Memorandum
City of Lawrence
City Auditor

TO: Members of the City Commission

FROM: Michael Eglinski, City Auditor

CC: Tom Markus, City Manager
Diane Stoddard, Assistant City Manager
Casey Toomay, Assistant City Manager

Date: May 30, 2017

RE: Audit Recommendation Follow-Up May 2017

Following-up on performance audit recommendations provides the City Commission with information on management's efforts to implement recommendations. This report covers recommendations from five performance audits: Pavement Data Use, Cash Handling, RCP Infrastructure, Protecting Personally Identifiable Information, and Economic Development. City Code requires follow-up reporting.

Figure 1 Implementation summary

Status	Number of Recommendations
Implemented	9
Not-Implemented	6
In Progress	7

Figure 2 summarizes the status of all of the recommendations. See Appendix A for the City Manager's written update on recommendation status.

Action item

The City Commission can direct the City Auditor to "close" the audit recommendations categorized as "implemented" or "not implemented." Closed recommendations won't be included in future follow-up.

Figure 2 Summary of recommendations

Performance audit	Recommendation	Implemented	Not Implemented	In Progress	Undetermined
Pavement Data Use (2011)	Develop a maintenance policy for city streets paved in brick and with pavement over brick.		☑		
Cash Handling (2012)	Develop training for employees and managers responsible for handling cash.			☑	
RCP Infrastructure (2014)	Provide training to city employees who handle cash			☑	
Protecting Personally Identifiable Information (2015)	The City Manager should develop a city-wide record retention schedule.			☑	
	The City Manager should work with the Information Technology Department and the City Attorney's Office to establish a framework for safeguarding personally identifiable information.			☑	
	The City Manager should work with the Information Technology Department and the City Attorney's Office to provide training and communication to employees about the framework.			☑	
	The City Manager should work with the Information Technology Department and the City Attorney's Office to establish a way to monitor how well the safeguards have been implemented.			☑	
	The City Manager should work with the Information Technology Department and the City Attorney's Office to develop a plan to respond to a data breach.			☑	
Economic Development (2016)	The City Manager's Office should develop written procedures to address "pirating" and unfair advantage.		☑		
	The City Manager's Office should ensure the Public Incentives Review Committee schedules annual reviews of the City Neighborhood Revitalization Area policy as required by resolution.	☑			
	The City Manager's Office should establish a control to ensure disclosure requested of applicants is collected and disclosed.	☑			
	The City Manager's Office should work with the Finance Department to include payments to the City related to economic development in the City's billing system.	☑			

		Implemented	Not Implemented	In Progress	Undetermined
	The City Manager's Office should develop written procedures to address incentives other than those incentives established by state law.		☑		
	The Finance Department should develop procedures for Utilities Department fee and charge rebates and waivers.		☑		
	The City Manager's Office should develop procedures to guide activities before an applicant submits a formal application.	☑			
	The City Manager's Office should analyze risks and uncertainties related to economic development projects and communicate the results of the analysis to decision-makers.		☑		
	The City Manager's Office should ensure the annual reports go to the Public Incentives Review Committee and the City Commission in accordance with the deadlines established in the City Code.	☑			
	The City Manager's Office should take steps to verify some of the self-reported data used in the annual compliance report.		☑		
	The City Manager's Office should develop procedures to require performance agreements for all incentives.	☑			
	The City Manager's Office should measure and report on the City's three overall goals for economic development.	☑			
	The City Manager's Office should work with the City Attorney to include audit access language in performance agreements.	☑			
	The City Manager's Office should propose for City Commission consideration application fees consistent with the City's fee policy.	☑			
		Implemented	**Not Implemented**	**In Progress**	**Undetermined**

Recently implemented recommendations

Management implemented nine recommendations since the October 2016 audit recommendation follow-up memo.

Economic Development (2016)

Two recommendations were addressed when the City Commission eliminated the required annual review of the Neighborhood Revitalization Areas (NRA) policy and deadlines for annual reporting to the Public Incentives Review Committee and City Commission.[1] The related recommendations are considered implemented.

