

# CITY OF SAN JOSÉ

Audit Report

## ANIMAL ADOPTION PROGRAM

Chapter 752, Statutes of 1998,  
and Chapter 313, Statutes of 2004

*July 1, 1999, through June 30, 2007*



JOHN CHIANG  
California State Controller

June 2010



**JOHN CHIANG**  
California State Controller

June 16, 2010

The Honorable Chuck Reed  
Mayor of the City of San José  
200 East Santa Clara Street  
San José, CA 95113

Dear Mayor Reed:

The State Controller's Office audited the costs claimed by the City of San José for the legislatively mandated Animal Adoption Program (Chapter 752, Statutes of 1998, and Chapter 313, Statutes of 2004) for the period of July 1, 1999, through June 30, 2007.

The city claimed \$3,768,395 (\$3,778,077 less a \$9,682 penalty for filing a late claim) for the mandated program. Our audit disclosed that \$2,413,107 is allowable and \$1,355,288 is unallowable. The costs are unallowable because the city misstated animal census data, claimed unsupported and ineligible costs, misclassified costs, understated eligible costs, and overstated offsetting revenues. The State paid the city \$1,402,129. Allowable costs claimed exceed the amount paid by \$1,010,978.

Regarding the unsupported costs for veterinary care, if the city subsequently provides supporting documentation, we will revise the final audit report as appropriate.

If you disagree with the audit findings, you may file an Incorrect Reduction Claim (IRC) with the Commission on State Mandates (CSM). The IRC must be filed within three years following the date that we notify you of a claim reduction. You may obtain IRC information at the CSM's Web site at [www.csm.ca.gov/docs/IRCForm.pdf](http://www.csm.ca.gov/docs/IRCForm.pdf).

If you have any questions, please contact Jim L. Spano, Chief, Mandated Cost Audits Bureau, at (916) 323-5849.

Sincerely,

*Original signed by*

JEFFREY V. BROWNFIELD  
Chief, Division of Audits

JVB/sk:wm

cc: Scott P. Johnson, Director of Finance  
City of San José  
Jon Cicirelli, Deputy Director  
San José Animal Care and Services  
Jeff Carosone, Principal Program Budget Analyst  
Cor-Gen Unit, Department of Finance  
Angie Teng, Section Supervisor  
Division of Accounting and Reporting  
State Controller's Office

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# Audit Report

## Summary

The State Controller's Office (SCO) audited the costs claimed by the City of San José for the legislatively mandated Animal Adoption Program (Chapter 752, Statutes of 1998, and Chapter 313, Statutes of 2004) for the period of July 1, 1999, through June 30, 2007.

The city claimed \$3,768,395 (\$3,778,077 less a \$9,682 penalty for filing a late claim) for the mandated program. Our audit disclosed that \$2,413,107 is allowable and \$1,355,288 is unallowable. The costs are unallowable because the city misstated animal census data, claimed unsupported and ineligible costs, misclassified costs, understated ineligible costs, and overstated offsetting revenues. Allowable costs claimed exceed the amount paid by \$1,010,978.

## Background

Food and Agriculture Code sections 31108, 31752-31753, 32001, and 32003 (added and amended by Chapter 752, Statutes of 1998) attempt to end the euthanasia of adoptable and treatable animals. It expressly identifies the state policy that "no adoptable animal should be euthanized if it can be adopted into a suitable home" and that "no treatable animal should be euthanized." The legislation increases the holding period for stray and abandoned dogs, cats, and other specified animals. It also requires:

- Verifying the temperament of feral cats;
- Posting of lost-and-found lists;
- Maintaining records for impounded animals; and
- Ensuring that impounded animals receive necessary and prompt veterinary care.

On January 25, 1981, the Commission on State Mandates (CSM) determined that Chapter 752, Statutes of 1998, imposed a state mandate reimbursable under Government Code section 17561.

The program's parameters and guidelines establish the state mandate and define reimbursement criteria. CSM adopted the parameters and guidelines on February 28, 2002, corrected them on March 20, 2002, and last amended them on January 26, 2006. In compliance with Government Code section 17558, the SCO issues claiming instructions to assist local agencies and school districts in claiming mandated program reimbursable costs.

For fiscal year (FY) 2003-04, the Legislature suspended the Animal Adoption program.

## **Objective, Scope, and Methodology**

We conducted the audit to determine whether costs claimed represent increased costs resulting from the Animal Adoption Program for the period of July 1, 1999, through June 30, 2007.

Our audit scope included, but was not limited to, determining whether costs claimed were supported by appropriate source documents, were not funded by another source, and were not unreasonable and/or excessive.

We conducted this performance audit under the authority of Government Code sections 12410, 17558.5, and 17561. We did not audit the city's financial statements. We conducted the 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 findings and conclusions based on our audit objectives.

We limited our review of the city's internal controls to gaining an understanding of the transaction flow and claim preparation process as necessary to develop appropriate auditing procedures.

## **Conclusion**

Our audit disclosed instances of noncompliance with the requirements outlined above. These instances are described in the accompanying Summary of Program Costs (Schedule 1) and in the Findings and Recommendations section of this report.

For the audit period, the City of San José claimed \$3,768,395 (\$3,778,077 less a \$9,682 penalty for filing a late claim) for costs of the Animal Adoption Program. Our audit disclosed that \$2,413,107 is allowable and \$1,355,288 is unallowable.

For the FY 1999-2000 claim, the State paid the city \$169,762. Our audit disclosed that \$89,266 is allowable. The State will offset \$80,496 from the other mandated program payments due the city. Alternatively, the city may remit this amount to the State.

For the FY 2000-01 claim, the State paid the city \$405,816. Our audit disclosed that the \$283,343 is allowable. The State will offset \$122,473 from the other mandated program payments due the city. Alternatively, the city may remit this amount to the State.

For the FY 2001-02 claim, the State made no payment to the city. Our audit disclosed that \$664,318 is allowable. The State will pay allowable costs claimed that exceed the amount paid, totaling \$664,318, contingent upon available appropriations.

For the FY 2002-03 claim, the State made no payment to the city. Our audit disclosed that \$698,026 is allowable. The State will pay allowable costs claimed that exceed the amount paid, totaling \$698,026, contingent upon available appropriations.

For the FY 2004-05 claim, the State paid the city \$504,628. Our audit disclosed that the entire amount is allowable.

For the FY 2005-06 claim, the State paid the city \$164,961. Our audit disclosed that \$72,452 is allowable. The State will offset \$92,509 from other mandated program payments due the city. Alternatively, the city may remit this amount to the State.

