



**Office of the City Auditor**

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**Report to the City Council  
City of San José**

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**AN AUDIT OF THE EMERGENCY  
COMMUNICATION SYSTEM  
SUPPORT FEE**

**Opportunities Exist For The City To  
Improve The Calculation, Allocation,  
Assessment, And Collection Processes For  
The Emergency Communication System  
Support Fee**

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**Report 08-01  
April 2008**

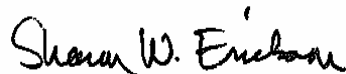
April 8, 2008

Honorable Mayor and Members  
of the City Council  
200 East Santa Clara Street  
San Jose, CA 95113

Transmitted herewith is the report *An Audit of the Emergency Communication System Support Fee*. This report is in accordance with City Charter Section 805. An Executive Summary is presented on the blue pages in the front of this report. The City Administration's response is shown on the yellow pages before the appendices.

I will present this report to the *Public Safety, Finance & Strategic Support Committee* at its April 17, 2008 meeting. If you need any additional information, please let me know. The City Auditor's Office staff members who participated in the preparation of this report are Steve Hendrickson, Ruth Garcia Merino, and Chris Constantin.

Respectfully submitted,



Sharon W. Erickson  
City Auditor

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## **Executive Summary**

In accordance with the City Auditor's 2007-08 Workplan, we performed an audit of the City's Emergency Communication System Support Fee (ECSS Fee). We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objectives. We limited our work to those areas specified in the Objectives, Scope and Methodology section of this report. The City Auditor's Office thanks the management and staff of the City Manager's Budget Office, the Finance Department, San José Police Department and the City Attorney's Office for their cooperation during the audit.

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### **Finding I**

#### **Opportunities Exist For The City To Improve The Calculation, Allocation, Assessment, And Collection Processes For The Emergency Communication System Support Fee**

In 2004, the City of San Jose (City) established an Emergency Communication System Support Fee (ECSS Fee). The ECSS Fee is a flat monthly fee to cover most of the cost of maintaining the Emergency Communications Center's (ECC) function that enables telephone subscribers to access the City's emergency communications system. The telephone lines of LifeLine telephone customers; non-profit hospitals and educational organizations; government agencies; and payphones are exempt from paying the ECSS Fee. The costs associated with these exempt telephone lines are funded by the General Fund. Furthermore, the ECSS Fee covers only the ECC's eligible costs.

Since January 2005 through June 2007, the ECSS Fee has funded \$49 million of ECC costs, and the General Fund has funded about \$13 million. We identified that the ECSS Fee can fund an additional \$857,000 for past and current year ECC costs.

We evaluated the City's ECSS Fee calculation, allocation, assessment, and collection processes. Although most of the processes are in accordance with the San Jose Municipal Code (Municipal Code), we found some exceptions. Specifically, we found that:

- Better sources of data exist for the number of telephone customers exempt from the ECSS Fee, particularly the number of LifeLine and payphone exemptions. If the Budget Office were to begin using updated exemption information to determine the amount of ECC costs that should be paid for from the fees collected, an additional \$607,000 would be available in fiscal year 2007-08. This also means that General Fund spending on the ECC could be reduced by \$607,000.
- The City estimates that a percentage of the ECC's costs are non-911 activities and are therefore not funded by the ECSS Fee. The City cannot locate documentation as to how it developed this percentage of non-911 activity, or "ineligible operating costs rate". Also, the Budget Office does not use the ineligible operating costs rate when it funds overtime expenses with the ECSS Fee as it does with the other personal services operating costs. By reducing the amount of ECC overtime cost, the amount funded by the ECSS Fee is reduced by \$44,703, \$45,077 and \$41,314 for fiscal years 2005-06, 2006-07 and forecast 2007-08, respectively.
- By using a calculation methodology more closely aligned with provisions of the Municipal Code, the Budget Office can apportion a greater share of the cost of the ECC to ECSS Fee revenues, an additional \$113,000 and \$268,000 from fiscal years 2005-06 and 2006-07, respectively, rather than to the General Fund.

Based on our audit, we found that the City should make the following adjustments to the key components of the ECSS Fee calculation:

**Exhibit 4 Summary Of Key Components That Increase/(Decrease) The Amount Of ECSS Fee Funding And Additional Amounts Available To Reimburse The General Fund**

<b>Key ECSS Fee Components</b>	<b>2005-06</b>	<b>2006-07</b>	<b>Forecast 2007-08</b>	<b>Total</b>
<b>Decrease In LifeLine Exemptions</b>	n/a	n/a	\$570,000	\$570,000
<b>Decrease In Payphone Exemptions</b>	n/a	n/a	\$37,000	\$37,000
<b>Overtime Costs That Should Not Be Funded By The Fee</b>	(\$44,703)	(\$45,077)	(\$41,314)	(\$131,094)
<b>Methodology To Apportion Costs</b>	\$113,079	\$267,990	n/a	\$381,069
<b>Net Findings</b>	\$68,376	\$222,913	\$565,686	\$856,975

We also found that

- The City is at risk of funding ineligible indirect costs with the ECSS Fee;
- Service providers erroneously billed subscribers that are exempt under the Municipal Code from having to pay;
- Service providers do not register with the City as required; and
- Service providers do not provide information required under the Municipal Code.

Better sources of data for the number of LifeLine exemptions, payphone exemptions, as well as the more precise methods for calculating eligible salary and overtime operating costs, indirect costs, and the basis for allocating ECSS Fee revenues would improve the calculation of the ECSS Fee. To ensure that it has the most up to date information available, the Budget Office should annually request the number of LifeLine exemptions from the California Public Utilities Commission (PUC), and the number of payphones from the Santa Clara County Communications Department. Furthermore, the Budget Office should also ensure that only that portion of overtime considered as eligible operating costs is included in the calculation of the amount to be funded by the ECSS Fee. In addition, the City Manager's Office should perform a study to determine the amount of time ECC staff spends on 911-related activities to determine the portion of staff costs that are eligible operating costs. Furthermore, we recommend that the Finance Department conduct a review of ECC indirect costs to ensure indirect costs are allocated in compliance with the Municipal



Code and determine the necessity for a separate ECC indirect cost rate. By adopting the actions described above, the City will be able to improve the ECSS Fee calculation and allocation processes.

We found the City can further improve its calculation of the ECSS Fee by establishing a process to ensure service providers do not charge the ECSS Fee to exempt City of San José phones. To make sure the City communicates timely information to service providers, the City should annually obtain and verify current service provider registrations from each service provider and annually provide relevant instructions and documents necessary for implementing the ECSS Fee. To maintain Municipal Code compliance, the City should annually identify and request from service providers the information necessary to comply with annual fee requirements, maintain an annual fee cap adjustment process, and ensure service providers maintain controls over billing, collecting, and remitting the ECSS Fee. Lastly, the City can improve their regular review of the ECSS Fee by updating the subscriber fee cap annually, and conducting a review to determine whether the fee rates for trunk line fees continue to reasonably reflect the estimated ECC workload relative to access lines.

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## RECOMMENDATIONS

We recommend that the Budget Office staff:

**Recommendation #1**      **Annually obtain the most up-to-date number of LifeLine telephone customers from the California Public Utilities Commission. (Priority 3)**

**Recommendation #2**      **Annually obtain the number of payphones in the City of San Jose from the Santa Clara County Communications Department. (Priority 3)**

We recommend that the City Manager's Office:

**Recommendation #3**      **Perform a study to determine the amount of time ECC staff spends on 911-related activity; and officer-initiated and other non-911-related activity to determine the portion of staff costs that are 911-related and can be funded with the ECSS Fee in compliance with the Municipal Code definition of eligible operating costs. (Priority 3)**

We recommend that the Budget Office:

**Recommendation #4**      **Include only that portion of overtime considered as eligible operating costs in the calculation of the amount to be funded by the ECSS Fee. (Priority 2)**

**Recommendation #5**      **Use the Municipal Code definition of “eligible operating costs” as the amount of ECSS Fees to transfer to the General Fund. (Priority 2)**

We recommend the Finance Department:

**Recommendation #6**      **Conduct a review of ECC indirect costs to ensure indirect costs are allocated in compliance with the Municipal Code and determine the necessity for a separate ECC indirect cost rate. (Priority 2)**

**Recommendation #7**      **Establish a regular monitoring process to ensure service providers do not charge the ECSS Fee to exempt City of San José phones. (Priority 3)**

**Recommendation #8**      **Inform the identified education organization of the Municipal Code exemption. (Priority 3)**

**Recommendation #9**      **Obtain current registrations from each service provider in accordance with the form prescribed by the Director of Finance, establish an annual process of verifying registrations, and annually provide relevant instructions and documents necessary for the ECSS Fee program to registered agents. (Priority 3)**

**Recommendation #10**      **1) Annually identify and request from service providers the information identified in the Municipal Code and such additional information as Finance determines necessary for it to perform the fee review requirements set forth in the Code,**  
**2) Work with service providers to determine the documentation and review necessary to assess the strength of controls over billing, collecting, and remitting the ECSS Fee,**  
**3) Assess if service provider controls ensure proper billing, collecting, and remitting the ECSS Fee, and**

- 4) **If the service providers are unable or unwilling to provide the information the City seeks, the City should explore whether other options or sources are viable ways to comply with Municipal Code provisions. (Priority 3)**

We recommend the Finance Department:

**Recommendation #11**      **Maintain a fee cap updating process and update the service providers on an annual basis. (Priority 3)**

**Recommendation #12**      **Conduct a review to determine whether the fee rates for trunk lines continue to reasonably reflect the estimated ECC workload relative to access lines. (Priority 3)**

We recommend the City Administration:

**Recommendation #13**      **Exercise its right to an onsite compliance audit of select service providers, if the City does not obtain sufficient information and documentation. (Priority 3)**

# Introduction

In accordance with the City Auditor's 2007-08 Workplan, we performed an audit of the City's Emergency Communication System Support Fee (ECSS Fee). We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objectives. We limited our work to those areas specified in the Objectives, Scope and Methodology section of this report. The City Auditor's Office thanks the management and staff of the City Manager's Budget Office, the Finance Department, San José Police Department and the City Attorney's Office for their cooperation during the audit.

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## Background

### *Establishment Of The Emergency Communication System Support Fee*

In August 2004, the City Council approved the establishment of an Emergency Communication System Support Fee (ECSS Fee) to "*recover the cost of providing adequate and reliable 911 emergency communication system ....*" The City Council applied the ECSS Fee to residential, commercial, and wireless subscribers maintaining telephone services within the City of San José, with limited exemptions for specified subscribers. According to City staff, the City adopted the cost recovery fee in part due to the State's decision to transfer responsibility for handling cellular phone calls from the California Highway Patrol to the City's Emergency Communication Center (ECC), which resulted in a significantly increased workload. Further, the City believed an ECSS Fee was the most practical and equitable mechanism to provide revenue needed to maintain an adequate and reliable 911 emergency communication system. The City hired a consultant to explore the feasibility of an ECSS Fee prior to implementation.