The City began using the miscellaneous billing process for economic development application fees. The City will be able to review outstanding invoices on a regular basis and follow up as needed when payments are delinquent. Implementing the recommendation to use the billing system strengthens controls over receiving and recording fees related to economic development.

The City Commission's adoption of a new economic development policy clarified the process for the time before an applicant submits a formal application. The performance audit found that the pre-application process could involve preliminary cost-benefit analysis and conditional offers of incentives, but wasn't guided by procedures. Implementing the recommendation increases transparency about the City's process.

The City Commission's adoption of a new economic development policy clarifies that staff are responsible for ensuring complete applications. This should help ensure that applications include the disclosure information requested. The performance audit noted that after the city began requiring disclosure information in 2103. Applicants provided the information, but about two years after the requirement was put in place, only one of the next five applicants provided the disclosure information. Applicants provide disclosure information including the company's form of organization, tax delinquencies, litigation, bankruptcy, and defaults. Implementing the recommendation helps to ensure that City Commissioners, residents and staff have information to inform decisions about granting incentives.

The City Commission's adoption of a new economic development policy clarifies the requirement that every economic development incentive granted by the city shall have a performance agreement. The performance audit found that some incentives didn't have performance agreements. Implementing recommendation improves transparency, helps monitor incentives, and helps evaluate the success of incentives.

The 2016 annual report on economic development includes an appendix with economic indicators that address the City's three economic development goals. The goals are related to growth in employment, tax base, and income. The performance audit noted that the city had established overarching goals for economic development, but was not reporting on those goals. Implementing the recommendation improves monitoring and provides context to understand the City's economic development efforts.

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[1] Ordinance 9325 and Resolution 7184

The new economic development policy requires that performance agreements include audit language to permit access to certain records to monitor compliance with the agreements. Audit access language can address keeping records, providing access to those records, and requiring subcontractors to meet the requirements. Implementing consistent audit language clarifies expectations and improves the City's ability to monitor or audit incentives.

The City Commission's adoption of new economic development application fees addresses the recommendation. Non-refundable application fees range from $500 to $2,500 depending on the incentive. The City can also require a funding agreement where the applicant agrees to cover the actual processing costs if it appears the cost will exceed the application fee. The City will return half of the application fees if the application is not considered. The recommendation was intended to ensure that the fees were set with consideration of the costs involved.

Recommendations not implemented

Based on the follow-up, six recommendations are considered not implemented.

Pavement Data Use (2011)

Staff developed guidelines for maintaining streets that are asphalt surface over bricks and that are brick surfaced, but the guidelines were not adopted. The performance audit found that maintenance of these streets wasn't driven by maintenance policies. Maintenance of other city streets was based on pavement condition index (PCI) scores. Asphalt-over-brick and brick-surfaced streets were in worse condition, as measure by the pavement condition index, than the rest of the street system. These streets are a relatively small part of the city's street system and are concentrated in a specific part of town. Implementing the recommendation would require management to approve the draft guidelines.

Draft Maintenance Guidelines

Staff met with neighborhood groups, the Historic Resources Commission, and shared draft guidelines with the City Commission. The draft guidelines for street maintenance set pavement condition index (PCI) goals based on the type of street and defined maintenance approaches. For example, the goal for residential streets would be to maintain a PCI score above 55. The guidelines spell out how the city would maintain the street depending on the surface (asphalt over brick or brick surface) and the measured PCI.

Economic Development (2016)

The City hasn't developed procedures to address unfair advantages over existing businesses and piracy of businesses already in Kansas. The performance audit found that the application review process didn't address these two policy elements. Best practices include analyzing the impact of projects on existing business. Implementing the recommendation would involve deciding what data collect and provide to help inform the City Commission's decisions about the policies of avoiding unfair advantage and pirating.

The City's economic development policy addresses the major incentives, but the City hasn't develop procedures for other types of incentives that have been used. The performance audit found that the city hadn't developed procedures to address incentives such as training grants,

parking passes for employees, rebates of fees, and reimbursing relocation expenses. The City hadn't developed procedures for consistently reviewing these types of incentives. Implementing the recommendation would involve developing guidelines for the process for considering and monitoring these incentives.