For the FY 2006-07 claim, the State paid the city \$156,962. Our audit disclosed that \$101,074 is allowable. The State will offset \$55,888 from other mandated program payments due the city. Alternatively, the city may remit this amount to the State.

### **Views of Responsible Officials**

We issued a revised draft audit report on May 10, 2010. After the revised draft report was issued, we became aware of a recent Appellate Court Decision, dated March 26, 2010, stating that Saturday should not be considered a business day. Accordingly, we revised the audit findings as appropriate and advised the city by e-mail on June 2, 2010.

Jon Cicirelli, Deputy Director of Animal Care and Services, responded by letter dated June 14, 2010 (Attachment), disagreeing with the audit results, except for Finding 1. This final audit report includes the city's response.

### **Restricted Use**

This report is solely for the information and use of the City of San José, the California Department of Finance, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.

*Original signed by*

JEFFREY V. BROWNFIELD  
Chief, Division of Audits

June 16, 2010

**Schedule 1—  
Summary of Program Costs  
July 1, 1999, through June 30, 2007<sup>1</sup>**

<u>Cost Elements</u>	<u>Actual Costs Claimed</u>	<u>Allowable per Audit</u>	<u>Audit Adjustment</u>	<u>Reference<sup>2</sup></u>
<u>July 1, 1999, through June 30, 2000</u>				
Policies and procedures	\$ 36,907	\$ —	\$ (36,907)	Finding 1
Acquiring space and facilities	17,236	15,193	(1,323)	Finding 2
Care and maintenance of dogs and cats	64,426	23,181	(41,245)	Finding 3
Care and maintenance of other animals	4,969	2,471	(2,498)	Finding 3
Necessary and prompt veterinary care	<u>233,094</u>	<u>47,701</u>	<u>(185,393)</u>	Finding 4
Total costs	356,632	89,266	(267,366)	
Less offsetting revenues/reimbursements	<u>(186,870)</u>	<u>—</u>	<u>186,870</u>	Finding 5
Total program costs	<u>\$ 169,762</u>	89,266	<u>\$ (80,496)</u>	
Less amount paid by the State		<u>(169,762)</u>		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ (80,496)</u>		
<u>July 1, 2000, through June 30, 2001</u>				
Acquiring space and facilities	\$ 189,487	\$ 162,608	\$ (26,879)	Finding 2
Care and maintenance of dogs and cats	110,821	38,275	(72,546)	Finding 3
Care and maintenance of other animals	5,910	2,126	(3,784)	Finding 3
Necessary and prompt veterinary care	<u>244,891</u>	<u>80,334</u>	<u>(164,557)</u>	Finding 4
Total costs	551,109	283,343	(267,766)	
Less offsetting revenues/reimbursements	<u>(145,293)</u>	<u>—</u>	<u>145,293</u>	Finding 5
Total program costs	<u>\$ 405,816</u>	283,343	<u>\$ (122,473)</u>	
Less amount paid by the State		<u>(405,816)</u>		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ (122,473)</u>		
<u>July 1, 2001, through June 30, 2002</u>				
Acquiring space and facilities	\$ 714,454	\$ 577,510	\$ (136,944)	Finding 2
Care and maintenance of dogs and cats	78,744	35,225	(43,519)	Finding 3
Care and maintenance of other animals	9,129	4,006	(5,123)	Finding 3
Necessary and prompt veterinary care	<u>194,901</u>	<u>57,259</u>	<u>(137,642)</u>	Finding 4
Total costs	997,228	674,000	(323,228)	
Less late penalty	<u>(9,682)</u>	<u>(9,682)</u>	<u>—</u>	
Total program costs	<u>\$ 987,546</u>	664,318	<u>\$ (323,228)</u>	
Less amount paid by the State		<u>—</u>		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 664,318</u>		

## Schedule 1 (continued)

Cost Elements	Actual Costs Claimed	Allowable per Audit	Audit Adjustment	Reference <sup>2</sup>
<u>July 1, 2002, through June 30, 2003</u>				
Acquiring space and facilities	\$ 1,079,025	\$ 584,805	\$ (494,220)	Finding 2
Care and maintenance of dogs and cats	82,628	21,169	(61,459)	Finding 3
Care and maintenance of other animals	9,422	3,660	(5,762)	Finding 3
Necessary and prompt veterinary care	<u>207,645</u>	<u>88,392</u>	<u>(119,253)</u>	Finding 4
Total program costs	<u>\$ 1,378,720</u>	698,026	<u>\$ (680,694)</u>	
Less amount paid by the State		—		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 698,026</u>		
<u>July 1, 2004, through June 30, 2005</u>				
Acquiring space and facilities	\$ 299,904	\$ 565,290	\$ 265,386	Finding 2
Care and maintenance of dogs and cats	50,239	75,739	25,500	Finding 3
Care and maintenance of other animals	6,369	6,839	470	Finding 3
Necessary and prompt veterinary care	<u>164,716</u>	<u>49,852</u>	<u>(123,864)</u>	Finding 4
Total costs	521,228	688,720	167,492	
Less offsetting savings/reimbursements	(16,600)	—	16,600	Finding 5
Less allowable costs that exceed amount claimed <sup>3</sup>	—	<u>(184,092)</u>	<u>(184,092)</u>	
Total program costs	<u>\$ 504,628</u>	504,628	<u>\$ —</u>	
Less amount paid by the State		<u>(504,628)</u>		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ —</u>		
<u>July 1, 2005, through June 30, 2006</u>				
Computer software	\$ 8,237	\$ 8,237	\$ —	
Care and maintenance of dogs and cats	49,181	61,440	12,259	Finding 3
Care and maintenance of other animals	1,479	2,775	1,296	Finding 3
Necessary and prompt veterinary care	<u>106,064</u>	<u>—</u>	<u>(106,064)</u>	Finding 4
Total program costs	<u>\$ 164,961</u>	72,452	<u>\$ (92,509)</u>	
Less amount paid by the State		<u>(164,961)</u>		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ (92,509)</u>		
<u>July 1, 2006, through June 30, 2007</u>				
Computer software	\$ 8,237	\$ 8,237	\$ —	
Care and maintenance of dogs and cats	59,086	91,163	32,077	Finding 3
Care and maintenance of other animals	1,283	1,674	391	Finding 3
Necessary and prompt veterinary care	<u>88,356</u>	<u>—</u>	<u>(88,356)</u>	Finding 4
Total program costs	<u>\$ 156,962</u>	101,074	<u>\$ (55,888)</u>	
Less amount paid by the State		<u>(156,962)</u>		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ (55,888)</u>		