The ECSS Fee is a charge for individual landline and wireless access lines and trunk lines where the physical connection or the primary use of the lines is in the City of San José. The San José Municipal Code (Municipal Code) defines an access line as "*any connection from a customer within the geographic boundaries of the city of San José to a provider of local telephone service offered to the public for compensation.*" The code section includes mobile telephones where the place of

primary use is with the City of San José. The Municipal Code defines a trunk line as “*a line between a service supplier’s switching device and a private branch exchange or automatic call distributing system, or other similar device, at a telephone subscriber location.*” In other words, an access line is a single connection between a telephone company and a single location. A trunk line is a single connection between a telephone company and location with the capacity to serve several extension phones at the location. The City utilizes an estimate of 7.5 extension lines per trunk line. Some subscribers have high capacity trunk lines, which accommodate significantly more than the average of 7.5 extension lines per trunk. High capacity trunks are primarily or partially utilized for data transmission.

The City established two monthly fees of \$1.75 and \$13.13, respectively, for each access line and trunk line. The City does not have a separate fee for high capacity trunks. In 2006, the City Council extended the fees to June 30, 2009.

In fiscal year 2006-07, the City collected over \$23 million in ECSS Fees to support the ECC’s \$21 million in eligible operating costs. In 2007-08, the ECC is currently staffed with a total of 209 Police and Fire Department full-time equivalent positions and is projected to have \$25 million in eligible operating costs.

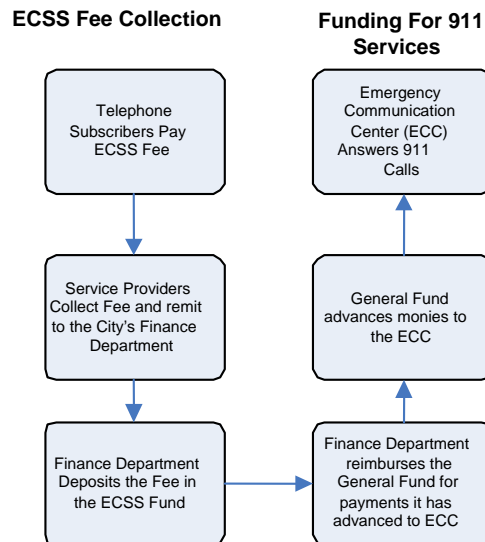
*ECSS Fee  
Functional  
Organization*

The Finance Department handles the assessment and collection processes. The Budget Office handles the calculation and allocation processes. Finally, the City Attorney’s Office handles non-disclosure and confidentiality agreements and also monitors pending litigation involving other jurisdictions. There is currently no pending litigation challenging the City of San Jose’s ECSS Fee.

*ECSS Fee Funding  
Process*

The ECSS Fee is collected from telephone subscribers by telephone providers on behalf of the City. The Finance Department deposits the fees into the ECSS Fee Fund. The General Fund initially pays for the ECC costs. Monthly, the Finance Department transfers the ECSS Fees to the General Fund to reimburse the General Fund for eligible ECC costs. Exhibit 1 shows this funding process.

## Exhibit 1 Emergency Communication System Support Fee Funding Process



Source: City Auditor prepared.

### The Emergency Communication System Support Fee Calculation And Allocation Processes

The City Manager's Budget Office (Budget Office) performs the ECSS Fee calculation and allocation processes. The Budget Office and ECSS Fee Consultant (Consultant) developed the recommended ECSS Fee rates that the City Council adopted in August 2004. The Budget Office also made an initial revenue forecast. The initial revenue forecast calculation was equal to the amount of eligible Emergency Communication Center (ECC) expenditures less the amount allocated to exempt phone lines. The Budget Office has made subsequent annual revenue forecasts based on historical fee revenue collections. Also, the Budget Office annually projects the ECC operating costs. Furthermore, the Budget Office annually documents the actual revenue received and the actual operating costs for the prior fiscal year.

### ECSS Fees

The initial ECSS Fee rate calculation was performed by the Budget Office. The ECSS Fee was set at an amount sufficient to cover eligible operating costs, which equaled the revenue forecast. Subsequent revenue forecasts have been performed based on historical collections. On August 31, 2004, the City Council approved two monthly fees of \$1.75 and \$13.13, for each access and trunk line, respectively. The fee rates have not changed.

According to the Municipal Code Section 8.20.210 A., “*The amount of the fee imposed by this section shall be established by resolution of the city council and shall be paid, on a per-line basis, by the person paying for such local telephone service.*”

The fee rate calculation is shown in the Initial ECSS Fee Rate Calculation Revenue Forecast section of this report.

*Exemptions,  
Exclusions And Fee  
Caps*

The City’s ECSS Fee provides for exemptions, exclusions, and a cap on the fee to ensure an appropriate fee policy. The Budget Office annually revises its exemptions projections.

Exemptions

The City Manager described the exemptions in a May 2004 memorandum (ECSS Fee Memorandum) to the City Council regarding the ECSS Fee. He stated that the City estimated the revenue from the proposed fee assuming the following four exemptions. If the City Council were to direct additional exemptions, the rate per line per month would not change; however, the total revenue collected would decline.

Specifically, he described the exemptions as follows:

- Lifeline Customers – customers who are designated as disadvantaged and limited income users who received lower phone rates;
- Governmental Agencies – State, local, and Federal organizations;
- Educational Exemption – Schools and universities; and
- Coin and Pay Phones – Public phones charging a fee for use.

The Municipal Code Section 8.20.220 defines exemptions as follows:

*Nothing in this chapter shall be construed as imposing a fee upon the access lines of:*

- A. *A lifeline customer of a service supplier; or*
- B. *A telephone corporation; or*
- C. *Coin-operated telephones; or*

- D. *A nonprofit hospital which is exempt from federal income tax under Section 501(a) of the United States Code; or*
- E. *A nonprofit educational organization which is exempt from income tax under Section 501(a) of the United States Code; or*
- F. *Any person when imposition of such fee upon that person would violate the Constitution of the United States or that of the State of California or preemptive federal or state law; or*
- G. *City of San José, county of Santa Clara, state of California and United States government offices.*

Exclusions

The City Manager's ECSS Fee Memorandum also discussed the exclusions to the ECSS Fee. San Jose State University (SJSU) phones are excluded from the fee because SJSU has its own public safety answering point (PSAP) within the City's boundaries. Therefore, SJSU 911 calls placed on phones at the university are not answered by the City's dispatch center, but by SJSU's own dispatch center. As a result, SJSU phone lines are an automatically excluded group. Voice over Internet Protocol calls are also excluded because this technology does not always have the ability to initiate 911 calls.

Fee Cap

There is a \$20,000 cap on the ECSS Fee from any one subscriber. According to the Municipal Code: *No telephone subscriber shall be required to pay fees in excess of twenty thousand dollars per account per service location in any calendar year. The cost of wireless telephone services shall not be considered for purposes of the fee cap established by this subsection, regardless of whether the service location is also a primary place of use for a wireless line. The amount of the cap established by this subsection shall be adjusted annually by the consumer price index: all urban consumers for the San Francisco/Oakland/San José area for all items as reported by the United States Bureau of Labor Statistics.*



Initial ECSS Fee Rate Calculation And Revenue Forecast

The ECSS Fee revenue is collected by the telephone companies from telephone subscribers. The Budget Office used information from the State of California’s Public Utilities Commission, (PUC), which regulates phone companies, to develop the ECSS fee and initial revenue projection. The Budget Office also used California Department of Finance population forecasts to determine the overall ratio of total State population to City population. Specifically, to determine how many lines are located within the City, the Budget Office used the California Department of Finance population forecasts to determine the overall ratio of total State population to City population. The Budget Office also determined the rate of exemptions from the Statewide data. The Government and Education exemptions were determined using State and County of Santa Clara data.

The following chart shows the City’s initial calculation of phone lines and exemptions.

**Exhibit 2 Initial Calculation Of City Of San Jose Phone Lines And Exemptions**

<b>Factor</b>	<b>Calculation</b>	<b>Amount</b>
<b>Calculation of Lines in San Jose Based on Statewide Line and Population Data</b>		
Lines Statewide per CPUC		41,800,000
CA Population on 1/1/03 per CA Dept of Finance		35,591,000
Lines/capita	41,800,000 lines/35,591,000 pop	1.174
City of San Jose 2004-05 Population Estimate		926,241
Estimated Number of Telephone Lines	926,241 * 1.174	1,087,407
Lines served by SJSU PSAP		7,564
All lines except for SJSU lines	1,087,407 lines less 7,564 SJSU lines	1,079,843
Lines-Annualized	1,079,843* 12	12,958,115
<b>Calculation of Percent of Exempt Lines</b>		
Statewide LifeLines per CPUC		3,300,000
LifeLine Exemption Percentage	3,300,000 State LifeLines/41,800,000 State lines	7.89%
Statewide Pay Phones per CPUC		255,001
Pay Phones Percentage	255,001 State Pay Phones /41,800,000 State lines	0.61%
Government Exemption Percentage		1.49%
Education Exemption		2.28%

Source: Based on City Manager’s May 2004 Memorandum.

As shown in Exhibit 2 above, the LifeLine, pay phones, government and education exemptions are 7.89%; 0.61%; 1.49% and 2.28%, respectively. The Budget Office then multiplied each of the exemptions by the amount of the ECC costs to be recovered. The Budget Office calculated the initial costs to be recovered for 2004-05 to be \$22,657,324.

Exhibit 3 below shows the projected revenues after deducting the costs attributed to exemptions.

**Exhibit 3 Initial Calculation Of Annual Revenues And Rates For 2004-05**

<b>Eligible Costs to be Recovered by Fee before Exemptions</b>		\$22,657,324
<b>Exempt Costs</b>		
LifeLine Exemption	\$22,657,324 * 7.89%	-1,787,663
Governmental Exemption	\$22,657,324 * 1.49%	-337,594
Education Exemption	\$22,657,324 * 2.28%	-516,587
Pay Phones Exemption	\$22,657,324 * 0.61%	-138,210
<b>Sub-total: Costs Attributed to Exemptions</b>		-2,780,054
<b>Projected Total Revenue Less Exemptions</b>		\$19,877,270
<b>Initial Exemption Rate</b>		12.27%
<b>Fee Rate Calculation</b>	Total Cost \$22,657,324/ Total Lines 1,079,843/12 months	\$1.75 per month
<b>Trunk Rate Calculation</b>	\$1.75 * 7.5 lines per trunk = \$13.13	\$13.13 per month

Source: Based on City Manager's May 2004 Memorandum.

As shown above, the initial revenue was projected at \$19,877,270 and the exemption rate was calculated at 12.27%. For fiscal year 2005-06, the Budget Office re-calculated the exemption rate to 10.36%.

