for the purpose of ensuring full cost recovery of General Fund costs spent for Building and Safety operations. The rates might be acceptable for Federal grant purposes but still may not be appropriate for this purpose)

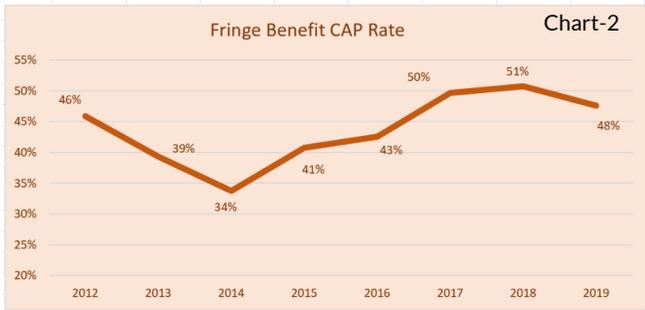
As we shared previously the total CAP rates comprise of three components Fringe Benefits rate, Central Services Rate and Department Administration and Support.

In the following section we will analyze each rate to determine why we think it is not appropriate:

What went wrong and why?

Fringe Benefit Rate

Following chart shows the trend of Fringe benefit rates for Building and Safety Department.



As shown in the chart the Fringe benefits rate has fluctuated significantly from year to year. It dropped from 46% in Fiscal year 2012 to 34% in Fiscal Year 2014 a 26% drop and stayed below FY 2011 until FY 2017. The average rate for the period Fiscal Year 2012 to Fiscal Year 2019 is 44%, which is lower than the 2011-12 rate.

The two major components of this rate are retirement and medical costs, both these costs have not declined, in fact they have increased.

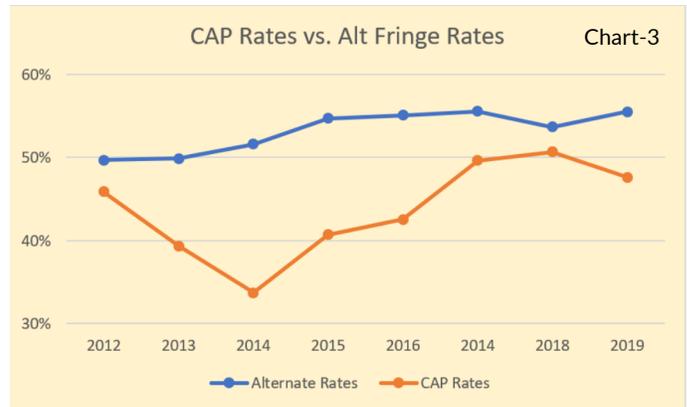
Upon a closer look at the rates and the underlying calculations it appears that various cost components fluctuated from one year to another as well as there were inconsistencies and fluctuation in the salary used to calculate the rates. The rate is a factor of numerator the cost such as retirement or medical and the denominator salary. Any unusual fluctuations in either would impact the rate. There is also the issue of carry forward that impacts the rates. A refined process would eliminate this issue as well.

It is not known why the various cost components, salary or rates would fluctuate from one year to another. Whatever the reason, these trends create doubts about the appropriateness of fringe benefits component of the CAP rate for the purpose of recovering General Fund costs from Building and Safety Fund.

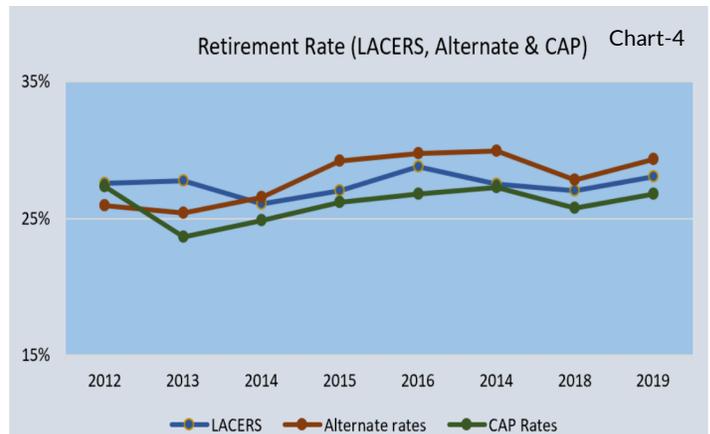
An alternate Approach

To determine the amount of Fringe benefit cost that should be recovered and paid to the General Fund we used an alternate and much simpler methodology to develop an alternate CAP rate. The details of our methodology and process are included in *appendix 5 page 35*.