## Schedule 1 (continued)

Cost Elements	Actual Costs Claimed	Allowable per Audit	Audit Adjustment	Reference <sup>2</sup>
<u>Summary: July 1, 1999, through June 30, 2007</u>				
Policies and procedures	\$ 36,907	\$ —	\$ (36,907)	
Computer software	16,474	16,474	—	
Acquiring space and facilities	2,300,106	1,906,126	(393,980)	
Care and maintenance of dogs and cats	495,125	346,192	(148,933)	
Care and maintenance of other animals	38,561	23,551	(15,010)	
Necessary and prompt veterinary care	<u>1,239,667</u>	<u>314,538</u>	<u>(925,129)</u>	
Total costs	4,126,840	2,606,881	(1,519,959)	
Less offsetting revenues/reimbursements	<u>(348,763)</u>	<u>—</u>	<u>348,763</u>	
Subtotal	3,778,077	2,606,881	(1,171,196)	
Less late penalty	(9,682)	(9,682)	—	
Less allowable costs that exceed amount claimed <sup>3</sup>	<u>—</u>	<u>(184,092)</u>	<u>(184,092)</u>	
Total program costs	<u>\$ 3,768,395</u>	2,413,107	<u>\$(1,355,288)</u>	
Less amount paid by the State		<u>(1,402,129)</u>		
Allowable costs claimed in excess of (less than) amount paid		<u>\$ 1,010,978</u>		

<sup>1</sup> The Animal Adoption Program was suspended for FY 2003-04.

<sup>2</sup> See the Findings and Recommendations section.

<sup>3</sup> Government Code section 17568 stipulates that the State will not reimburse any claim more than one year after the filing deadline specified in the SCO's claiming instructions. That deadline has expired for FY 2004-05.

# Findings and Recommendations

## **FINDING 1— Misclassified policies and procedures costs**

The city included \$36,907 in its claim for fiscal year (FY) 1999-2000 under the Policies and Procedures cost component. We determined that the costs were misclassified and should have been included in the formula for claiming Acquiring Space and Facilities costs instead.

The documentation provided by the city showed that the costs were claimed for a feasibility study. The study was used to evaluate alternatives between the costs of building an animal shelter or contracting with another entity for animal control services. When asked about the costs, city representatives stated that the costs should have been included as Acquiring Space and Facilities costs. We agreed that the costs are related to planning for the city's new shelter. Accordingly, we reclassified the costs and included them in the formula for determining allowable Acquiring Space and Facilities costs for FY 1999-2000 (see Finding 2).

### Recommendation

We recommend that the city establish and implement procedures to ensure that claimed costs are properly classified in its claim.

### City's Response

The city agreed with the finding.

**FINDING 2—  
Misstated acquiring  
space and facilities  
costs**

The city claimed \$2,300,106 for construction of new facilities for the audit period. We determined that the city overstated costs by the net amount of \$393,980 (understated by \$265,386 and overstated by \$659,366). The misstated costs occurred because the city claimed reimbursement using pro-rata percentages that were misstated, claimed ineligible and unsupported costs, misclassified costs, and understated allowable costs.

The following table summarizes the audit adjustment:

	Fiscal Year					Total
	1999-2000	2000-01	2001-02	2002-03	2004-05	
Allowable costs	\$ 15,913	\$ 162,608	\$ 577,510	\$ 584,805	\$ 565,290	\$ 1,906,126
Claimed costs	17,236	189,487	714,454	1,079,025	299,904	2,300,106
Difference	\$ (1,323)	\$ (26,879)	\$ (136,944)	\$ (494,220)	\$ 265,386	\$ (393,980)

*Misstated Pro-rata Percentages*

Allowable costs for this cost component are based on a formula that includes all costs incurred by the city applicable to construction of the animal shelter multiplied by a ratio of animals euthanized after the required holding period to the number of animals housed at the shelter during the required holding period. We made adjustments to costs incurred and the animal population information. In addition, our calculations took into consideration that the required holding period does not include Saturday as a business day. This is consistent with an Appellate Court decision dated March 26, 2010.

*Construction Costs Incurred*

Costs incurred for construction were adjusted for the following reasons:

- The city claimed \$36,239 for salaries and benefits that were not supported (\$8,602 for FY 1999-2000, \$14,031 for FY 2000-01, and \$13,606 for FY 2001-02). The variances were the result of differences between the city’s Peoplesoft and FAMIS systems that the city did not reconcile. We used the Peoplesoft amounts, which were adequately supported.
- The city included in its calculations \$16,416 of materials and supplies that were not related to construction of the animal shelter (\$2,445 for FY 2000-01, \$3,611 for FY 2001-02, and \$10,360 for FY 2002-03). These costs included such things as professional license renewal fees, travel costs incurred for employee attendance at seminars and conventions, and costs for employee training seminars and workshops.
- As noted in Finding 1, the city misclassified \$36,907 incurred for a feasibility study during FY 1999-2000 as costs incurred for policies and procedures. These costs were included as facility planning costs and added to the formula to determine allowable costs for FY 1999-2000.

- The city did not include \$66,039 of indirect costs in its calculations (\$4,895 for FY 1999-2000, \$10,829 for FY 2000-01, \$12,460 for FY 2001-02, \$30,264 for FY 2002-03, and \$7,591 for FY 2004-05). Our calculations were based on the 10% of direct salaries allowable per the parameters and guidelines.
- The city subtracted costs labeled as “adjustments” totaling \$9,576 (\$2,454 for FY 2000-01 and \$7,122 for FY 2001-02). The city’s analysis did not indicate how the adjustments were determined or why they were made. Accordingly, we did not include these amounts in our analysis of applicable construction costs.

#### *Pro-rata Representation of Animals*

Animal population information is used to develop the pro-rata percentages that are multiplied by allowable construction costs incurred to determine reimbursable costs. The parameters and guidelines (Section IV.B.1–Acquisition of Additional Space and/or Construction of New Facilities) state that eligible costs are based on a pro-rata representation of impounded stray or abandoned dogs, cats, and other animals that are held during the increased holding period and die or are ultimately euthanized to the total population of animals housed in the facility during the entire required holding period. For the purposes of this calculation, the term “animals that are held and die during the increased holding period” means that the animals died of natural causes and the phrase “are ultimately euthanized” means only animals that were euthanized *after* the required holding period.

We used the animal census data that the city provided to determine the total number of animals housed at the facility during the required holding period, the number of stray and abandoned animals that died of natural causes during the required holding period, and the number of stray and abandoned animals that were ultimately euthanized after the required holding period.