*Auditing Service  
Provider  
Compliance*

Under the Municipal Code, the Finance Director has the authority to conduct audits of service providers which include inspection, auditing, and copying relevant records and material during regular business hours, upon advanced, written request.

*Annual Fee Review*

The City set January 1, 2005 as the start date of the ECSS Fee. Municipal Code Section 8.20.230 provides for an annual fee review. The Municipal Code requires that annually before December 15<sup>th</sup>, the Finance Director shall identify the data required and make requests to service providers for information sufficient to identify the number of access and trunk lines maintained during the past 12 months. The Municipal Code requires also service providers to respond within 60 days of request. Further, service providers may request the City to sign a nondisclosure, confidentiality agreement approved to form by the City Attorney to ensure that the City does not disclose proprietary information.

The Municipal Code requires that, annually before March 1, the Finance Director shall estimate the percentage of access lines subject to the ECSS Fee during the previous fiscal year and report this percentage as the eligible costs for the following fiscal year. During each even year, the Finance Director is also required to assess whether trunk lines continue to reasonably reflect the increased estimated access to the 911 system.

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**The ECSS Fee  
Assessment And  
Collection Process**

The Finance Department is responsible for processing the ECSS Fee from service providers.

*Assessing The  
Emergency  
Communication  
System Support Fee*

According to Finance staff, in July 2004, the Finance Department informed service providers of the City's intent to consider an ECSS Fee. In a letter dated July 30, 2004, Finance requested service providers to identify the number of access lines servicing the City of San José. If the service providers were unable to provide timely, complete, and accurate information, Finance would rely on information obtained from the California Public Utilities Commission and City wireless service records to establish the initial fee.

In August 2004, the City Council adopted Resolution 27229 implementing the Emergency Communication System Support Fee. The resolution required service providers to collect the fee from subscribers. In a letter dated September 16, 2004, the City informed service providers of the City Council's action to implement the fee. The letter offered a workshop to discuss implementation of the fee and answer provider questions.

*Collecting The  
Emergency  
Communication  
System Support Fee*

The Municipal Code requires telephone service providers to bill and collect the ECSS Fee from telephone subscribers monthly. Service providers must submit the ECSS Fee collected to the City by the end of the month following the billing month to avoid penalty payments. Additionally, late payments and penalty charges accrue an interest assessment from the date of delinquency and the date a penalty is assessed.

When the Finance Director determines a telephone subscriber willfully withheld fee payment from the service provider for four or more billing cycles, the Finance Director can assume the responsibility for collection for the specified billing cycles. The same penalty and interest assessments apply for subscriber billings. According to the Municipal Code, the service providers must provide monthly reports to the City with the names, addresses, and unpaid fee amount of any telephone subscriber who has not paid the ECSS Fee for four or more billing cycles.

*Finance Department  
Process*

The City instituted the ECSS fee starting January 2005 with the first remitted payments due to the City around the end of February 2005. According to Finance staff, providers send the monthly ECSS Fee payments to the Finance Department's Payment Processing Group (PPG). With the payments, service providers submit either the City's standardized remittance form or a self-generated form documenting the fee calculation and number of access lines. The PPG processes and books the individual payments into the City's Financial Management System cash collection system.

Finance's Revenue, Compliance, and Monitoring group (RCM group) reconciles access line and fee amounts into an electronic spreadsheet which is their tracking mechanism. The RCM group reconciles the fee payments with the payment information in the Financial Management System and documentation submitted by the service providers.

From this effort, the RCM group performs a compliance review to identify service providers that have not remitted payments and the related documentation. The RCM group sends letters, emails, or makes phone calls to service providers who have not submitted documentation and/or payments and informs them that they owe the City information and/or money. The RCM group provides service providers with a calculation of the

penalty and interest charges due. Late providers submit documentation and/or payment to the PPG and the collection process begins again.

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**Objectives, Scope  
And Methodology**

In June 2007, the Santa Clara County Civil Grand Jury issued a report on the ECSS Fee. The Grand Jury recommended that the City Auditor's Office perform an audit to ensure that ECSS Fee calculation, allocation, assessment, and collection processes comply with the City's ordinances. In August 2007, the City Council Rules Committee approved adding the ECSS Fee audit to the City Auditor's Workplan.

Our audit objectives were to determine if the processes to calculate, allocate, assess, and collect the ECSS Fee are in compliance with the Municipal Code. The scope of our audit was from the establishment of the ECSS Fee in 2004 through June 2007. We reviewed the City's ordinances and Municipal Code sections related to the ECSS Fee. We also reviewed the ECSS Fee Consultant's Report. Further, we performed a site visit to the City's Emergency Communication Center.

We used the following methodologies to achieve our audit objectives:

- To verify the City's compliance with the accuracy of LifeLine exemptions information, we contacted the California Public Utilities Commission.
- To verify the City's compliance with the accuracy of payphones exemptions information, we contacted the Support Services - County Coordinator with Santa Clara County Communications Department who maintains 911 Master Street Address Guide database for the California 9-1-1 Emergency Communications Office.
- To verify ECSS Fee calculation, we reviewed the Budget Office's 2004-05, 2005-06, and 2006-07 Emergency Response Fee Calculations spreadsheets. We also compared the Budget Office calculation spreadsheets information to the corresponding information in the City's Financial Management System.
- To verify the indirect costs rates, we reviewed the 2007-08 City-wide Cost Allocation Plan and process.

- To ensure that the amount of the ECSS Fee allocated to the General Fund was in compliance with the Municipal Code, we compared the eligible operating costs with the 2005-06 and 2006-07 ECSS Fee revenues.

To verify compliance with key Municipal Code requirements, we reviewed Finance Department documentation, compared Finance Department records to the City's Financial Management System, and performed sample testing of service provider reports and government phone records. We reviewed other jurisdictions emergency communications fee regulatory requirements.

In addition to the above methodologies, we interviewed management and staff from the City Manager's Budget Office, the Finance Department, the Police Department, and the City Attorney's Office. Furthermore, we interviewed the ECSS Fee Consultant, and staff at the California Public Utilities Commission (PUC). Finally, we reviewed City memorandums and a PUC report on the State LifeLine Program.

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## Finding I

# Opportunities Exist For The City To Improve The Calculation, Allocation, Assessment, And Collection Processes For The Emergency Communication System Support Fee

In 2004, the City of San Jose (City) established an Emergency Communication System Support Fee (ECSS Fee). The ECSS Fee is a flat monthly fee to cover most of the cost of maintaining the Emergency Communications Center's (ECC) function that enables telephone subscribers to access the City's emergency communications system. The telephone lines of LifeLine telephone customers; non-profit hospitals and educational organizations; government agencies; and payphones are exempt from paying the ECSS Fee. The costs associated with these exempt telephone lines are funded by the General Fund. Furthermore, the ECSS Fee covers only the ECC's eligible costs.

Since January 2005 through June 2007, the ECSS Fee has funded \$49 million of ECC costs, and the General Fund has funded about \$13 million. We identified that the ECSS Fee can fund an additional \$857,000 for past and current year ECC costs.

We evaluated the City's ECSS Fee calculation, allocation, assessment, and collection processes. Although most of the processes are in accordance with the San Jose Municipal Code (Municipal Code), we found some exceptions. Specifically, we found that:

- Better sources of data exist for the number of telephone customers exempt from the ECSS Fee, particularly the number of LifeLine and payphone exemptions. If the Budget Office were to begin using updated exemption information to determine the amount of ECC costs that should be paid for from the fees collected, an additional \$607,000 would be available in fiscal year 2007-08. This also means that General Fund spending on the ECC could be reduced by \$607,000.
- The City estimates that a percentage of the ECC's costs are non-911 activities and are therefore not funded by the ECSS Fee. The City cannot locate documentation as to how it developed this percentage of non-911 activity,



or “ineligible operating costs rate”. Also, the Budget Office does not use the ineligible operating costs rate when it funds overtime expenses with the ECSS Fee as it does with the other personal services operating costs. By reducing the amount of ECC overtime cost, the amount funded by the ECSS Fee is reduced by \$44,703, \$45,077 and \$41,314 for fiscal years 2005-06, 2006-07 and forecast 2007-08, respectively.

- By using a calculation methodology more closely aligned with provisions of the Municipal Code, the Budget Office can apportion a greater share of the cost of the ECC to ECSS Fee revenues, an additional \$113,000 and \$268,000 from fiscal years 2005-06 and 2006-07, respectively, rather than to the General Fund.

Based on our audit, we found that the City should make the following adjustments to the key components of the ECSS Fee calculation:

**Exhibit 4 Summary Of Key Components That Increase/(Decrease) The Amount Of ECSS Fee Funding And Additional Amounts Available To Reimburse The General Fund**

<b>Key ECSS Fee Components</b>	<b>2005-06</b>	<b>2006-07</b>	<b>Forecast 2007-08</b>	<b>Total</b>
<b>Decrease In LifeLine Exemptions</b>	n/a	n/a	\$570,000	\$570,000
<b>Decrease In Payphone Exemptions</b>	n/a	n/a	\$37,000	\$37,000
<b>Overtime Costs That Should Not Be Funded By The Fee</b>	(\$44,703)	(\$45,077)	(\$41,314)	(\$131,094)
<b>Methodology To Apportion Costs</b>	\$113,079	\$267,990	n/a	\$381,069
<b>Net Findings</b>	\$68,376	\$222,913	\$565,686	\$856,975

We also found that

- The City is at risk of funding ineligible indirect costs with the ECSS Fee;
- Service providers erroneously billed subscribers that are exempt under the Municipal Code from having to pay;
- Service providers do not register with the City as required; and

- Service providers do not provide information required under the Municipal Code.

Better sources of data for the number of LifeLine exemptions, payphone exemptions, as well as the more precise methods for calculating eligible salary and overtime operating costs, indirect costs, and the basis for allocating ECSS Fee revenues would improve the calculation of the ECSS Fee. To ensure that it has the most up to date information available, the Budget Office should annually request the number of LifeLine exemptions from the California Public Utilities Commission (PUC), and the number of payphones from the Santa Clara County Communications Department. Furthermore, the Budget Office should also ensure that only that portion of overtime considered as eligible operating costs is included in the calculation of the amount to be funded by the ECSS Fee. In addition, the City Manager's Office should perform a study to determine the amount of time ECC staff spends on 911-related activities to determine the portion of staff costs that are eligible operating costs. Furthermore, we recommend that the Finance Department conduct a review of ECC indirect costs to ensure indirect costs are allocated in compliance with the Municipal Code and determine the necessity for a separate ECC indirect cost rate. By adopting the actions described above, the City will be able to improve the ECSS Fee calculation and allocation processes.