The City has not developed procedures for rebating and waiving Utilities Department fees and charges. The performance audit found that the rebates and waivers were being used as incentives without procedures to ensure compliance with Utilities Department bond requirements. Implementing the recommendation would involve drafting procedures and reviewing them with bond counsel. Having written procedures is important for consistency and continuity.

The City has not developed a practice of analyzing and communication risks related to economic development projects. The performance audit found that the process for evaluating applications didn't require systematically identifying risks and uncertainty and communication those to decision-makers. Risks assessment is a best practice. Implementing the recommendation could involve holding brainstorming meetings and tracking issues that have appeared historically. The recommendation was intended to provide information for making informed decision and help the city achieve desired outcomes of economic development.

Risks inherent to economic development projects

The Government Finance Officers Association identified a number of risks inherent to economic development projects that include:

- **Completion**: complete project failure; not achieving results within timeframe or to the desired outcome; an external organization's failure to perform.

- **Financial-related**: revenues falling short; cost overruns; unexpected operation, maintenance or capital costs after project completion; debt limitations; and debt instruments.

- **Regulatory/legal**: jurisdictional authority; negative legal actions against the government related to a project; liability and insurance risks; legislation with potential adverse outcomes.

- **Operational**: negative environmental impacts; displacement of other businesses or residences.

GFOA recommend identifying and evaluating potential risks. GFOA described several simple methods to identify risks, including holding brainstorming meetings and identifying risks based on experience with previous projects. Identifying risks can also involve more complex analysis, such as feasibility analysis and analysis strengths, weaknesses, opportunities and threats.

Once risks have been identified, assessing the risks can involve considering both the likelihood that the risk would occur and the impact. Simple ratings, such as low/medium/high can be assigned to both the likelihood and impact.

The City has not developed steps to verify some of the self-reported data used to monitor the success of economic development incentives. The performance audit found that the City relied on self-reported data from businesses that received incentives. A best practice would be to take steps to verify some of the data. Implementing the recommendation could involve steps such as interviewing the person who prepared the information to understand how they compiled the information and ensured its reliability; ensuring that the business retains required records; or spot checking some of the information. The intent of the recommendation is to enhance the credibility of the reported data.

Scope, method and objectives

Following-up on the status of performance audit recommendations provides the City Commission with information about management's efforts to implement audit recommendations. The City Code requires the City Auditor to follow-up on audit recommendations no later than 6-months after issuing an audit, to determine that corrective action was taken and is achieving the desired results. City Code requires that the auditor inform the City Manager and the City Commission of the results of the follow-up.

The City Auditor provided the City Manager with a list of audit recommendations on February 10, 2017, and asked management to provide updates by March 20. The City Manager provided an update on March 23. The recommendation follow-up covered open recommendations for reports released more than 120 days prior to February 10, 2017. For recommendations that weren't covered in the City Manager's response, the City Auditor reviewed the follow-up memo from October 2016 and conducted limited interviews with staff to understand the status.

The auditor compiled the information but did not verify the information provided by management. The auditor did not verify that policy and procedure recommendations are being followed. For each recommendation, the auditor made a judgment about the status of the recommendation.

Figure 3 Implementation Status Guidelines

Status	Indicator
Implemented	Management describes steps taken to implement the recommendation.
Not implemented	Management asserts that the recommendation will not be implemented or has not taken steps to implement the recommendations.
In progress	Management describes progress toward implementing the recommendation.
Undetermined/pending	Status cannot be determined, for example, because the recommendation requires future actions or because management describes steps that will be taken in the future.

The City Auditor, with the City Commissions' direction, will "close" a recommendation and exclude it from future follow-up reports. Open recommendations will be included in future follow-up reports unless "closed" by the City Commission.

The follow-up information on the status of implementing recommendations was not conducted as a performance audit under *Government Auditing Standards*.

The City Auditor shared a draft of this report with the City Manager.