The table below summarizes the changes to pro-rata percentages by fiscal year:

	Reimbursement Ratio				
	Fiscal Year				
	1999-2000	2000-01	2001-02	2002-03	2004-05
Percentage allowable	12.52%	19.96%	14.19%	10.31%	60.51%
Percentage claimed	18.36%	23.17%	17.57%	19.09%	32.37%
Audit adjustment	-5.84%	-3.21%	-3.38%	-8.78%	28.14%

The program’s parameters and guidelines allow reimbursement, beginning January 1, 1999, for acquiring additional space by purchase or lease and/or construction of new facilities to provide appropriate or adequate shelter necessary to comply with the mandated activities during the increased holding period for impounded stray or abandoned dogs, cats, and other animals specified in Statutes of 1998, Chapter 752 that die during the increased holding period or are ultimately euthanized.

Eligible claimants are entitled to reimbursement for the proportionate share of actual costs required to plan, design, acquire, and/or build facilities in a given fiscal year. These costs are based on the prorata representation of impounded stray or abandoned dogs, cats, and other animals specified in Statutes of 1998, Chapter 752 that are held during the increased holding period specified in sections IV (B) (3) and (4) of these parameters and guidelines and die during the increased holding period or are ultimately euthanized, to the total population of animals housed in the facility. The population of animals housed in the facilities includes those animals that are excluded from reimbursement, as specified in sections IV (B)(3) and (4) of these parameters and guidelines period required by Food and Agriculture Code sections 31108, 31752, and 31753.

The table below summarizes the misstated gross construction costs used in the formula to compute reimbursable acquisition of facilities costs:

	Fiscal Year					Total
	1999-2000	2000-01	2001-02	2002-03	2004-05	
Gross construction costs:						
Allowable	\$ 127,098	\$ 814,671	\$ 4,069,840	\$ 5,672,209	\$ 934,210	\$ 11,618,028
Claimed	93,898	817,864	4,067,475	5,652,305	926,619	11,558,161
Misstated costs	<u>\$ 33,200</u>	<u>\$ (3,193)</u>	<u>\$ 2,365</u>	<u>\$ 19,904</u>	<u>\$ 7,591</u>	<u>\$ 59,867</u>
Misstated costs:						
Direct costs:						
Salaries and benefits	\$ (8,602)	\$ (14,031)	\$ (13,606)	\$ —	\$ —	\$ (36,239)
Materials and supplies	—	(2,445)	(3,611)	(10,360)	—	(16,416)
Contract services	36,907	—	—	—	—	36,907
Indirect costs	4,895	10,829	12,460	30,264	7,591	66,039
Miscellaneous adjustments	—	2,454	7,122	—	—	9,576
Total	<u>\$ 33,200</u>	<u>\$ (3,193)</u>	<u>\$ 2,365</u>	<u>\$ 19,904</u>	<u>\$ 7,591</u>	<u>\$ 59,867</u>

The following table summarizes the audit adjustment related to acquisition of facilities costs after applying the mandate formula:

	Fiscal Year					Total
	1999-2000	2000-01	2001-02	2002-03	2004-05	
Allowable:						
Eligible animals	1,166	1,480	948	1,279	3,978	
Housed animals	÷ 9,310	÷ 7,415	÷ 6,683	÷ 12,405	÷ 6,574	
Reimbursement ratio	12.52%	19.96%	14.19%	10.31%	60.51%	
Gross costs	× \$127,098	× \$814,671	× \$4,069,840	× \$5,672,209	× \$934,210	\$ 11,618,028
Total allowable	<u>\$ 15,913</u>	<u>\$ 162,608</u>	<u>\$ 577,510</u>	<u>\$ 584,805</u>	<u>\$ 565,290</u>	<u>\$ 1,906,126</u>
Claimed:						
Eligible animals	3,936	4,456	3,754	3,606	5,027	
Housed animals	÷ 21,443	÷ 19,233	÷ 21,372	÷ 18,885	÷ 15,532	
Reimbursement ratio	18.36%	23.17%	17.57%	19.09%	32.37%	
Gross costs	× \$93,898	× \$817,864	× \$4,067,475	× \$5,652,305	× \$926,619	\$ 11,558,161
Total claimed	<u>17,236</u>	<u>189,487</u>	<u>714,454</u>	<u>1,079,025</u>	<u>299,904</u>	<u>\$ 2,300,106</u>
Audit adjustment	<u>\$ (1,323)</u>	<u>\$ (26,879)</u>	<u>\$ (136,944)</u>	<u>\$ (494,220)</u>	<u>\$ 265,386</u>	<u>\$ (393,980)</u>

### Recommendation

We recommend that the city establish and implement procedures to ensure that claimed costs include only eligible costs, are based on actual costs, and are properly supported.

### City's Response

The City believes the calculation in the May 10, 2010 is nearly correct and the change contained in the June 2, 2010 e-mail is incorrect. The City does not believe the court case, filed March 26, 2010 should be applied retroactively to the year in which the costs were incurred, namely the 1999-2000 through 2004-05 fiscal years.

The City also questions the Controller challenge of the \$36,239 in salaries and benefits which the Controller disallowed based on variances between the City's PeopleSoft and FAMIS systems included in the FY 1999-2000 and FY 2000-2001 claims by purporting they were not adequately supported.

### SCO's Comment

The finding and recommendation remain unchanged.

We issued a revised draft report on May 10, 2010. In that report, we determined that the city understated costs by the net amount of \$117,287 (understated by \$211,617 and overstated by \$94,330). The misstated costs occurred because the city claimed reimbursement using pro-rata percentages that were misstated, claimed ineligible and unsupported costs, misclassified costs, and understated allowable costs.

Shortly after the revised draft report was issued, we became aware of an Appellate Court decision that was issued on March 26, 2010, relating to this mandated program (*Purifoy v. Howell*, First Appellate District, Division Three, Case No. A123856). The court held, in part, that Saturday is not a business day within the meaning of Food and Agriculture Code section 31108(a).

In the body of the audit finding, we noted that the parameters and guidelines allow reimbursement for this cost component based on the number of stray or abandoned dogs, cats, or other animals that die during the increased holding period or are ultimately euthanized. We determined that the Appellate Court case cited above changed the increased holding period when Saturday was excluded as a business day. Accordingly, the increased holding period was extended from two days to three days for stray and abandoned dogs and cats and from five days to six days for other animals. The phrase "ultimately euthanized" refers to the number of animals that are euthanized after the increased holding period expires. Our original calculations were based, in large part, on the number of animals that were euthanized on day six of the holding period and beyond. As a result of the court decision, we changed the calculations to include only animals that were euthanized on day seven of the holding period and beyond. As a result of this change, the audit adjustment

changed from a net understated costs of \$117,287 to a net overstated costs of \$393,980 (overstated by \$659,366 for FY 1999-2000 through FY 2002-03 and understated by \$265,386 for FY 2004-05).