We found the City can further improve its calculation of the ECSS Fee by establishing a process to ensure service providers do not charge the ECSS Fee to exempt City of San José phones. To make sure the City communicates timely information to service providers, the City should annually obtain and verify current service provider registrations from each service provider and annually provide relevant instructions and documents necessary for implementing the ECSS Fee. To maintain Municipal Code compliance, the City should annually identify and request from service providers the information necessary to comply with annual fee requirements, maintain an annual fee cap adjustment process, and ensure service providers maintain controls over billing, collecting, and remitting the ECSS Fee. Lastly, the City can improve their regular review of the ECSS Fee by updating the subscriber fee cap annually, and conducting a review to determine whether the fee rates for trunk line fees continue to reasonably reflect the estimated ECC workload relative to access lines.

**Better Data On The Number Of LifeLine And Payphone Exemptions Is Available To Improve The Accuracy Of The ECSS Fee Calculation And Allocation**

The Municipal Code allows certain categories of telephone subscribers an exemption from paying the ECSS Fee. The City estimates the number of these exemptions in order to calculate the revenue that cannot be collected due to these exemptions. However, better sources of data for LifeLine and payphone exemptions are available to determine the number of subscribers exempt from the ECSS Fee.

*Recent Changes In Federal Communications Commission Regulations Have Improved The Information Available On The Number Of LifeLine Exemptions By City*

The Municipal Code provides for exemptions from the ECSS Fee, including exemptions for LifeLine telephone subscribers. Furthermore, the City's June 2006 ordinance for extending the ECSS Fee stipulates that the portion of operating and project costs that reflect the cost to provide the estimated 911 emergency communication system benefits to telephone subscribers who are exempt from the ECSS Fee should not be funded from the ECSS Fee revenues. Instead, the General Fund provides the funding for the exempt costs. Therefore, it is important to have accurate LifeLine telephone exemptions information. However, the California Public Utilities Commission (PUC), whose information the City used initially in 2004 to estimate the number of LifeLine exemptions, did not previously have the information available by city. As such, the City has been using estimates for determining the number of subscribers with LifeLine exemptions. In 2004, the Federal Communications Commission ordered changes to the Universal Lifeline and Link-up program (the FCC Lifeline Order). The changes required a change to the LifeLine certification and verification procedures. The PUC implemented these changes in 2006. As a result of these changes, the PUC now has data by city on the number of LifeLine exemptions. We found that based on a lower number of LifeLine exemptions since the 2006 changes, beginning in fiscal year 2007-08, the City can use the ECSS Fee to fund an additional \$570,000 of the ECC.

The City's Ordinance No. 27785, which extended the ECSS Fee until June 2009, states that the portion of operating and project costs that reflect the cost to provide the ECC services to telephone subscribers who are exempt from the ECSS Fee,

should not be funded by the ECSS Fee. Furthermore, the Municipal Code defines LifeLine service and that it is an exemption to the ECSS Fee:

*8.20.100 Lifeline service.*

*Lifeline service" means discounted telephone service available to eligible low-income residential customers.*

*8.20.220 Exemptions.*

*Nothing in this chapter shall be construed as imposing a fee upon the access lines of:*

*A. A lifeline customer of a service supplier; or...*

Given the Municipal Code exemption, the City needs to determine the number of LifeLine customers in the City. Currently, the Budget Office estimates the number of LifeLine customers based on Statewide data. However, recent federal changes have resulted in the availability of actual data for the number of LifeLine customers in San Jose.

The PUC administers the State of California LifeLine Program. The LifeLine Program provides discounted residential basic wireline telephone service to eligible low-income Californians. The PUC began implementing changes to the LifeLine Program in July 2006 in response to the FCC Lifeline Order, which ordered improvements to the Universal Service Lifeline and Link-Up program. The FCC Lifeline Order requires States to document a customer's income qualifications when a customer's participation in the program is based on level of income, in order to continue to receive subsidies from the Federal Lifeline/Link-Up program. Therefore, the PUC, through a contractor, now certifies new Lifeline customers and annually verifies existing Lifeline customers. Prior to July 2006, the process was handled by telephone companies.

Our office requested the number of Lifeline telephone customers from the PUC. According to the PUC, its LifeLine contractor indicated that there were 58,615 LifeLine telephone customers living in the City of San Jose as of December 2007. As indicated in the Background Section of this report, the current ECSS Fee is \$1.75 monthly. Therefore, the amount of exempt LifeLine cost that cannot be funded by the ECSS Fee is as follows:

\$1,230,915, or, 58,615 LifeLine telephone customers \*  
\$1.75 fee per month \*12 months.

The Budget Office performs a calculation to forecast ECSS Fee revenue, exemptions and costs. The Budget Office's 2007-08 forecast of operating costs was \$28 million. Based on the Budget Office's 2007-08 calculation, the LifeLine customers represented about 86,000 exemptions, or approximately \$1.8 million. However, because the Budget Office used estimates, the actual number of LifeLine exemptions was overstated. The updated number of exemptions represents \$1,231,000 of the cost of the ECC that cannot be funded with the ECSS Fee. In other words, for 2007-08, the City can use the ECSS Fee to fund an additional \$570,000 of the ECC costs.

By obtaining the actual number of LifeLine exemptions, the City can more accurately determine the cost of the ECC that should not be funded by the ECSS Fee. In our opinion, the City needs to use the updated information that is now available on the number of LifeLine telephone customers to ensure compliance with the Municipal Code. Therefore, we recommend that the Budget Office staff annually obtain the number of LifeLine telephone customers in the City from the PUC.

We recommend that the Budget Office staff:

**Recommendation #1**

**Annually obtain the most up-to-date number of LifeLine telephone customers from the California Public Utilities Commission. (Priority 3)**

*A Better Source Of  
Data Is Available On  
The Number Of  
Payphone  
Exemptions*

The City does not impose the ECSS Fee on payphones. According to the City Manager's May 2004 Emergency Response Fee memorandum (2004 ECSS Fee Memorandum), which recommended establishing the ECSS Fee, payphones are exempt from the State of California 911 surcharge. Furthermore, the ECSS Fee Memorandum stated that all other jurisdictions with a local ECSS fee have exemptions for these phones. Therefore, the City included payphones as an exemption category in the Municipal Code.

Based on the Municipal Code requirement, the City needs to determine the number of payphones in the City. The City currently estimates the percentage of payphones based on FCC

Statewide data because it was not able to obtain actual data. We contacted PUC staff, who stated that the number of payphones has been rapidly declining because of the proliferation of cell phone use. We also contacted the Support Services - County Coordinator (County 911 Coordinator) with Santa Clara County Communications Department. The County 911 Coordinator maintains the Master Street Address Guide (MSAG) for the State of California 9-1-1 Emergency Communications Office. The MSAG database includes information on the number of payphones in San Jose. According to the County 911 Coordinator, there were 2,236 payphones in the City of San Jose as of February 2007. As indicated previously, the current ECSS Fee is \$1.75 monthly. Therefore, the number of payphone exemptions that cannot be funded by the ECSS Fee is as follows:

\$46,956, or, 2,236 payphones \* 1.75 fee per month \*12 months.

The Budget Office's 2007-08 Emergency Response Fee Calculation eligible operating costs forecast for the ECC was \$28 million. Of this amount, the payphone exemptions represented about 4,000 payphones or \$84,000 annually. As noted above, the number of payphone exemptions represents \$46,956. Therefore, for 2007-08, the City should increase the amount of ECC costs that can be funded by the ECSS Fee by \$37,000.

By obtaining the actual number of payphone exemptions, the City can more accurately determine the cost of the ECC that can be funded with the ECSS Fee. Therefore, we recommend that the Budget Office annually obtain the number of payphones in the City from the Santa Clara County Communications Department.

We recommend that the Budget Office staff:

**Recommendation #2**

**Annually obtain the number of payphones in the City of San Jose from the Santa Clara County Communications Department. (Priority 3)**

**The City Cannot Locate Documentation As To How It Computed The Costs That Are Not To Be Recovered Through The ECSS Fee**

When the City established the ECSS Fee in 2004, the City did not intend to use the ECSS Fee to fund non-911 related ECC costs. The 2004 ECSS Fee Memorandum indicated that the City's ordinance would exclude costs not associated with 911 calls. The City Manager estimated that 10% of non-supervisory personal services costs were not associated with 911 calls. However, according to the City Manager's Office, its staff cannot locate documentation as to how the City identified ineligible personal services costs to ensure compliance with the eligible operating costs as defined in the Municipal Code. The Municipal Code defines those ECC operating costs which can be funded by the ECSS Fee. Specifically, the Municipal Code allows the City to allocate the ECSS Fee to direct and indirect costs associated with 911 calls. The Budget Office reduces the annual personal services costs by 10% to account for the costs of non-911 activity.

The Municipal Code definition of the 911 emergency communications system clearly states that staff who respond to requests for service are not considered a part of that system, and are therefore not funded by the ECSS Fee. The Municipal Code defines eligible operating costs as the portion of the operating costs attributable to the 911 emergency communications system. According to the City Attorney's Office, although the Municipal Code does not specifically define ineligible operating costs, the City's ability to reduce the amount of operating costs funded by the ECSS Fee is implicit in the definition of eligible operating costs. Specifically, the clause in the definition of eligible operating costs "*...attributable to the operation of the 911 emergency communication system...*" allows the City to determine ineligible operating costs. Furthermore, according to the City Attorney's Office, the portion of staff costs for time spent on officer-initiated and other non-911 related activity and the allocated associated downtime for the dispatchers are not considered eligible operating costs, and therefore should not be funded by the ECSS Fee.

The ECC is staffed with Police and Fire Department Public Safety Dispatchers who perform the functions of call taking and dispatching. The cost of Police Department staff who answer 911 calls is an eligible operating expense. Also, the cost of Fire Department staff, who handle 911 calls and dispatch fire and medical emergencies, is an eligible operating expense. However, the Police Department staff who dispatch officers for

911 calls also handle the communications for officer-initiated calls and other non-911 related activity. These costs associated with non-911 activity are not an eligible operating expense. To address the amount of the ineligible operating costs, the City Manager stated in the 2004 ECSS Fee Memorandum that:

*However, we are generally recommending use of the San Francisco ordinance definition of cost, with one modifications[sic], the comparatively small deletion of the costs associated with dispatcher time spent talking with field units about issues not associated with any call. This has the impact of reducing the fee by about 10%. Supervisory, facility, and overhead costs are not changed.*

The Budget Office reduces the annual personal services costs by 10% to account for the costs of non-911 activity.<sup>1</sup> The amount of costs related to non-911 activity is not funded by the ECSS Fee. However, we found that the Budget Office, the Police Department, or the ECSS Fee Consultant could not provide documentation that 10% of the operating costs are not related to the 911 emergency communications system. The Police Communications Manager (Communications Manager) stated that he recalled the ECSS Fee Consultant observing the dispatchers for a brief period of time prior to the establishment of the ECSS Fee. Furthermore, the Communications Manager said that he was interviewed by the ECSS Fee Consultant. According to the Communications Manager, the ECSS Fee Consultant did not confirm or verify the 10% ineligible rate with him. In addition, the Communications Manager believes that the rate may be higher than 10%, although he has not performed a study. Finally, the ECSS Fee Consultant told us that he does not recall studying the ineligible operating expenses.