Following chart shows the trend of Fringe benefits rate based on CAP as well as the alternate methodology. As shown in the chart the alternate rates are more consistent.



We also compared the retirement component of our rate with LACERS actuarial reports. The average rates for this period are; alternate rate 27.84%, LACERS rate 27.48%, and CAP rate 26.09%. The difference between alternate and LACERS rates is because of timing. LACERS rate is estimated in advance and based on estimated salary. Our rate is based on actual payments to LACERS. The CAP rate dropped from 2012 to 2013 and stayed lower. A 2% rate difference results in more than \$1.5 million impact every year.



What went wrong and why?

Central Service Rate

Similar issues were notice with the central services rate also, which also appears to be lower than what it should be. Generally, this rate should include all costs for support departments such as Personnel, GSD, ITA, City Attorney, Council, etc. However, it appears that it does not, further we noticed inconsistencies with this rate also.

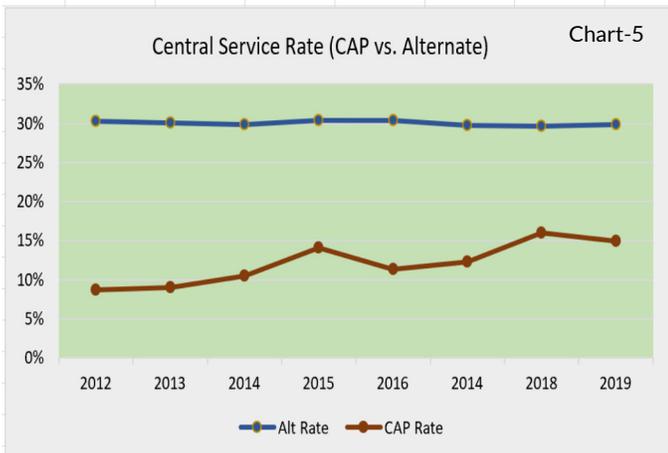
The central service rate went from 21.04% for CAP 31 for fiscal year 2009 to 8.94% for CAP 33 for fiscal year 2011. almost a 57% reduction. CAP 31 was the rate used to increase the fees in 2010. If the rate of 21.04% is incorrect then it means that the fees are incorrect and the City is charging more than it should, if the rate of 8.94% is incorrect then it means that the GF lost significant amount of money. We believe that the central service rate of 8.94% is significantly lower than the rate required to ensure full cost recovery.

We noticed inconsistencies and fluctuations in various components, of rates from one year to another year, for example the building lease rate ranged from a high of 3.23% to a low of 0.69% similar fluctuations were notice in others as well.

Just like the Fringe benefits rate this CAP rate is also considered not appropriate for allocating General Fund costs to Building and Safety Permit Fund.

We used an alternate methodology for calculating this rate as discussed in *appendix 5 page 36*.

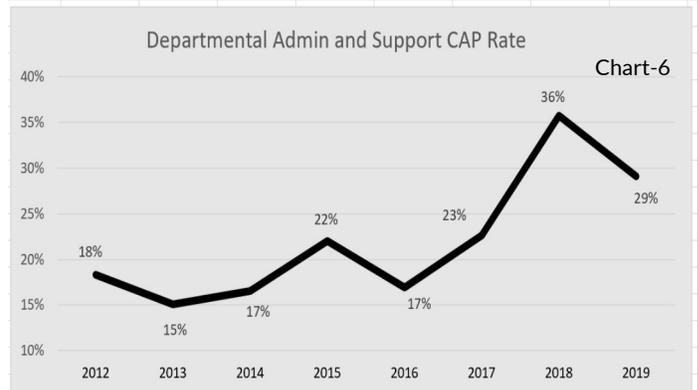
Following chart shows the central service rate per CAP and per our alternate methodology. As shown in the chart the alternate rates are much higher because they include most costs and are also very consistent unlike the CAP rates.



Departmental Administration and Support Rate

The third component of the CAP rate is the Department Administration and Support rate. For Building and Safety this rate includes expenditures that are not directly charged to grant or fee program and includes costs such as costs of department management, clerical staff, systems staff etc. or other unallocated costs.