The city argues that the court case cited above should not be applied retroactively to the city's claims for FY 1999-2000 through FY 2004-05. We disagree. We believe that the court case in question clarifies existing law, which in this case is Food and Agriculture Code section 31108, subdivision (a). Accordingly, the clarification should be effective as of the date that the statute became effective, which was July 1, 1999 (Senate Bill 1785, Statutes of 1998, Chapter 752). There is nothing in the decision to suggest that Saturday should have been considered as a business day at any time since the effective date of the statute.

The city is also contesting \$36,239 in salary and benefit costs that were removed from the gross amount of construction costs incurred by the city from FY 1999-2000 through FY 2001-02. During the course of the audit, the city provided worksheets detailing the amounts claimed each year as labor costs for facility construction. In each of the three worksheets provided, the reconciliations detail the costs recorded in the city's PeopleSoft system. Each worksheet also includes an amount labeled "Labor variance between FMS and PS" along with the notation that "Finance is researching the variance between systems." The amounts labeled as labor variances between systems are the amounts that make up the \$36,239 in question. The city has not yet provided any information to us regarding the variances between accounting systems. Accordingly, we are unable to apply these costs as eligible construction costs incurred by the city until the city provides clarification as to the composition of these costs and that they were incurred in order to comply with the mandated activities. If the city is able to adequately support that these costs were eligible for reimbursement under the mandated program, we will modify the audit results as appropriate.

**FINDING 3—  
Unallowable care and  
maintenance costs**

The city claimed \$533,686 for care and maintenance costs. We determined that \$369,743 is allowable and \$163,943 is unallowable. The unallowable costs occurred because the city misstated animal census data, misstated the number of animals that died of natural causes during the holding period and those that were euthanized after the holding period, claimed ineligible costs, understated eligible costs, and understated indirect costs.

The following table summarizes the claimed, allowable and unallowable costs for the audit period by fiscal year:

	Fiscal Year							Totals
	1999-2000	2000-01	2001-02	2002-03	2004-05	2005-06	2006-07	
Allowable costs:								
Dogs and cats	\$ 23,181	\$ 38,275	\$ 35,225	\$ 21,169	\$ 75,739	\$ 61,440	\$ 91,163	\$ 346,192
Other animals	2,471	2,126	4,006	3,660	6,839	2,775	1,674	23,551
Subtotal	25,652	40,401	39,231	24,829	82,578	64,215	92,837	369,743
Claimed costs:								
Dogs and cats	64,426	110,821	78,744	82,628	50,239	49,181	59,086	495,125
Other animals	4,969	5,910	9,129	9,422	6,369	1,479	1,283	38,561
Subtotal	69,395	116,731	87,873	92,050	56,608	50,660	60,369	533,686
Audit adjustment:								
Dogs and cats	(41,245)	(72,546)	(43,519)	(61,459)	25,500	12,259	32,077	(148,933)
Other animals	(2,498)	(1,704)	(5,123)	(5,762)	470	1,296	391	(15,010)
Total adjustment	\$ (43,743)	\$ (76,330)	\$ (48,642)	\$ (67,221)	\$ 25,970	\$ 13,555	\$ 32,468	\$ (163,943)

The parameters and guidelines allow reimbursement, beginning July 1, 1999, for providing care and maintenance during the increased holding period for impounded stray or abandoned dogs and cats that die during the increased holding period or are ultimately euthanized. The increased holding period shall be measured by calculating the difference between the days from the day of capture and four or six business days from the day after impoundment.

The parameters and guidelines also allow reimbursement beginning on January 1, 1999, for providing care and maintenance for stray or abandoned animals (specified in Food and Agriculture Code section 31753) that die during the increased holding period or are ultimately euthanized.

Eligible claimants are not entitled to reimbursement for the care and maintenance of the following population of dogs and cats:

- Stray or abandoned dogs, cats, and other animals that are irremediably suffering from a serious illness or severe injury;
- Newborn stray or abandoned dogs, cats, and other animals that need maternal care and have been impounded without their mothers;
- Stray or abandoned dogs, cats, and other animals too severely injured to move or where a veterinarian is not available and it would be more humane to dispose of the animal;

- Owner-relinquished dogs, cats, and other animals; and
- Stray or abandoned dogs, cats, and other animals that are ultimately redeemed, adopted, or released to a nonprofit animal rescue or adoption organization.

Eligible claimants may elect one of two methods, Actual Cost Method or Time Study Method, to claim costs for the care and maintenance of impounded stray or abandoned dogs, cats, and other animals that die during the increased holding period or are ultimately euthanized. The city elected to use the Actual Cost Method to claim these costs.

Under the Actual Cost Method, actual reimbursable care and maintenance costs per animal per day are computed for an annual claim period, as follows:

1. Determine the total annual cost of care and maintenance for all dogs, cats, and other animals impounded at a facility. Total cost of care and maintenance includes labor, materials, supplies, indirect costs, and contract services.
2. Determine the average daily census of all dogs, cats, and other animals. For purposes of claiming reimbursement under IV.B.3, average daily census is defined as the average number of all dogs and cats at a facility housed on any given day in 365-day period and the average number of all other animals at a facility housed on any given day in a 365-day period.
3. Multiply the average daily census of dogs, cats, and other animals by 365 to calculate the yearly census of dogs and cats and the yearly census of other animals.
4. Divide the total annual cost of care by the yearly census of dogs and cats to calculate cost per dog and cat per day and yearly census of other animals = cost per other animal per day.
5. Multiply the cost per animal per day by the number of impounded stray or abandoned dogs, cats, and other animals that die during the increased holding period, or are ultimately euthanized, by each reimbursable day. The reimbursable days for dogs and cats are the difference between three days from the day of capture, and four or six business days from the day after impoundment. The reimbursable days for other animals are four or six business days from the day after impoundment.