The City needs to document the rate of ineligible operating expenses to ensure that the City is complying with the Municipal Code when determining the amount of eligible operating costs to be funded by the ECSS Fee. Specifically, the City Manager's Office should perform a study to determine the amount of time that staff spends on activities related to 911 calls and on officer-initiated and other non-911 related calls. The portion of staff costs for time spent on officer-initiated and

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<sup>1</sup> The Budget Office also reduces supervisory costs by 10%. In our opinion, this practice is consistent with the other personal services costs.



other non-911 related activity and the allocated associated downtime for the dispatchers would not be funded by the ECSS Fee.

We recommend that the City Manager's Office:

**Recommendation #3**

**Perform a study to determine the amount of time ECC staff spends on 911-related activity; and officer-initiated and other non-911-related activity to determine the portion of staff costs that are 911-related and can be funded with the ECSS Fee in compliance with the Municipal Code definition of eligible operating costs. (Priority 3)**

*The Budget Office Includes More In Overtime Expenses Than It Should In ECSS Fee Eligible Costs*

As noted in the above section, a portion of the ECC operating costs is not related to the 911 emergency communications system and is therefore not an eligible operating cost. The Budget Office calculates the ECC operating costs by reducing the Police and Fire Department staff salaries and benefits by 10% to account for non-911 activity. Furthermore, the Budget Office calculates the overhead costs by applying the overhead cost rate to the reduced salaries and benefits. However, although overtime also includes non-911 activity, the Budget Office does not reduce overtime costs by 10%. The Budget Office should also reduce overtime costs consistent with the way that it handles regular salaries and benefits.

Also noted in the above section, the 2004 ECSS Fee Memorandum stated that the 10% reduction did not apply to supervisory, facility, and overhead costs. Although the 2004 ECSS Fee Memorandum fee calculation showed the overtime costs included at 100% eligible operating costs, the memorandum did not describe how overtime should be calculated with respect to the ECSS Fee. Furthermore, according to the Communications Manager, the overtime costs include both the call taking and the dispatch functions as described in the prior section. As such, overtime costs include staff time spent on officer-initiated calls and other non-911 activity. As a result, overtime costs should be reduced by the ineligible operating costs rate. The ECC Police and Fire overtime costs for fiscal years 2005-06 and 2006-07 were \$447,033 and \$450,774, respectively. Therefore, overtime costs to be recovered by the ECSS Fee should be reduced by 10%, or \$44,703 and \$45,077 for fiscal years 2005-06 and 2006-07, respectively. Furthermore, the Budget Office 2007-08

overtime forecast of \$413,137 should also be reduced by 10% or \$41,314. Finally, in future calculations, the Budget Office should include only that portion of overtime considered to be eligible operating costs in the calculation of the amount to be funded by the ECSS Fee.

We recommend that the Budget Office:

**Recommendation #4**

**Include only that portion of overtime considered as eligible operating costs in the calculation of the amount to be funded by the ECSS Fee. (Priority 2)**

**The Budget Office Can Apportion A Greater Share Of The Cost Of The ECC To The ECSS Fee Revenues**

During the annual budget process, the Budget Office staff forecasts exemptions, revenues, and costs related to the ECSS Fee. The ECSS Fee revenue is deposited to the ECSS Fee Fund and is transferred monthly to the General Fund because the General Fund initially paid for the ECC operating costs, and it needs to be reimbursed for paying ECC operating expenses, up to the budgeted amount. At the end of the fiscal year, the Budget Office staff calculates the actual amount of costs to be covered by the actual ECSS Fee revenues and the amount of costs to be covered by the General Fund. The Municipal Code defines eligible operating costs as 911 related costs less the amount related to exemptions. We found that the Budget Office calculates the amount of ECC costs that can be funded by the ECSS Fee by factoring for exemptions using a calculation based on revenue instead of cost. As a result, the Budget Office overstates the impact of the exemptions. In our opinion, calculating the amount that can be funded by the ECSS Fee by factoring exemptions based on cost instead of revenue, is more closely aligned with the Municipal Code definition of eligible operating costs. By basing the amount to be covered by the ECSS Fee on provisions in the Municipal Code, the ECSS Fee can fund an additional \$113,000 and \$268,000 from fiscal years 2005-06 and 2006-07 revenues, respectively.

The Municipal Code definition of eligible operating costs is the ECC cost excluding both exemptions and non-911 related activity. As described in the prior sections on ECSS Fee exemptions and ECC eligible operating costs, the Budget Office reduces salary and benefits operating costs by 10% to

account for non-911 activity, such as dispatching officer-initiated calls. Furthermore, the Budget Office accounts for exemptions by using an exemptions rate, currently, 10.36%.

The Budget Office calculates the amount of ECC costs that can be funded by the ECSS Fee by factoring for exemptions using a calculation based on revenues. Specifically, instead of deducting exemptions from cost, the Budget Office adds the estimated amount of revenue that would have been received if the exempt users had paid, to the actual revenue received. To determine the total amount of costs that can be funded by the ECSS Fee, the Budget Office then subtracts from actual revenue, the difference between the revenue adjusted for exemptions and the ECC 911 cost, without reducing it for exemptions. The Budget Office does not reduce the ECC 911 cost for exemptions, as the exemptions have already been accounted for in revenue.

We independently calculated the ECSS Fee based on the Municipal Code provisions. And, we noted that our calculation varied from the way the Budget Office currently performs the calculation. Since the ECSS Fee must only provide sufficient revenue to cover the cost of providing 911 services, and since our calculation of the ECSS Fee emphasizes the cost of exemptions to the program, we believe our method of calculating the ECSS Fee is the most appropriate. As the following Exhibit shows, the Budget Office does not calculate the ECSS Fee on a cost basis, rather, it accounts for the amount of the ECSS Fee that the City can reimburse the General Fund on a revenue basis. We simplified the Budget Office calculation of the total amount available to fund the ECC and compared it to the City Auditor's method as follows:

**Exhibit 5 Comparison Of City Auditor And Budget Office Methods Of Determining The Impact Of Exemptions When Calculating The ECC Costs That Can Be Funded With The ECSS Fee**

City Auditor Method	Budget Office Method
<p><b>Step 1.</b>            911 Cost            Less: <u>Exempts Costs</u></p> <p><b>Result: 911 costs that can be funded with the ECSS Fee</b></p>	<p><b>Step 1.</b>            Actual Revenue            Plus: <u>Estimated Exemption Revenue</u>            Result: Adjusted Estimated Revenue  <u>Less 911 Cost</u>            Result: Subtotal</p> <p><b>Step 2.</b>            Actual Revenue            Less: <u>Subtotal from Step 1</u></p> <p><b>Result: 911 costs that can be funded with the ECSS Fee</b></p>

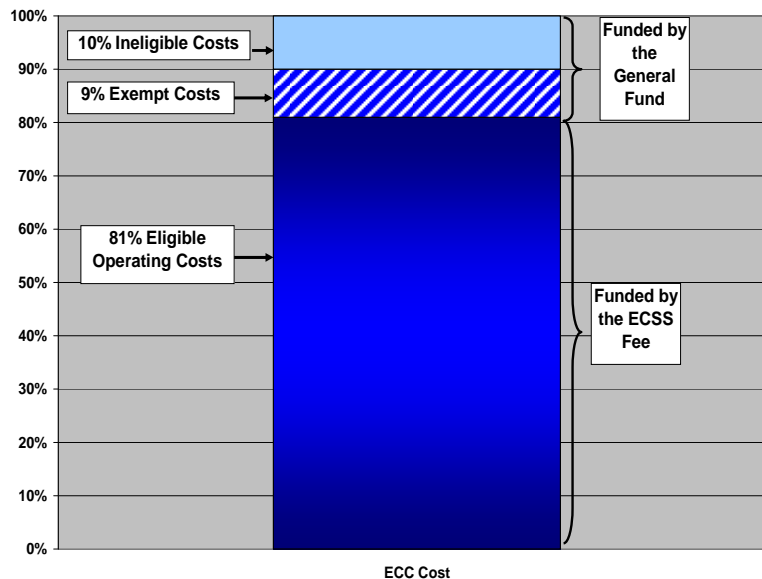
Source: City Auditor description of methods.

As shown in Exhibit 5, the City Auditor uses cost to determine the impact of exemptions, whereas, the Budget Office uses revenue. Each method determines the amount of 911 costs that can be paid from the ECSS Fee revenues.

As noted earlier, 10% of the ECC costs are non-911 activity. That amount is funded by the General Fund. Furthermore, 9%<sup>2</sup> of the ECC cost is attributable to telephone subscribers who are exempt from the ECSS Fee. That amount is also funded by the General Fund. The remaining 81% of the ECC’s total costs, are associated with non-exempt telephone subscribers. The 81% of the ECC’s total costs represents the amount that can be funded by the ECSS Fee. Exhibit 6 below shows the ECC cost components and their funding sources.

<sup>2</sup> Given that the Budget Office reduces the 10% non-911 activity first, the exemption rate on the 911-only activity is 10.36%.

**Exhibit 6 ECC Cost Components And Funding Sources**



Source: City Auditor prepared.

Exhibit 7 below shows the actual ECSS Fee revenues, actual ECC costs, and the actual amounts the Budget Office transferred to the General Fund for 2005-06 and 2006-07; and the forecast for 2007-08. It also shows the City Auditor's calculation of exempt costs, eligible operating costs and the remaining balance that can be funded by the ECSS Fee.

**Exhibit 7      ECC Costs And ECSS Fee Revenues For Fiscal  
Years 2005-06 And 2006-07; Forecast 2007-08; And  
City Auditor Calculation Of Exempt Costs, Eligible  
Operating Costs And Remaining Balance**

	<b>2005-06 Actual</b>	<b>2006-07 Actual</b>	<b>2007-08 Forecast</b>
<b>ECSS Fee Revenue*</b>	\$21,509,294	\$23,251,468	\$23,400,000
<b>ECC 911 Costs</b>			
Direct Costs Police and Fire Staffing <sup>3</sup>	17,470,830	17,993,035	20,541,669
Total Citywide Overhead Costs	5,268,219	5,216,526	7,411,899
Other costs <sup>4</sup>	164,646	142,378	80,000
<b>Total ECC 911 Costs</b>	22,903,695	23,351,939	28,033,568
<b>City Auditor Calculation of Exempt Costs</b>			
10.36% Portion of Operating Costs that Reflect Cost to Provide 911 Service to Exempt Telephone Subscribers	(2,372,823)	(2,419,261)	(2,904,278)
<b>City Auditor Calculation of Total Eligible Operating Costs that can be Funded with ECSS Fee</b>	\$20,530,872	\$20,932,678	\$25,129,290
<b>Amount Reimbursed to General Fund</b>	\$19,800,000	\$20,600,000	n/a
<b>City Auditor Estimate of Remaining Balance that can be funded by the ECSS Fee**(Total Eligible Operating Costs minus Amount Transferred to General Fund)</b>	\$730,872	\$332,678	n/a

\*In 2004-05 the City used \$9 million in ECSS Fee revenue to fund the ECC.