We noticed some issues with this rate as well. Following chart shows the departmental administration and support component of the CAP rate for Building and safety operations.



As shown in the chart the rate saw a significant increase since Fiscal year 2016.

The increase since 2015-16 appears to be very unreasonable. It is not known why the rate would more than double in two years?

Applying this rate would result in excessive recovery. For example, in Fiscal year 2018, the General Fund salaries allocated to the Building and Safety Permit Fund were \$77 million. Applying the rate of 36% would result in a \$28 million cost allocation for this component of the CAP rate alone, which is far greater than the remaining unallocated costs, which were only \$9 million. Even after applying the fringe and central service rate there will be over recovery.

For these reasons, this rate also appears to be not appropriate. Further this rate is not necessary under the alternate methodology whereby all costs are accumulated in BSPF.

What went wrong and why?

Summary (d) - CAP Rates are not appropriate for this purpose

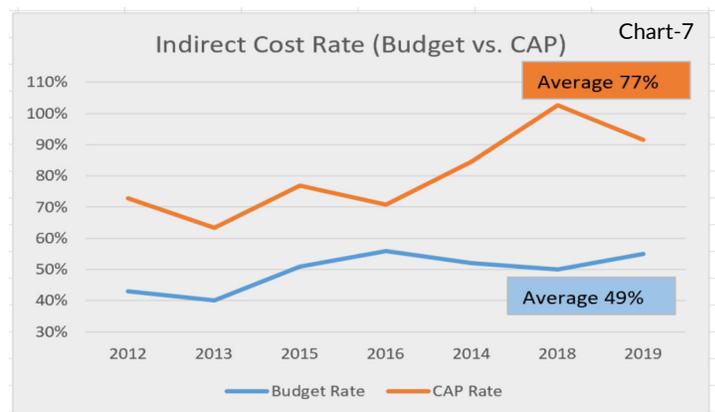
To summarize; why we think the CAP rates are not appropriate for allocating General Fund costs to the Building and Safety Permit Fund?

- The CAP rates are prepared for use for Federal grants, and do not include all costs
- The CAP rates appear to have numerous inconsistencies and unreasonable fluctuations
- Departmental administration and Support rate is not necessary
- Because of these reasons the CAP rates appear to be significantly lower
- The CAP rates as calculated may be acceptable for the purpose they were developed namely allocation of cost for Federal Grants, but as shown here they are not appropriate for recovering General Fund costs from the Building and Safety Permit Fund and result in significant lower recovery for the General Fund.

(e.) The annual budgets established a lower than required expectation for indirect costs to be paid to the General Fund

It appears that the annual budgets did not use CAP rates for budgeting the indirect costs that should be payable to the General Fund, it is not known, how the budget amounts were arrived at.

The indirect cost amounts that the General Fund was supposed to recover per annual budgets were much lower than amounts necessary for the General Fund to recover full cost that it had spent for Building and Safety operations. The following chart shows the budgeted amounts and the amounts per CAP rates



As shown in the chart the annual budgets expected the General Fund to get paid at a much lower rate (average 49%) compared to the average CAP rate of 77%. The fees set in 2010 included an indirect cost rate of 75% subject to annual adjustments per annual CAP rates. Lower amounts in the budget were also a contributing factor.

(f.) Lack of sufficient oversight and monitoring prevented the problem from being discovered until now

There does not appear to be a process to maintain sufficient oversight on what the department was doing, if they were paying the General Fund appropriate amounts. There also does not appear to be a good process for fiscal monitoring or auditing resulting in the problem staying hidden.

What went wrong and why?

Recommended simpler and more efficient Process

The City's CAP plan process was established decades ago, it is overly complicated and manual.

Since the CAP rates are developed for Federal grants and are subject to review by Federal representatives it takes a very long time to finalize them.

While the City can continue to use the current CAP process for Federal grant purposes, there is no need to use an overly complex process that results in an incorrect outcome for allocating General Fund indirect costs to the Building and Safety Permit Fund or even other funds.