#### *Care and Maintenance Formula*

As the city elected to use the Actual Cost Method to claim costs, the parameters and guidelines provide for a formula-driven methodology to determine allowable mandated costs for the care and maintenance of dogs, cats, and other animals. The use of this method requires claimants to calculate the total amount of eligible costs incurred to provide care and maintenance for the animals housed in its shelter. This total is divided by the annual census of animals housed in the shelter to determine a cost per animal per day. The next element of the formula is adding the number of stray and abandoned animals that died of natural causes during the

holding period plus those animals that were euthanized after the required holding period. This total number of animals is then multiplied by the cost per animal per day. The resulting amount represents allowable costs for providing care and maintenance. Our calculations took into consideration that the required holding period does not include Saturday as a business day. This is consistent with an Appellate Court decision dated March 26, 2010.

What the mandate is reimbursing claimants for are costs associated with animals that were not relinquished, redeemed, adopted, or released to a nonprofit agency—animals for which the local agency was unable to assess fees to recover such costs.

During the first four years of the audit period, the city contracted with the Humane Society of Santa Clara Valley for animal control services. Accordingly, costs incurred for these years consisted of contract services costs. The city continued contracting with the Humane Society through September 30, 2004, after which the city opened its own shelter. Costs incurred for care and maintenance, beginning on October 1, 2004, consisted of salaries and benefits, materials and supplies, and related indirect costs. During the course of the audit, we made adjustments to salaries and benefits, contract services, and indirect cost amounts incurred by the city. As a result, we adjusted the costs per animal per day. We also made adjustments to the animal data that was used to claim costs. All of these adjustments are noted below.

#### *Salaries and Benefits*

The city included \$1,661,978 of salaries and benefits in its care and maintenance formulas during the audit period. This amount consisted of \$2,259,528 in supported salaries and benefits less \$597,550 related to non-reimbursable activities. We determined that the city overstated the non-reimbursable activities by \$315,598 relating to the following unrelated activities:

- Cleaning adoptable rabbit and small animal cages
- Cleaning adoptable cat cages
- Cleaning adoptable dog kennels
- Adoption counseling
- Euthanasia
- Intake of owned animals

Costs for the non-reimbursable activities were overstated because the activities of adoption counseling and euthanasia are the only costs that should have been excluded. We used the amounts claimed as an offset by the city for adoption counseling. We adjusted the amounts claimed for euthanasia by calculating costs incurred based on the city's average time data, the number of euthanasia procedures performed (using the city's Chameleon data), and the productive hourly rates for the employees involved.

The following table summarizes the audit adjustment by fiscal year for the salaries and benefits portion of the care and maintenance formulas:

Cost Component	Fiscal Year			Total
	2004-05	2005-06	2006-07	
Allowable costs:				
Salaries and benefits	\$ 450,375	\$ 757,385	\$ 1,051,768	\$ 2,259,528
Non-reimbursable activities	<u>(68,698)</u>	<u>(101,526)</u>	<u>(111,728)</u>	<u>(281,952)</u>
Subtotal	<u>381,677</u>	<u>655,859</u>	<u>940,040</u>	<u>1,977,576</u>
Claimed costs:				
Salaries and benefits	450,375	757,385	1,051,768	2,259,528
Non-reimbursable activities	<u>(147,437)</u>	<u>(198,004)</u>	<u>(252,109)</u>	<u>(597,550)</u>
Subtotal	<u>302,938</u>	<u>559,381</u>	<u>799,659</u>	<u>1,661,978</u>
Audit adjustment	<u>\$ 78,739</u>	<u>\$ 96,478</u>	<u>\$ 140,381</u>	<u>\$ 315,598</u>

### *Materials and Supplies*

The city included \$308,509 of materials and supplies costs in its care and maintenance formulas during the audit period (\$109,836 for FY 2004-05, \$113,243 for FY 2005-06, and \$85,430 for FY 2006-07). We determined that the entire amount is allowable.

### *Contract Services*

The city included \$3,375,751 for contract services costs in its care and maintenance formulas during the audit period. We determined that \$3,224,410 is allowable and \$151,341 is unallowable. The costs are unallowable because the city did not reduce contract shelter costs by the costs of euthanasia procedures performed during FY 1999-2000 and FY 2000-01, understated the number of euthanasia procedures performed during FY 2002-03, and overstated the number of euthanasia procedures performed during FY 2001-02 and FY 2004-05.

Until September 30, 2004, the city contracted with the Humane Society of Santa Clara Valley for its animal control services. The contract states that the Humane Society provided shelter services and dead animal services to the city. The shelter services portion of the contract consisted of both shelter services and medical services. The medical services component is discussed in Finding 4 for the Necessary and Prompt Veterinary Care cost component. Per the terms of the contract, shelter services consisted of:

- Shelter of abandoned, impounded, lost, or stray animals;
- Quarantine of biting animals;
- Rabies testing of suspected animals;
- Provision for surrendering and reclaiming abandoned, lost, or stray animals; and
- Euthanasia and disposal of abandoned, lost, impounded, or stray animals.

The Humane Society's billings during FY 1999-2000 through FY 2001-02 only separated the total charges billed by shelter services and dead animal services. Beginning in FY 2002-03, the Humane Society's

invoices separated costs billed for shelter services and medical services. Based on the amounts billed for that year, we determined that 56.62% of the contracted shelter costs in the previous years were for care and maintenance and 43.38% of the costs were for medical services.

As costs for euthanasia procedures are not reimbursable under the mandated program, the Humane Society performed an analysis for FY 2001-02 and determined that it cost \$16 to euthanize an animal. This cost was used until the Humane Society performed a revised analysis for FY 2004-05, that determined the euthanasia cost per animal was \$17.41. Accordingly, the city reduced contract services costs included in its care and maintenance formulas for FY 2001-02 and FY 2002-03 based on the number of animals euthanized at \$16 per animal and reduced contract costs for FY 2004-05 by \$17.41 per euthanized animal.

However, the city did not reduce its contract services costs for FY 1999-2000 and FY 2000-01 for the costs of euthanasia procedures performed. Accordingly, we determined the number of animals euthanized for those two years (7,956 and 6,592, respectively) based on the animal data provided by the city and reduced allowable contract services costs based on a cost of \$16 per euthanized animal (per the Humane Society's analysis for FY 2001-02). As a result, contract services costs included in the care and maintenance formulas were reduced by \$127,296 for FY 1999-2000 and \$105,472 for FY 2000-01.

For FY 2001-02, FY 2002-03, and FY 2004-05, we noted that the number of animals euthanized in the city's calculations of allowable contract services costs was not consistent with the number of animals euthanized that the city provided in its summary animal data. The detailed animal data supported that the number of euthanized animals was overstated by 1,247 for FY 2001-02 and 4,133 for FY 2004-05, and was understated by 1,621 for FY 2002-03. Accordingly, we determined that the city's offsets for euthanasia procedures were overstated by \$19,952 for FY 2001-02 and \$71,939 for FY 2004-05 and understated by \$14,760 for FY 2002-03.