\*\*As of the end of Fiscal Year 2006-07, the ECSS Fee Fund 154 balance totaled \$4,360,761. This amount consists of the balances that were not transferred plus the amounts over collected. The Budget Office states that they plan to use part of this balance to cover future eligible operating costs shortfalls, such as the one projected for 2007-08, or for project costs. The Municipal Code allows for ECSS Fee funding of project costs, such as ECC equipment.

As shown in Exhibit 7, the amount transferred to the General Fund in 2005-06 and 2006-07 was less than the amount available to be transferred. During the year, the ECSS Fees are transferred to the General Fund up to the budgeted amount. After the fiscal year end, the Budget Office calculates the total amount that can be covered by the ECSS Fee. To be

<sup>3</sup> Salary and benefit expenditures have been reduced by 10% for non-911 activity costs.

<sup>4</sup> Software, facility, phone company collection fees, cost to administer "cap", other exclusions and audit cost, net of Central Fire District revenues.

conservative, the Budget Office has not transferred additional amounts it calculated that can be transferred, over the budgeted amount.

Exhibit 8 shows the difference in the two calculations for the total amount of the ECSS Fee revenues that can be transferred to the General Fund.

**Exhibit 8      Difference Between The City Auditor And Budget Office Calculations For The Amount Of ECC Costs That Can Be Funded With The ECSS Fee Revenues For 2005-06 And 2006-07**

<b>Fiscal Year</b>	<b>City Auditor Calculation</b>	<b>Budget Office Calculation</b>	<b>Additional Amount That Can Be Funded Per City Auditor*</b>
<b>2005-06</b>	\$20,530,872	\$20,417,793	\$113,079
<b>2006-07</b>	\$20,932,678	\$20,664,688	\$267,990

\*As shown in Exhibit 6, we calculated that \$730,872 and \$332,678 are still available to be transferred to the General Fund. The Budget Office calculates that \$617,793 and \$64,688 are still available to be transferred to the General Fund.

As shown in Exhibit 8, our calculation method results in additional amounts that can be funded by the ECSS Fee, when compared to the Budget Office calculation. Specifically, we calculated that the ECSS Fee can fund an additional \$113,079 and \$267,990, for fiscal years 2005-06 and 2006-07, respectively. Our calculation of the total amount available to be transferred is based on the Municipal Code definition of eligible operating costs. The Municipal Code definition of eligible operating costs is the ECC cost excluding both exemptions and non-911 related activity. For example, in 2006-07, we calculated the amount of eligible operating costs at \$20,932,678. Therefore, that is the amount that can be transferred to the General Fund.

On the other hand, the Budget Office calculated the amount of costs that can be covered by the ECSS Fee using the methodology shown in Exhibit 5. Specifically, the Budget Office calculated the total amounts to be \$20,417,793 and \$20,664,688 for 2005-07, and 2006-07, respectively, as shown in Exhibit 8.

In our opinion, using the Municipal Code definition of eligible operating costs to determine the amount of ECSS Fees that can fund ECC costs more closely aligns with the Municipal Code provisions.

We recommend that the Budget Office:

**Recommendation #5**

**Use the Municipal Code definition of “eligible operating costs” as the amount of ECSS Fees to transfer to the General Fund. (Priority 2)**

**The City Is At Risk Of Funding Ineligible Indirect Services Costs With The ECSS Fee**

We found the City’s approach to allocating indirect services costs to the ECC may result in funding ineligible costs with the ECSS Fee. The Municipal Code defines eligible costs as costs directly associated with providing emergency communications services to phone subscribers paying the ECSS Fee. Further, the Municipal Code clearly states that staff costs for staff who respond to calls for service are not to be funded by the ECSS Fee.

The Finance Department (Finance) is responsible for administering the City’s overhead cost allocation process. The overhead cost allocation process allows the City to recover costs for indirect services to the line departments. Indirect support services to the line departments include payroll from the Finance Department, recruiting from the Human Resources Department, and legal counsel from the City Attorney’s Office, to name a few. The allocation basis includes types such as relative budget size, level of service and number of transactions. As a result, an overhead cost rate allocates costs to programs based on the relative benefit to the program. Periodically, Finance staff solicit information from the departments to use during the overhead cost allocation process. For the Police Department, the core service area is the lowest level utilized in the allocation process.

We reviewed the process that Finance uses to allocate indirect costs to the ECC. The Police ECC costs are included in the Police Department Respond to Calls for Service core service. Additionally, the core service includes Bureau of Field Operations costs, which include patrol staff who respond to calls for service. The Respond to Calls core service is the largest Police core service utilized to allocate indirect costs



representing 69 percent of the Police Department in the 2007-08 City-wide Cost Allocation Plan. The allocation formula uses personnel costs upon which indirect services costs are allocated to program within the core service. Since the Municipal Code disallows Police response costs from being paid through the ECSS Fee, the City's overhead process of combining Police response indirect costs with the ECC indirect costs increases the risk the City allocates ineligible costs to the ECC. The City develops separate indirect cost rates for other programs with specific cost restrictions. For example, the City develops overhead cost rates for grant programs funded by the federal government, and assigns costs in accordance to federal guidelines.

According to Finance, as of February 2008, the City has not analyzed whether all indirect costs allocated to the ECC are allowable under the Municipal Code. In our opinion, the City can reduce the risk of funding ineligible costs by conducting a thorough review of ECC indirect costs and determining the necessity for a separate ECC indirect cost rate.

We recommend the Finance Department:

**Recommendation #6**

**Conduct a review of ECC indirect costs to ensure indirect costs are allocated in compliance with the Municipal Code and determine the necessity for a separate ECC indirect cost rate. (Priority 2)**

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**Service Providers  
Bill Exempt  
Subscribers**

According to the Municipal Code, the City of San José and educational organizations are exempt from paying the ECSS Fee for government phones. We found that service providers we sampled improperly charged the ECSS Fee to exempt organizations.

Our review revealed service providers charged the ECSS Fee to the City. Specifically, from 2005 to 2007, two service providers charged the \$1.75 fee on exempt City cellular phone lines in about nine City departments. We informed City staff of the finding, and staff responded immediately with one of the service providers. According to City staff, the service provider agreed to address the billing problem. The exempt billing issue reveals that service providers may be billing other exempt subscribers. For example, we found a service provider billed

the ECSS Fee to an educational organization. As a result, it appears subscribers who are exempt may be paying the ECSS Fee.

The City should monitor exempt City of San José phones to ensure service providers do not charge the ECSS Fee. Additionally, the City should inform the identified educational organization of the Municipal Code exemption.

We recommend the Finance Department:

**Recommendation #7**

**Establish a regular monitoring process to ensure service providers do not charge the ECSS Fee to exempt City of San José phones. (Priority 3)**

**Recommendation #8**

**Inform the identified education organization of the Municipal Code exemption. (Priority 3)**

**Service Providers Do Not Register With The City As Required**

Based on Finance’s records, Finance staff found that 13 out of 13 service providers we sampled did not register their business name and agent with the Finance department. According to the Municipal Code, service providers providing local telephone services to subscribers within the City shall register with the Director of Finance. Providers shall use the form prescribed by the Director of Finance, which shall include:

- Name under which they transact business and
- Identify a registered agent for process.

The Municipal Code stipulates that all notices and communications must be directed to the agent designated in the service supplier’s registration in order to be effective notice. Finance staff indicated that they were unable to locate registration forms for 13 service providers identified during the City Auditor’s testing.

As the Municipal Code directs the City to provide all notices and communications directly to the registered agent, the City should maintain current and complete registration forms. Additionally, the City should ensure service providers are informed of their obligations regarding the ECSS Fee. The lack of current registrations increases the likelihood of miscommunication between the City and service providers

regarding ECSS Fee program requirements, Fee payment, and documentation issues. The City should regularly update registration information and educate registered agents about Municipal Code requirements.

We recommend the Finance Department:

**Recommendation #9**

**Obtain current registrations from each service provider in accordance with the form prescribed by the Director of Finance, establish an annual process of verifying registrations, and annually provide relevant instructions and documents necessary for the ECSS Fee program to registered agents. (Priority 3)**

**Service Providers  
Do Not Provide  
Information  
Required Under  
The Municipal  
Code**

We found service providers do not provide information required under the Municipal Code. According to the Municipal Code, service providers must minimally submit subscriber information separated into the number of access lines, trunk lines, and high-capacity trunk lines as well as lines exempt from the ECSS Fee. Additionally, the Municipal Code requires service providers to submit monthly reports on a form provided by the Finance Department stating the amount of fees collected. The Finance Director may require additional readily available information. Currently, the Finance Department form includes information such as:

- Basis of Remittance – gross fees collected or gross fees charged (must be the same basis for at least 12 months),
- Total number of access lines,
- Number of exempt access lines,
- Total number of trunk lines,
- Number of exempt trunk lines, and
- Signed declaration indicating information is true, correct, and complete.

*Service Provider  
Monthly Reporting*

We sampled 26 monthly payment records from 13 service providers and found that 23 of 26 monthly payments were submitted without the required monthly form. Only one of the 13 service providers sampled reported access, trunk, and high-capacity trunk line information, and none of the service providers reported exempt line information. Although these service providers remitted the monthly fee, most service

providers aggregated access line information into a single number. As a result, the lack of required information hinders the Finance Department's ability to comply with Municipal Code annual fee review provisions.

The Municipal Code requires the Finance Director to conduct a fee review to ensure the fee is reflective of ECC cost and workload. Specifically, the Municipal Code requires:

- On or before December 15 annually, the Finance Director shall identify data required and request from each service provider information sufficient to identify the number of access lines maintained by each service provider for the past 12 months (by type – single, trunk, high-capacity trunk, exempt). Further, the service provider shall respond to the City's request in 60 days.
- On or before March 1<sup>st</sup> annually, the Finance Director shall use the above data and establish a historical percentage of non-exempt costs which shall become the following year's percentage for the purposes of funding eligible ECC costs.
- Maximum fee for a telephone subscriber (per service location annually) shall be adjusted annually by the consumer price index.
- On or before March 1, 2006 and March 1<sup>st</sup> each even year thereafter, the Finance Director shall evaluate information from industry sources, regulatory bodies, and City experience to determine whether the fee rates from trunk and high-capacity trunk lines continue to reflect the estimated workload to the ECC relative to access lines.

In the City's response to the June 2007 Grand Jury report, the City reports it attempted to negotiate a non-disclosure agreement with a large provider; however, the language in the service provider's proposed agreement would significantly restrict the sharing of information. Consequently, the City and service provider did not come to an agreement. According to the City's response to the Grand Jury report, the service provider also asserted that its computer database system is unable to produce the requested information.