Using an alternate approach as described in appendix 5 would be much simpler, accurate, consistent and efficient and will save the City significant time and resources and eliminate all of the problems discussed above

To summarize:

While the Building and Safety Permit Fund was charging customers a higher rate for indirect costs as part of the fees it was only paying the General Fund a much smaller amount (Chart 1, page 27) due to various reasons discussed in this appendix. We developed a new process that uses:

- Different methodology to accumulate and allocate costs
 - Alternate simpler CAP rates
- and
- Provides greater oversight and monitoring
 - Supports verification and validation of results

Our process is a model and for demonstration purposes only. Before adoption the, the City should verify and refine it and replace estimates with actuals.

We hope that the information provided in this appendix demonstrates that there were issues with City's accounting, CAP and budget processes that resulted in the GF losing hundreds of millions of dollars.

It is very important to note that the issues mentioned are not the fault of any individual.

The problems are the result of overly complex and manual processes. Further loss of knowledge due to recession, absence of subject matter expertise and lack of training compounded the problem.

How much is owed to the General Fund and How was it Calculated?

In appendices 3 and 4, we discussed why the General Fund lost money. In chapter 4 we provided an estimate of how much money could be available to the General Fund (GF). In this appendix we provide information on how we estimated the amount, due to the General Fund, our methodology, approach and a framework we used to estimate the amount.

We had to develop an alternate accounting process and alternate CAP rates to estimate the amount owed to the General Fund. This was necessary because there were numerous problems with the current processes and to determine the exact amount using the current processes will require significant time and resources. Many of the processes are manual and offline, are not properly documented or consistent and staff who prepared them are not there any more. As a result lot of the relevant information required is not readily available in one place in City's financial system, financial records or budget documents.

Further inconsistency in how various processes were performed was another problem.

In order to deliver accurate and reliable information, processes need to be standard, consistent and should result in outcomes that can be supported and validated. To determine exactly what went wrong, the City would need to conduct an audit, review and analyze transactions for almost a decade and the whole process could take many years to unravel.

Need for simple, standard and consistent processes and CAP rates

Therefore, rather than retracing every step to pinpoint exactly what was not done and its impacts we developed a different approach to estimate the amount owed to the General Fund.

Our approach is based on how things should have been in the first place, giving us a new path or direction to reach the goal in a highly efficient manner and also produce consistent and reliable outcomes. For example under the current CAP process the fringe rate is calculated separately for each department using different costs and salaries.

This is not necessary because majority of costs for civilian employees do not change based on the department an employee works. This would eliminate lot of complexity, simplify the process and save significant time and costs. Similarly other components of the rates could also be simplified using this approach.

If the City agrees with the report it can use our framework to determine the exact amount to be transferred to the GF. We are confident that our alternate approach could also provide a framework for the City to replace the current processes with something that is more efficient, save significant time and money and would produce consistent and accurate outcomes in the long run. Our approach can be easily automated and integrated with City's payroll and financial systems to make the process even more efficient.

In the following pages we provide the details of our alternate approach, which includes two components, a different methodology to accumulate costs and alternate CAP rates.

How much is owed to the General Fund and How was it Calculated? cont.

An Alternate Approach

There are two components of the new approach:

- A. Alternate cost accumulation methodology and process**
- B. Alternate CAP rates**

This approach is relatively simple and easy and unlike the current complex process results in amounts that are consistent, can be readily verified and validated and addresses most of the problems that resulted in the General Fund losing such substantial amount of money.

A. Alternate Cost Accumulation Methodology and Process

The new process follows the following steps to accumulate and allocate General Fund costs for Fiscal Years 2012 to 2019: As mentioned earlier we used the same model to estimate the amount for FY 2011 as well because many details for FY 2011 are not readily available since the City migrated to a new system in FY 2012,

STEPS FOLLOWED:

1. Accumulate all costs in one place
2. Apply alternate CAP rates
3. Accumulate all receipts in one place
4. Determine total costs
5. Identify amounts paid to GF previously
6. Determine amounts owed to the GF

1. Accumulate all costs in one place

One of the biggest problems was that costs and revenues are accounted in different funds with no robust process for reconciliation. Under the new approach, all direct costs for Building and Safety Operations, are accumulated in one place.

All (100%) direct costs for Building and Safety Operations, which are incurred and recorded in the General Fund should either be recorded directly or transferred to the Building and Safety Permit Fund. (Since the Council established a separate fund it is not known why the costs were not charged there directly). The costs for the Building and Safety Operations should be accounted for in the same way as Recreation and Parks or Library, whereby all costs salary, overtime etc. are charged and paid for directly by the respective Funds.