We also determined that the city understated its contract services costs paid by \$4,296 for FY 2004-05.

The following table summarizes the audit adjustment by fiscal year for the contract services portion of the care and maintenance formulas:

	Fiscal Year					Total
	1999-2000	2000-01	2001-02	2002-03	2004-05	
Allowable costs:						
Contract costs paid	\$ 659,649	\$ 788,923	\$ 952,629	\$ 1,035,461	\$ 334,800	\$ 3,771,462
Euthanasia costs	(127,296)	(105,472)	(117,360)	(161,408)	(35,516)	(547,052)
Subtotal	532,353	683,451	835,269	874,053	299,284	3,224,410
Claimed costs:						
Contract costs paid	659,649	788,923	952,629	1,031,165	334,800	3,767,166
Euthanasia costs	—	—	(137,312)	(146,648)	(107,455)	(391,415)
Subtotal	659,649	788,923	815,317	884,517	227,345	3,375,751
Audit adjustment	<u>\$ (127,296)</u>	<u>\$ (105,472)</u>	<u>\$ 19,952</u>	<u>\$ (10,464)</u>	<u>\$ 71,939</u>	<u>\$ (151,341)</u>

### *Indirect Costs*

The city included indirect costs totaling \$161,908 in its care and maintenance formulas for the audit period. We determined that \$154,765 is allowable and \$7,143 is unallowable (overstated by \$16,789 and understated by \$9,646). Indirect costs were misstated because the city made calculation errors.

The city used the default indirect cost rate of 10% of direct wages allowable by the parameters and guidelines. However, for FY 2004-05, the city's calculation of \$19,660 for indirect costs in its care and maintenance formula was determined by applying the 10% rate to "total salaries paid" less "salaries and benefits paid for activities not related to stray animals." We applied the 10% rate to "total salaries paid" less "salaries paid for euthanasia and adoption counseling activities" and determined that the indirect cost amount should have been \$29,306.

For FY 2005-06 and FY 2006-07, the city included indirect cost amounts of \$60,297 and \$81,951, respectively, in its care and maintenance formulas. The amounts were determined by applying the 10% rate to total shelter salary costs incurred. However, the city did not subtract salary costs paid for the ineligible activities of adoption counseling and euthanasia procedures before applying the 10% rate. We adjusted total salaries paid for the activities of adoption counseling and euthanasia procedures and determined that the correct amount of indirect costs was \$52,214 for FY 2005-06 and \$73,245 for FY 2006-07.

### *Animal Census Data*

For all years of the audit period, the city applied the calculated cost per animal per day to the total number of dogs and cats that died or were euthanized and that had been held for one or more reimbursable days. It also applied the cost per animal per day to the number of "other" animals euthanized during the increased holding period. This is an incorrect application of the animal census data within the care and maintenance formula.

Using the city's detailed animal data that the city provided, we determined the number of stray and abandoned dogs, cats, and other animals that died of natural causes during the increased holding period and the number that were euthanized after the required holding period. The resulting number of cats and dogs was multiplied by two and the resulting number of other animals was multiplied by five. Both multiplication factors represent the number of increased holding period days required by the mandate. The resulting number of animals was then multiplied by the cost per animal per day to determine the allowable costs for care and maintenance.

In addition, by using the city's detailed animal data, we calculated the annual census for each year of the audit period. We determined that the number of animals included in the city's calculations were overstated in some years and understated in other years.

The table below summarizes misstated gross costs for care and maintenance used in the formula to compute reimbursable care and maintenance costs:

	Fiscal Year							Total	
	1999-2000	2000-01	2001-02	2002-03	2004-05 <sup>1</sup>	2004-05 <sup>2</sup>	2005-06		2006-07
Gross costs:									
Allowable	\$ 532,353	\$ 683,451	\$ 835,269	\$ 874,053	\$ 299,284	\$ 520,819	\$ 821,316	\$ 1,098,715	\$ 5,665,260
Claimed	659,649	788,923	815,317	884,517	227,345	432,434	732,921	967,040	5,508,146
Misstated costs	<u>\$(127,296)</u>	<u>\$(105,472)</u>	<u>\$ 19,952</u>	<u>\$ (10,464)</u>	<u>\$ 71,939</u>	<u>\$ 88,385</u>	<u>\$ 88,395</u>	<u>\$ 131,675</u>	<u>\$ 157,114</u>
Misstated costs:									
Direct costs:									
Salaries and benefits	\$ —	\$ —	\$ —	\$ —	\$ —	\$ 78,739	\$ 96,478	\$ 140,381	\$ 315,598
Contract services	(127,296)	(105,472)	19,952	(10,464)	71,939	—	—	—	(151,341)
Indirect costs	—	—	—	—	—	9,646	(8,083)	(8,706)	(7,143)
Misstated costs	<u>\$(127,296)</u>	<u>\$(105,472)</u>	<u>\$ 19,952</u>	<u>\$ (10,464)</u>	<u>\$ 71,939</u>	<u>\$ 88,385</u>	<u>\$ 88,395</u>	<u>\$ 131,675</u>	<u>\$ 157,114</u>

<sup>1</sup> Costs for July 1, 2004, through September 30, 2004, are for animal shelter services provided under contract by the Humane Society of Santa Clara Valley.

<sup>2</sup> Costs for October 1, 2004, through June 30, 2005, are from the operations of the city’s new animal shelter.

The table below summarizes misstated costs per animal used in the formula to compute reimbursable care and maintenance costs:

	Fiscal Year							
	1999-2000	2000-01	2001-02	2002-03	2004-05 <sup>1</sup>	2004-05 <sup>2</sup>	2005-06	2006-07
Allowable costs:								
Gross costs	\$ 532,353	\$ 683,451	\$ 835,269	\$ 874,053	\$ 299,284	\$ 520,819	\$ 821,316	\$ 1,098,715
Animal census	÷ 76,283	÷ 77,169	÷ 63,814	÷ 146,137	÷ 23,514	÷ 92,532	÷ 173,914	÷ 173,372
Cost per animal	<u>\$ 6.98</u>	<u>\$ 8.86</u>	<u>\$ 13.09</u>	<u>\$ 5.98</u>	<u>\$ 12.73</u>	<u>\$ 5.63</u>	<u>\$ 4.72</u>	<u>\$ 6.34</u>
Claimed costs:								
Gross costs	659,649	788,923	815,317	884,517	227,345	432,434	732,921	967,040
Animal census	÷ 75,675	÷ 76,087	÷ 79,899	÷ 80,299	÷ 24,608	÷ 94,260	÷ 173,914	÷ 173,372
Cost per animal	<u>\$ 8.7168</u>	<u>\$ 10.3687</u>	<u>\$ 10.2040</u>	<u>\$ 11.0156</u>	<u>\$ 9.2387</u>	<u>\$ 4.5877</u>	<u>\$ 4.2143</u>	<u>\$ 5.5778</u>
Misstated cost per animal	<u>\$ (1.74)</u>	<u>\$ (1.51)</u>	<u>\$ 2.88</u>	<u>\$ (5.03)</u>	<u>\$ 3.49</u>	<u>\$ 1.04</u>	<u>\$ 0.51</u>	<u>\$ 0.76</u>