*Fee Review*

We found that the ECSS Fee has not been reviewed as directed in the Municipal Code. In 2005, the Finance Department requested specific line information from service providers. According to the Finance Department, some service providers contend that the information requested is already provided on their monthly reports. Other service providers express the limitations of their billing systems and are unable to extract the information required by the Finance Department. Since 2005, the Finance Department has not requested detailed line information from service providers. Consequently, the Finance Department has not fully responded to the Municipal Code requirements for an annual assessment of actual exempt and non-exempt line information. Additionally, the Finance Department is currently uncertain of the true capabilities of most service provider database systems or the controls in place to ensure service providers properly bill, collect, and remit ECSS Fees to the City. An assessment of system controls may provide sufficient evidence of database system capabilities and identify controls that service providers properly bill, collect, and remit ECSS fees.

Because service providers remit monthly fee payments without the minimally required and Finance requested information, the Finance Department is unable to comply with Municipal Code fee review provisions. The Finance Department should annually identify the minimal information it requires to comply with Municipal Code provisions and request the information from service providers. Further, the Finance Department should work with the service provider to assess if service provider controls ensure proper billing, collection, and remittance of ECSS fees. If the City's efforts reveal the service providers are unable or unwilling to provide the information the City seeks, the City should explore whether other options are viable ways to comply with Municipal Code provisions.

We recommend the Finance Department:

**Recommendation #10**

- 1) **Annually identify and request from service providers the information identified in the Municipal Code and such additional information as Finance determines necessary for it to perform the fee review requirements set forth in the Code,**
- 2) **Work with service providers to determine the documentation and review necessary to assess the strength of controls over billing, collecting, and remitting the ECSS Fee,**
- 3) **Assess if service provider controls ensure proper billing, collecting, and remitting the ECSS Fee, and**
- 4) **If the service providers are unable or unwilling to provide the information the City seeks, the City should explore whether other options or sources are viable ways to comply with Municipal Code provisions. (Priority 3)**

*Fee Cap Adjustment*

We found the Finance Department does not inform the service providers of the annual fee cap adjustment. According to the Municipal Code, the maximum fee for a telephone subscriber (per service location annually) shall be adjusted annually by the consumer price index. Although Finance reports no providers have reached the original \$20,000 cap, the Municipal Code requires the calculation and adjustment. Any ECSS Fee adjustment may result in subscribers reaching or exceeding the current cap. Therefore, the Finance Department should maintain an updating process, update the fee cap annually, and annually communicate the fee cap adjustment to the service providers.

We recommend the Finance Department:

**Recommendation #11**

**Maintain a fee cap updating process and update the service providers on an annual basis. (Priority 3)**

*Relative Workload  
Of Access And Trunk  
Lines*

According to the Municipal Code, on or before March 1, 2006 and March 1<sup>st</sup> of each even year thereafter, the Finance Director shall evaluate information from industry sources, regulatory bodies, and City experience to determine whether the fee rates for trunk line and high-capacity trunk lines continue to reflect the estimated workload of the ECC relative to access lines. However, we found the Finance Director does not perform an industry, regulatory body, and City experience review.

Based on a review in San Francisco, San Francisco determined that a trunk line is equivalent to 7.5 access lines and a high-capacity trunk is equivalent to 135 access lines. In comparison, San José maintains all trunks at 7.5 access lines. San Francisco charges significantly more for high-capacity trunks to recover the increased costs associated with high-capacity trunk lines. San José does not vary the fee for trunks and high-capacity trunks. San José charges \$13.13 for trunks, while San Francisco charges \$20.62 for trunks and \$371.15 for high-capacity trunks.

The City of San Jose has adopted a two-tier rate structure of \$1.75 per access line and \$13.13 per trunk line. We recommend the Finance Department conduct the industry, regulatory body, and City experience review to determine whether the fee rates for trunk line fees continue to reasonably reflect the estimated ECC workload relative to access lines.

We recommend the Finance Department:

**Recommendation #12**

**Conduct a review to determine whether the fee rates for trunk lines continue to reasonably reflect the estimated ECC workload relative to access lines. (Priority 3)**

*The Finance  
Department Should  
Consider Utilizing  
Their Right To  
Perform A  
Compliance Audit*

According to the Municipal Code, the Finance Director has authority to conduct onsite compliance audits of service providers in order to review compliance with the Municipal Code. However, we found the Finance Director has not conducted onsite audits of service providers.

Finance staff indicated that they have not seen or received any provider information that would enable them to assess the accuracy of the monthly report information or the capabilities of service provider database systems to produce accurate and sufficiently detailed monthly reports. As a result, the Finance Department is unable to determine if service providers fully

comply with all Municipal Code provisions. Therefore, the Finance Department should continue to work with service providers to obtain information and documentation sufficient to fully implement Municipal Code requirements, such as:

- Monthly Reporting requirements,
- Annual Fee Review, and
- Industry sources, regulatory bodies, and City experience review.

However, if the City does not obtain sufficient information and documentation, the City should exercise its right to an onsite compliance audit.

We recommend the City Administration:

**Recommendation # 13**

**Exercise its right to an onsite compliance audit of select service providers, if the City does not obtain sufficient information and documentation. (Priority 3)**

**CONCLUSION**

The City has opportunities to improve the ECSS Fee calculation, assessment, allocation, and collection processes. Specifically, the City can utilize better data sources that will allow for reduced General Fund spending on the ECC. In addition, the City should document what portion of direct and indirect costs are eligible for ECSS Fee funding, and use the Municipal Code definition of eligible operating costs to calculate the amount of ECSS Fee Funding. Further, the City can engage service providers in providing information necessary for the City to comply with annual fee requirements and reviewing service provider controls over billing, collecting, and remitting the ECSS Fee. The City should regularly update service provider agent registrations and annually communicate relevant instructions and documents necessary for the ECSS Fee program. Lastly, the City should update service providers on the fee cap and conduct a review to determine whether the fee rates for trunk line fees continue to reasonably reflect the estimated ECC workload relative to access lines.



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**RECOMMENDATIONS**

We recommend that the Budget Office staff:

**Recommendation #1**      **Annually obtain the most up-to-date number of LifeLine telephone customers from the California Public Utilities Commission. (Priority 3)**

**Recommendation #2**      **Annually obtain the number of payphones in the City of San Jose from the Santa Clara County Communications Department. (Priority 3)**

We recommend that the City Manager’s Office:

**Recommendation #3**      **Perform a study to determine the amount of time ECC staff spends on 911-related activity; and officer-initiated and other non-911-related activity to determine the portion of staff costs that are 911-related and can be funded with the ECSS Fee in compliance with the Municipal Code definition of eligible operating costs. (Priority 3)**

We recommend that the Budget Office:

**Recommendation #4**      **Include only that portion of overtime considered as eligible operating costs in the calculation of the amount to be funded by the ECSS Fee. (Priority 2)**

**Recommendation #5**      **Use the Municipal Code definition of “eligible operating costs” as the amount of ECSS Fees to transfer to the General Fund. (Priority 2)**

We recommend the Finance Department:

**Recommendation #6**      **Conduct a review of ECC indirect costs to ensure indirect costs are allocated in compliance with the Municipal Code and determine the necessity for a separate ECC indirect cost rate. (Priority 2)**

**Recommendation #7**      **Establish a regular monitoring process to ensure service providers do not charge the ECSS Fee to exempt City of San José phones. (Priority 3)**

We recommend the Finance Department:

- Recommendation #8**      **Inform the identified education organization of the Municipal Code exemption. (Priority 3)**
- Recommendation #9**      **Obtain current registrations from each service provider in accordance with the form prescribed by the Director of Finance, establish an annual process of verifying registrations, and annually provide relevant instructions and documents necessary for the ECSS Fee program to registered agents. (Priority 3)**
- Recommendation #10**      **1) Annually identify and request from service providers the information identified in the Municipal Code and such additional information as Finance determines necessary for it to perform the fee review requirements set forth in the Code,**  
**2) Work with service providers to determine the documentation and review necessary to assess the strength of controls over billing, collecting, and remitting the ECSS Fee,**  
**3) Assess if service provider controls ensure proper billing, collecting, and remitting the ECSS Fee, and**  
**4) If the service providers are unable or unwilling to provide the information the City seeks, the City should explore whether other options or sources are viable ways to comply with Municipal Code provisions. (Priority 3)**
- Recommendation #11**      **Maintain a fee cap updating process and update the service providers on an annual basis. (Priority 3)**
- Recommendation #12**      **Conduct a review to determine whether the fee rates for trunk lines continue to reasonably reflect the estimated ECC workload relative to access lines. (Priority 3)**

We recommend the City Administration:

- Recommendation #13**      **Exercise its right to an onsite compliance audit of select service providers, if the City does not obtain sufficient information and documentation. (Priority 3)**

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# Memorandum

**TO:** Sharon Erickson  
City Auditor

**FROM:** Scott P. Johnson  
Jennifer Maguire

**SUBJECT: RESPONSE TO THE AUDIT OF THE EMERGENCY COMMUNICATIONS SYSTEM SUPPORT FEE**      **DATE:** April 8, 2008

Approved

*Christine J. Shippy*

Date

*4-8-08*

The Administration has reviewed the “*Audit of the Emergency Communications System Support Fee*” (the Audit) and is in general agreement with the recommendations identified in the report. Following is the Administration’s response to the finding and each of the recommendations.

## FINDING

*Opportunities exist for the City to improve the ECSS Fee calculation, assessment, allocation, and collection processes*

**Comments on Finding:** The Administration will incorporate changes recommended by the City Auditor to improve the ECSS fee calculation and implementation. The Administration agrees that the fee calculation can be refined to more accurately determine the amount of the Emergency Communication System costs that can be recovered through the Emergency Communication System Support (ECSS) Fee. As shown in Exhibit 4 of the Audit, the General Fund has not recovered all of its eligible costs from the ECSS Fee and could transfer additional funding to the General Fund as reimbursement for prior year eligible costs. It should be noted that the annual variances between the City Administration and City Auditor eligible cost calculations range from less than 1% to 2% of the eligible costs. In addition to refining the ECSS fee calculation, the Administration will work with service providers to help ensure that exempted users are not assessed the ECSS fee and to improve the submission of data to the City.

## RECOMMENDATIONS

**Recommendation #1: The Budget Office staff annually obtain the most up-to-date number of Lifeline telephone customers from the PUC.**

**Response:** The Administration agrees with this recommendation and will use the information now available from the Public Utilities Commission (PUC). The Budget Office had been using Statewide Lifeline data and extrapolating for San José. The Auditor has identified a better source of data on the number of Lifeline subscribers in San José that has recently become available. While this data was not available when the 2007-2008 Adopted Budget was developed, it will be used in the reconciliation of 2007-2008 actual revenues and expenditures and in the development of future budgets.

**Recommendation #2: The Budget Office staff annually obtain the number of payphones in the City of San José from the Santa Clara County Communications Department.**

**Response:** The Administration agrees with this recommendation and will use this data source for updating the number of payphones in the City of San José.