This approach, if adopted would simplify accounting and improve accuracy, Additionally, it will also improve transparency, reduce the amount of time spent by staff in recording accounting transactions and save significant amount of costs.

2. Apply relevant/alternate CAP rates

Apply the new alternate CAP rates as calculated in the following section (page 35-36) to the overall Building and Safety operations based on total salaries recorded in the Building and Safety Permit Fund under step 1 above. (This method allocates all applicable indirect costs to the Building and Safety operations rather than partial costs as done currently.

3. Accumulate all receipts

Record/transfer all receipts for costs recovered by the General Fund from other funds to the Building and Safety Permit Fund

How much is owed to the General Fund and How was it Calculated? cont.

4. Total or Full costs (4=1+2+3)

The sum of 1, 2 and 3 represents the full costs for Building and Safety operations to be paid for by the fees collected in the Building and Safety Permit Fund and payable to the General Fund

5. Amount paid to General Fund previously

Calculate the amount paid to the General Fund by the Building and Safety permit fund in the past.

6. Amount owed to the General Fund (6=4-5)

The difference between 5 and 6 is the amount absorbed by the General Fund (GF), that should be paid back to it by the Building and Safety Permit Fund.

The above steps will:

1. Record all (full) costs for Building and Safety operations in the BSPF
2. Apply the correct CAP rates
3. Reimburse the GF for all costs incurred by it
4. Eliminate most of the problems and financial loss suffered by the GF
5. Save significant amount of time and money that is spent annually on complex and inefficient processes
6. Provide a process that can be verified, validated, provides audit trail, improves oversight and accountability, is simple and can be automated

B. Alternate CAP rates

We used the following process to calculate the alternate CAP rates for civilian employees. The amounts for various costs were compiled from City accounts using the following process:

Allocable Base

Obtained total civilian and sworn salaries from City's accounts. Civilian salaries were used as a base (denominator) to calculate various indirect rates as discussed below:

Fringe Benefits rate

Following costs are included in this rate:

- Retirement costs based on annual amounts paid to LACERS recorded in the General Fund
- Medical costs for Building and Safety employees per data received from City's third part y administrator and recorded in payroll system PaySR
- Medicate costs at 1.45%
- Workers Compensation costs were based on a ratio of actual costs spent based on civilian percentage of total costs per actuarial report
- Other employee related costs such as unemployment insurance, employee assistance program based on a portion of actual costs recorded in the General Fund
- The total of all these costs were divided by the allocable base to calculate the Fringe benefits rate

We did not consider benefits for part-time or the workers compensation costs for overtime and should be considered.

How much is owed to the General Fund and How was it Calculated?

Central Service rate

Following are the components and the process used to calculate this rate:

1. Utility, liability claims etc.

- This rate includes costs such as utilities, annual audit and liability claims (non-police, non-fire and non-street services related we suggest actual costs should be determined and used)
- These costs were compiled from amounts paid and recorded in the General Fund
- These costs were then allocated between sworn and non-sworn based on the ratio of sworn and civilian salaries, which is 50%

2. Support department component

A cost allocation plan should calculate and allocates all indirect costs. The City incurs substantial costs for support departments such as ITA, council, CAO, GSD, City attorney, Personnel etc. All of these costs should be allocated to primary departments to ensure full cost recovery. These costs are included under the central service rate; however, the current CAP does not include all of these costs. Our alternate CAP rate includes all costs for support departments.

Following steps were used to calculate this rate. (Note-3)

- All costs for support departments were accumulated
- Applied the Fringe benefits rates to these departments using their salary as a basis
- For GSD we only considered 90% of the costs on the basis that GSD costs may include a greater portion for sworn departments. The 10% results in excluding about \$27 million in GSD costs annually. City would need to determine a more exact allocation of GSD costs