Appendix A: City Manager's update on audit recommendation status

City of Lawrence
City Manager's Office

TO: Michael Eglinski, City Auditor
FROM: Thomas M. Markus, City Manager
CC: Diane Stoddard, Assistant City Manager
                Casey Toomay, Assistant City Manager
                Brandon McGuire, Assistant to the City Manager
DATE: March 23, 2017
RE: Response to Audit Recommendation Follow-Up Report March 2017

The following is provided in response to questions posed on the status of outstanding audit recommendation items as of the end of February 2017. My responses are noted in italics. There are a number of items that I am recommending be retired for follow-up purposes.

Pavement Data Use
- **Develop a maintenance policy for city streets paved in brick and with pavement over brick.**

  Draft brick street maintenance restoration [guidelines](#) were presented to the City Commission on January 21, 2014. The Historic Resources Commission (HRC) reviewed the draft guidelines on May 15, 2014 and provided suggested revisions. Further review by neighborhood associations, the Lawrence Preservation Alliance and the HRC, along with final review by the City Commission, is anticipated. Prior to that occurring, the City Commission should direct whether this is a priority given other goals. Staff suggests closing this recommendation.

Cash Handling
- **Develop training for employees and managers responsible for handling cash.**

  Finance Department staff is in the process of coordinating this cash handling review and plan to have this review and training done in 2017.

RCP Infrastructure

- **Provide training to city employees who handle cash.**

  See prior response to Cash Handling recommendation.

Protecting Personally Identifiable Information
- **The City Manager should develop a city-wide record retention schedule.**

- **The City Manager should work with the Information Technology Department and the City Attorney's Office to establish a framework for safeguarding personally identifiable information.**

- **The City Manager should work with the Information Technology Department and the City Attorney's Office to provide training and communication to employees about the framework.**

- **The City Manager should work with the Information Technology Department and the City Attorney's Office to establish a way to monitor how well the safeguards have been implemented.**

- **The City Manager should work with the Information Technology Department and the City Attorney's Office to develop a plan to respond to a data breach.**

  Staff has begun work on an Incident Response Policy, however, given other more pressing priorities, we have not been able to fully review this issue or develop policy recommendations. We did purchase a cyber-liability insurance policy in December of 2016 to cover the City in the event of a breach.

Economic Development

- **The City Manager's Office should develop written procedures to address "pirating" and unfair advantage.**

- **The City Manager's Office should ensure the Public Incentives Review Committee schedules annual reviews of the City Neighborhood Revitalization Area policy as required by resolution.**

- **The City Manager's Office should establish a control to ensure disclosure requested of applicants is collected and disclosed**

- **The City Manager's Office should work with the Finance Department to include payments to the City related to economic development in the City's billing system.**

- **The City Manager's Office should develop written procedures to address incentives other than those incentives established by state law.**

- **The Finance Department should develop procedures for Utilities Department fee and charge rebates and waivers.**

- **The City Manager's Office should develop procedures to guide activities before an applicant submits a formal application,**

- **The City Manager's Office should analyze risks and uncertainties related to economic development projects and communicate the results of the analysis to decision-makers.**

- **The City Manager's Office should ensure the annual reports go to the Public Incentives Review Committee and the City Commission in accordance with the deadlines established in the City Code.**

- **The City Manager's Office should take steps to verify some of the self-reported data used in the annual compliance report.**

- **The City Manager's Office should develop procedures to require performance agreements for all incentives.**

- **The City Manager's Office should measure and report on the City's three overall goals for economic development.**

- **The City Manager's Office should work with the City Attorney to include audit access language in performance agreements.**

- **The City Manager's Office should propose for City Commission consideration application fees consistent with the City's fee policy**

The City's economic development policies were completely overhauled in December 2016 after an extensive review process by the City Commission and various advisory boards and committees. A number of recommendations were addressed and resolved during that process, such as the requirement of performance agreements for incentives, audit language, the collection of applicant information on the application form, fees, etc. Additionally, the requirement naming a firm date for receipt and review of the annual economic development report was changed, along with the removal of the firm requirement to review the Neighborhood Revitalization Act (NRA) policy annually. Staff does plan on including various economic metrics in the annual economic development report for the 2016 year, which is currently being drafted. The staff response provided to accompany the audit is also still relevant for all remaining points. The response is located on pages 26-30 of the Economic Development Audit Report. Staff therefore recommends that all recommendations be retired by the City Commission.