**Recommendation #3: The City Manager’s Office should perform a study to determine the amount of time ECC staff spends on 911 related activity; and officer-initiated and other non-911 related activity to determine the portion of staff costs that are 911 related and can be funded with the ECSS Fee in compliance with the Municipal Code definition of eligible operating costs.**

**Response:** The Administration will reevaluate the amount of time the Emergency Communications System staff spends on 911-related activity. When the fee was originally developed, the Administration used an estimate of 10% for the time the communications staff spend on non-911 related activity. This percentage will be analyzed to ensure it is reflective of the amount of non-911 related activity.

**Recommendation #4: The Budget Office should include only that portion of overtime considered as eligible operating costs in the calculation of the amount to be funded by the ECSS Fee.**

**Response:** The Administration agrees with this recommendation. While the original calculation of the eligible costs that was approved when the fee was developed included 100% of the overtime expense, it is reasonable to calculate the overtime using the same eligibility percentage as the dispatch staff that earns the overtime.

**Recommendation #5: We recommend that the Budget Office use the Municipal Code definition of “eligible operating costs” as the amount of ECSS Fees to transfer to the General Fund.**

**Response:** The Administration agrees with this recommendation and will incorporate the modification to the fee calculation given the Municipal Code definition of “eligible operating costs”.

The Budget Office and the City Auditor ECSS Fee calculations differ in the treatment of exempt users. The different methodologies result in slightly different amounts that can be recovered from the ECSS Fee. Both methodologies account for exemptions in the fee calculation to ensure that non-exempt users are not subsidizing exempt users.

In its ECSS Fee calculation that compares revenues to eligible costs, the Budget Office treats the exempted telephone users by adjusting the actual or budgeted revenue figure upwards to account for the amount of revenue that would have been received had the exempt users paid the ECSS Fee. In determining the amount that can be transferred to the General Fund as reimbursement for ECSS costs, the Budget Office compares eligible costs, which have been calculated based on

90% of the ECSS staff time, to the adjusted revenue level. In the City Auditor calculation, the percentage associated with the exempt users is subtracted from the eligible costs.

The Budget Office calculation results in a slightly lower amount that can be transferred to the General Fund as reimbursement for the ECSS eligible costs. As shown in Exhibit 7, the variances associated with these two methodologies totaled \$381,000 for fiscal years 2005-2006 and 2006-2007, or slightly less than 1% of the \$41.5 million in eligible costs during this period.

**Recommendation #6: Conduct a review of ECC indirect costs to ensure indirect costs are allocated in compliance with the Municipal Code and determine the necessity for a separate ECC indirect cost rate.**

**Response:** The Administration agrees with this recommendation to review whether separate cost pools for the communications staff should be developed to calculate the ECSS indirect cost rate. Currently, existing overhead rates for Police (Respond to Calls for Service cost center) and Fire (Response cost center) are used to calculate the indirect costs associated with the ECSS. These cost centers include the communications staff as well as the line staff to deliver police and fire services. The portions of both the indirect and direct costs associated with the communications function could be segregated to develop the new rates, which may be lower or higher than the current rates depending on the ratios of indirect to direct costs. The Administration will need to consider the cost benefit analysis of separating out the communications staff in each department as separate cost centers and the impact it will have on existing resources and capacity in the Finance Department.

**Recommendation #7: Establish a regular monitoring process to ensure service providers do not charge the ECSS Fee to exempt City of San José phones.**

**Response:** The Administration agrees with this recommendation. Finance staff will inform City departments of the ECSS fee exemption and request all department liaisons to periodically review their phone bills to ensure that the ECSS fee is not being charged. City departments will be informed to contact the Revenue Compliance and Monitoring Section of Finance Department if ECSS fees are found on the phone bills so that service provider can be directed to stop the assessment of future ECSS fees.

**Recommendation #8: Inform the identified education organization of the Municipal Code exemption.**

**Response:** The Administration agrees with this recommendation and will inform the identified education organization of its exempt status. Upon receipt of the completed application for exemption, it will be forwarded to their service provider so that future ECSS charges will not be assessed.

In addition, Finance staff will send out a letter to remind all service providers that there are specific persons and organizations that are exempt from paying the ECSS fees.

**Recommendation #9: Obtain current registrations from each service provider in accordance with the form prescribed by the Director of Finance, establish an annual process of verifying registrations, and annually provide relevant instructions and documents necessary for the ECSS program to registered agents.**

**Response:** The Administration agrees with this recommendation. Finance staff will send out an annual recertification request to give the telephone providers an opportunity to update or provide the City with their current contact name, address and information on their agent for service of process.

**Recommendation #10: 1) Annually identify and request from service providers the information identified in the Municipal Code and such additional information as Finance determines necessary for it to perform the fee review requirements set forth in the code; 2) Work with service providers to determine the documentation and review necessary to assess the strength of controls over billing, collecting, and remitting the ECSS Fee; 3) Assess if service provider controls ensure proper billing, collecting, and remitting the ECSS Fee; and 4) If the service providers are unable or unwilling to provide the information the City seeks, the City should explore if other options or sources are viable ways to comply with Municipal Code provisions.**

**Response:** 1) The Administration agrees with this recommendation. The Director of Finance will review the monthly information that is being received from service providers to make a determination whether additional information is needed from the service providers to perform the annual fee and fee cap reviews that are required by Section 8.20.230 of the Municipal Code. Upon the request of any service provider, the Director of Finance will provide a confidentiality agreement that has been approved as to form by the City Attorney. The Director of Finance will evaluate the information that is received from service providers, along with information from industry sources, regulatory bodies and city experience to perform the annual fee and fee cap reviews.

2) The Administration does not oppose the concept of working with service providers concerning controls over billing, collecting and remitting the ECSS Fee. However, this work is not required under the Municipal Code and the annual fee review is not impacted by the quality of these controls. The fee evaluations that are dictated by the Municipal Code are unrelated to service provider fee billing, collection and remittance issues.

3) The Administration agrees that an assessment of fee billing, collection and remittance systems should be made as precursor to determining whether the Director of Finance should exercise the authority to perform a compliance audit of a service provider. However, as noted above, billing, collection and fee remittance concerns do not impact the fee reviews. The Administration also notes that the total revenue that is currently being received is at a level that is adequate to fund the eligible operating costs of the emergency communications system, which would tend to indicate that fee billing, collection and remittance systems are generally adequate.

4) The Administration agrees that if service providers are unwilling or unable to provide information that the City needs in order to conduct the annual fee reviews that are required by the Municipal Code, or to make an assessment of whether an audit is necessary, other options or sources for the necessary information should be explored. For example, one large service provider has estimated a cost of \$600,000 (2005 dollars) for computer programming to provide detailed line count information to the City. Before recommending an administrative agreement with the service provider for the City to pay the costs associated with this type of billing system change, the Administration would need to evaluate the likely magnitude of the impact of the information that would be provided on the fee calculation and/or revenue stream.

**Recommendation #11: Maintain a fee cap updating process and update the service providers on an annual basis.**

**Response:** The Administration agrees with this recommendation and will update the fee cap through the annual fees and charges process. Finance staff will inform service providers of the annual adjustment to the fee cap. The adjusted fee cap, which will take effect on July 1<sup>st</sup> of every year, will be included in the annual fee resolution approved by the City Council.

It should be noted that, to date, the City has not received any notification from a service provider that the fee cap has been reached by a telephone subscriber.

**Recommendation #12**

**Conduct a review to determine whether the fee rates for trunk lines continue to reasonably reflect the estimated ECC workload relative to access lines.**

**Response:** The City Administration agrees with this recommendation. The Director of Finance will evaluate information from industry sources, regulatory bodies and city experience to determine whether the fee rates for trunk lines reasonably continue to reflect the estimated ECC workload provided to trunk lines relative to access lines.

At this juncture, the ECC is not able to determine if the call is coming in from a trunk line or an access line. The Finance Director will also evaluate if additional funds should be requested to defray the estimated cost of \$600,000 (2005 dollars) asked by one large provider for computer programming to provide the detailed line count information in order to determine if that would be necessary to conduct this review. In addition, the Director of Finance will evaluate whether the ECC can provide information with respect to call origin (trunk line versus access line), and if so at what cost. Based on these evaluations, the Director of Finance will determine whether or not to recommend that the City Council amend the Municipal Code to drop this requirement.

**Recommendation #13: Exercise its right to an onsite compliance audit of select service providers, if the City does not obtain sufficient information and documentation.**



**Response:** The Administration agrees to consider exercising its right to conduct an onsite audit if service providers do not provide sufficient information to allow the Director of Finance to conduct the annual fee reviews that are required by the Municipal Code. However, based on the current level of revenue generated by the fee, which is adequate to fund operating costs and consistent with Administration revenue projections, and the limited experience with this fee (only three years of data) it does not appear that a compliance audit is necessary at this time. Moreover, the Administration would need to weigh the costs of conducting onsite compliance audits in relation to the potential impact of additional information that would be generated. Given the fact that overall revenues are in line with recoverable costs, minor adjustments in costs allocation between the fee payer categories (e.g. truck lines versus access lines) may not justify the costs of audit(s).

### COORDINATION

The responses in this memorandum have been coordinated with the City Attorney's Office.

  
Scott P. Johnson  
Finance Director

  
Jennifer A. Maguire  
Acting Budget Director

## APPENDIX A

### DEFINITIONS OF PRIORITY 1, 2, AND 3 AUDIT RECOMMENDATIONS

The City of San Jose's City Administration Manual (CAM) defines the classification scheme applicable to audit recommendations and the appropriate corrective actions as follows:

Priority Class <sup>1</sup>	Description	Implementation Category	Implementation Action <sup>3</sup>
1	Fraud or serious violations are being committed, significant fiscal or equivalent non-fiscal losses are occurring. <sup>2</sup>	Priority	Immediate
2	A potential for incurring significant fiscal or equivalent fiscal or equivalent non-fiscal losses exists. <sup>2</sup>	Priority	Within 60 days
3	Operation or administrative process will be improved.	General	60 days to one year

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<sup>1</sup> The City Auditor is responsible for assigning audit recommendation priority class numbers. A recommendation which clearly fits the description for more than one priority class shall be assigned the higher number. (CAM 196.4)

<sup>2</sup> For an audit recommendation to be considered related to a significant fiscal loss, it will usually be necessary for an actual loss of \$25,000 or more to be involved or for a potential loss (including unrealized revenue increases) of \$50,000 to be involved. Equivalent non-fiscal losses would include, but not be limited to, omission or commission of acts by or on behalf of the City which would be likely to expose the City to adverse criticism in the eyes of its citizens. (CAM 196.4)

<sup>3</sup> The implementation time frame indicated for each priority class is intended as a guideline for establishing implementation target dates. While prioritizing recommendations is the responsibility of the City Auditor, determining implementation dates is the responsibility of the City Administration. (CAM 196.4)