- Calculated support department revenues and the costs these departments have recovered from other departments and funds. The support department costs calculated in the previous step are reduced by these revenues to determine the net support department costs. Adjustments were made for citywide revenues such as interest income
- The net support department costs were divided by the total salaries (civilian and sworn) to calculate the support department rate
- We considered 4% for depreciation and MICLA costs, as these costs are not readily available. CAP rates include about 2% for building depreciation, in addition there is vehicle and equipment depreciation also. Even though the department has numerous vehicles the vehicle depreciation including in CAP rates is negligible. We expect that the actual rate for these items would be higher
- We also considered about 1% towards police, fire and street services costs incurred to support Building and Safety operations. Further Building and Safety is housed in a separate building and exact lease and maintenance costs for that building are not readily available at this time but need to be considered

(Note-3): The City should determine exact costs for these items before using these rates

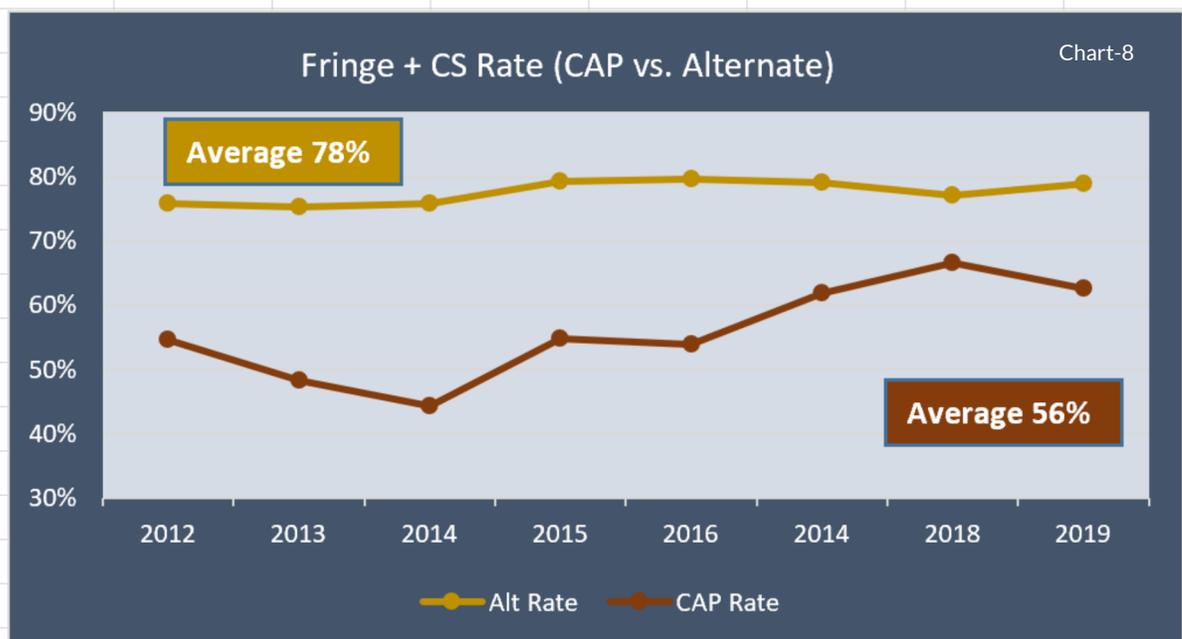
Total Rate

The sum of Fringe and Central Service rate is the new CAP rate. Using this approach, we calculated estimated rates for Fiscal years 2012 to 2019. For 2011 we considered 95% of the FY 2012 rates to be conservative.

Table 1 and chart 8 on the next page provide the alternate rates and the Fringe + Central Service rates per CAP. The alternate rates are more consistent.

CAP Rates Comparison Alternate Rates vs. CAP Rates

Fiscal Year	Fringe	Central Service	Total Alt Rate	CAP Rates (Fringe + CS)
2012	46%	30%	76%	55%
2013	45%	30%	75%	48%
2014	46%	30%	76%	44%
2015	49%	31%	79%	55%
2016	49%	30%	80%	54%
2017	49%	30%	79%	62%
2018	47%	30%	77%	67%
2019	49%	30%	79%	63%



Calculating and allocating Indirect costs

Now we have all the costs relating to Building and Safety operations in one place per item A (1) on page 34 and have calculated alternate CAP rates per item B as shown on page 35 and in table on page 37. Next we performed the steps 2-6 as listed on pages 34-35 to come up with an estimate of the amount owed to the General Fund.

Interest

In addition to the amount owed to the General Fund for unpaid costs, we also allocated interest. Between Fiscal years 2011 and 2019 the BSPF earned \$17 million in interest income. If it had paid the General Fund money owed to it annually it would not have earned the interest but the GF would have. Based on simple calculation our estimates included \$12.5 million in interest (subject to change).

Amount owed to the General Fund

Based on these steps the amount owed to the General Fund along with interest is estimated to be \$290 million subject to adjustments.

As shown in the table the amount of \$290 million is made up of two components as discussed in chapter 4. \$233 million in each respective year and \$57 million for FY 2011-2013 that would need to come from future years.

Due to the recession the Building and Safety revenues declined significantly, There was less work because of fewer developments and improvements and consequently the fees were lower, however, the City still needed to maintain staff to perform the various functions.

While the City was incurring the costs there was not enough revenue coming in to cover all the costs.

If the City had done correct accounting to begin with the fund would have accumulated deficits, which could have been offset against future revenues.

We believe that the total \$290 million can and should be recovered because it was the cost of doing business. The City may consult with the City Attorney's Office.

There still may be a risk

If the City only transfers \$233 million that would leave about \$113 million June 30, 2019 and higher amount in 2020 in the fund creating a potential for risk. To prevent risks the City in consultation with the City Attorney's Office should determine what would be considered an appropriate amount of reserve and cash and document it?

Other Items and consideration

Besides refining the calculation and coming up with and exact amount that should be recovered the City must analyze the other items listed in appendix 6 especially the unfunded liabilities and determine if additional amounts are owed to the General Fund.

We are positive that the City can recover amounts for accrued portions of the outstanding retirement, workers compensation and leave balance liabilities, we expect them to be quite substantial.

The table on the following page shows the amount available to the General Fund by Fiscal Year.

Estimated Amount Due to the General Fund

Total amount owed to GF for Fiscal Years 2011 to 2019**					
<u>Alternate</u> Methodology and <u>Alternate</u> CAP rates					
Fiscal Year (FY)	Total Due (Including Interest)	Maximum Amount Available in FY	Remaining Amount	Total	
2011	28,000,000	3,000,000	25,000,000	28,000,000	
2012	35,000,000	13,000,000	22,000,000	35,000,000	
2013	35,000,000	25,000,000	10,000,000	35,000,000	
2014	36,000,000	36,000,000	-	36,000,000	
2015	33,000,000	33,000,000	-	33,000,000	
2016	33,000,000	33,000,000	-	33,000,000	
2017	31,000,000	31,000,000	-	31,000,000	
2018	29,000,000	29,000,000	-	29,000,000	
2019	30,000,000	30,000,000	-	30,000,000	
**					
Total 2011-2019	\$ 290,000,000	\$ 233,000,000	\$ 57,000,000	\$ 290,000,000	

** In arriving at our estimate, we were conservative in our calculations. Additionally we also rounded down the amounts shown in the table by \$10 million.

The readers have probably realized that these are overly complex and confusing issues and cannot be easily explained in few pages. The purpose of this report and appendices as we have stated earlier is to give users some understanding of the issues and their impacts. Further due to time and resource constraints in arriving at the estimates we had to make some assumptions and estimates.

We recommend that this approach, methodology and numbers be considered as a model and framework and that the City engage subject matter experts to sort out all relevant details, address and resolve all issues, verify and validated the report before decision making.

Other Considerations

Policy issues and other factors that may impact the final amount available to the General Fund

Our analysis is not driven by whether the General Fund (GF) should get the money or how much it should get or whether an issue increases or decreases the amount available to the GF.

As a public agency we have an obligation to be transparent, accountable and uphold public's trust.

The purpose of this report is to objectively analyze all issues and pros and cons, irrespective of the outcome and submit recommendations to the City leadership for appropriate action.

In this appendix we discuss several other considerations and policy issues that may impact the amount estimated here, some may increase the amount, while others may decrease the amount.

Unfunded Liabilities

The City has substantial unfunded liabilities for retirement, workers compensation and unpaid leave balances. The City needs to determine to what extent they constitute cost of providing services and how much money if any should be recovered for prior years and how much should be included as part of full costs for recovery from future fees.

Including a portion of these liabilities will increase the amount owed to the General Fund. However, it is recommended that any amount collected for these liabilities should be set aside to pay down the liabilities. As of June 30, 2019 the unfunded liability for LACERS alone was almost 6 billion, while it is amortized and is expected to be recovered at some point in the future, it will take decades for it to be fully recovered

Unfunded liabilities cont.

It is only reasonable to have the recipients of service pay for the portion that relates to the cost of service they receive. otherwise the tax payers would have to pay it, it is recommended that the City discuss this matter with the actuary and develop an appropriate rate for recovery from fee payers.

Review and refine alternate CAP rates

In developing the alternate CAP rates the intent was to develop a framework. City would need to spend time and resources to verify and refine the rates and develop rates based on actual costs,

Other unknown factors

It is possible that there are other factors that we do not know about, for example it is possible though not likely that the amount of unearned revenue shown in audited statements is incorrect. Even though, financial statements and budgets should include all relevant information to ensure transparency and credibility of financial information it is possible even though not likely that there are other liabilities, obligations or commitments that are not recorded and reflected in budget or CAFR.

Revenues recorded in the General Fund

City collects and records some Building and Safety revenues in the GF these fees primarily relate to fines, which we believe are the result of City's police powers to mitigate the impacts of the fee payer's activity on the community and not subject to the provisions of the Government code section 66014 (a), however an adjustments may need to be made for the costs towards collecting these. An estimate of around 10% of fees should be a reasonable estimate.

City needs to confer with the City Attorney on the appropriate mechanism and percentage to address this matter.

Other Considerations

System Development Fees

Decades ago, the City approved a System Development Fee to pay for upgrading systems, which is also collected and accounted for in the Building and Safety Permit Fund. The fees collected and related costs are included in the total fees and costs for Building and Safety Operations in BSPF. Between Fiscal Years 2011 and 2019 the total of revenue source for system development in the Building and Safety Permit Fund is about \$90 million. Even though, the costs incurred for system development are not readily identifiable, but it appears that the costs may be much lower than the fees collected.

The City needs to conduct an analysis and discontinue the System development fees if it is no longer needed because this fees may also be subject to the requirements of State Law (California Government Code section 66014(a)). The original ordinance had a sunset clause to eliminate the fee when not needed.

The City needs to confer with the City attorney to explore its options and if the City can offset the system development fees with other fees to make up for the lack of fee increases that were supposed to happen but did not.

Need for fee increase?

There has been no fee increase since 2010 despite Council direction pursuant to ordinance 18068

In 2010 the ordinance No. 18068 amended Article 1 of Chapter IX of Los Angeles Municipal Code (LAMCC) and added a new Section 91.107.1.1, which reads:

In 2010 the ordinance No. 18068 amended Article 1 of Chapter IX of Los Angeles Municipal Code (LAMCC) and added a new Section 91.107.1.1, which reads:

Annual Review of Fees; The fees in this code **shall** be reviewed annually by the Superintendent of Building. Beginning on July 1, 2010 and thereafter on July 1 of every year, the amount of fee in this code **shall** be adjusted as follows: (emphasis added)

Per the new LAMCC the fees were supposed to be adjusted on July 1 every year based on Consumer Price Index-All Urban Consumers in the Los Angeles area as published by US Government Bureau of Labor Statistics.

No adjustments have been made to the fees since 2010. Since 2010 the CPI has increased by more than 20%. If the fees were increased as directed by the Council, then there would be additional moneys available.

It is hard to justify a fee increase when the fund had stockpiled more than \$300 million. After all the issues are resolved and if it is determined that the fees need to be increased to recover full cost the City may want to revisit this issue.

The City also needs to put processes in place to ensure that Council directions are followed and implemented and if the fees are supposed to be increased, they are evaluated and appropriate increase implemented in a timely manner.

Note and Disclaimer

The report should be used in totality to maintain the right and appropriate context

Acknowledgement

The images used in this report were obtained from the internet. We thank those who contributed to their creation. This report is not for sale and we do not claim any credit for the images

Together:

We are Strong

We are Resilient

We will Rise and Shine Again

For a Brighter Future

Our City is Hurting

Let us

Collaborate to Help

The Great City of Los Angeles and the Angelenos

This report is inspired by the vision of the Controller
and

Influenced by every member of the City team who
dares to care and wishes to make a difference
in the lives of those we are committed to serve



Respectfully,
City's Disruptive Innovation Team

April, 2020