<sup>1</sup> Costs for July 1, 2004, through September 30, 2004, are for animal shelter services provided under contract by the Humane Society of Santa Clara Valley.

<sup>2</sup> Costs for October 1, 2004, through June 30, 2005, are from the operations of the city’s new animal shelter.

The table below summarizes the audit adjustment related to care and maintenance for dogs and cats and for other animals after applying the mandate formula:

	Fiscal Year								
	1999-2000	2000-01	2001-02	2002-03	2004-05 <sup>1</sup>	2004-05 <sup>2</sup>	2005-06	2006-07	Total
Allowable:									
Cost per animal	\$ 6.98	\$ 8.86	\$ 13.09	\$ 5.98	\$ 12.73	\$ 5.63	\$ 4.72	\$ 6.34	
Eligible animals	× 3,321	× 4,320	× 2,691	× 3,540	× 1,623	× 9,783	× 13,017	× 14,379	
Total allowable	<u>\$ 23,181</u>	<u>\$ 38,275</u>	<u>\$ 35,225</u>	<u>\$ 21,169</u>	<u>\$ 20,661</u>	<u>\$ 55,078</u>	<u>\$ 61,440</u>	<u>\$ 91,163</u>	\$ 346,192
Claimed:									
Cost per animal	\$ 8.7168	\$ 10.3687	\$ 10.2040	\$ 11.0156	\$ 9.2387	\$ 4.5877	\$ 4.2143	\$ 5.5778	
Eligible animals	× 7,391	× 10,688	× 7,717	× 7,501	× 1,505	× 7,920	× 11,670	× 10,593	
Total claimed	<u>\$ 64,426</u>	<u>\$ 110,821</u>	<u>\$ 78,744</u>	<u>\$ 82,628</u>	<u>\$ 13,904</u>	<u>\$ 36,335</u>	<u>\$ 49,181</u>	<u>\$ 59,086</u>	495,125
Audit adjustment	<u>\$(41,245)</u>	<u>\$(72,546)</u>	<u>\$(43,519)</u>	<u>\$(61,459)</u>	<u>\$ 6,757</u>	<u>\$ 18,744</u>	<u>\$ 12,259</u>	<u>\$ 32,077</u>	<u>\$(148,933)</u>

<sup>1</sup> Costs for July 1, 2004, through September 30, 2004, are for animal shelter services provided under contract by the Humane Society of Santa Clara Valley.

<sup>2</sup> Costs for October 1, 2004, through June 30, 2005, are from the operations of the city’s new animal shelter.

The table below summarizes the audit adjustment related to care and maintenance for other animals after applying the mandate formula:

	Fiscal Year								Total	
	1999-2000	2000-01	2001-02	2002-03	2004-05 <sup>1</sup>	2004-05 <sup>2</sup>	2005-06	2006-07		
<b>Allowable:</b>										
Cost per animal	\$ 6.98	\$ 8.86	\$ 13.09	\$ 5.98	\$ 12.73	\$ 5.63	\$ 4.72	\$ 6.34		
Eligible animals	× 354	× 240	× 306	× 612	× 126	× 930	× 588	× 264		
Total allowable	\$ 2,471	\$ 2,126	\$ 4,006	\$ 3,660	\$ 1,604	\$ 5,235	\$ 2,775	\$ 1,674	\$	23,551
<b>Claimed:</b>										
Cost per animal	\$ 8.7168	\$ 10.3687	\$ 10.2040	\$ 11.0156	\$ 9.2387	\$ 4.5877	\$ 4.2143	\$ 5.5778		
Eligible animals	× 570	× 570	× 895	× 855	× 160	× 1,066	× 351	× 230		
Total claimed	\$ 4,969	\$ 5,910	\$ 9,129	\$ 9,422	\$ 1,478	\$ 4,891	\$ 1,479	\$ 1,283		38,561
Audit adjustment	\$ (2,498)	\$ (3,783)	\$ (5,124)	\$ (5,763)	\$ 126	\$ 343	\$ 1,296	\$ 391	\$	(15,010)

<sup>1</sup> Costs for July 1, 2004, through September 30, 2004, are for animal shelter services provided under contract by the Humane Society of Santa Clara Valley.

<sup>2</sup> Costs for October 1, 2004, through June 30, 2005, are from the operations of the city's new animal shelter.

### Recommendation

We recommend that the city establish and implement procedures to ensure that claimed costs include only eligible costs, are based on actual costs, and are properly supported.

### City's Response

The City disagrees with the reductions contained in the May 10, 2010 report as well as the slight increase in those reductions contained in the June 2, 2010 adjustment. The only claim years were the claimed amounts by the City for this component were reduced over-all were for the four year period where the City contracted with the Humane Society of Santa Clara Valley (FY 1999-2000 through FY 2002-03). However, the Controller disallowed \$597,550 of the \$2,259,528 in costs it determined were allowable for the above "bulleted" reasons. The City disagrees with that calculation.

While the June 2, 2010 e-mail calculation increased the Care and Maintenance component's allowable cost from \$362,001 to \$369,743 or \$7,732, to the extent that calculation is based on the retro-active application of the recent court case, we believe the City is not entitled to that increase.

### SCO's Comment

The finding and recommendation remain unchanged.

We issued a revised draft report on May 10, 2010. In that report, we determined that \$362,011 is allowable and \$171,675 is unallowable for the cost component of care and maintenance. The unallowable costs occurred because the city misstated animal census data, misstated the number of animals that died of natural causes during the holding period and those that were euthanized after the holding period, claimed ineligible costs, understated eligible costs, and understated indirect costs.

As a result of the change in the increased holding period due to the Appellate Court decision cited in Finding 1, we decreased the audit adjustment by \$7,732; from \$171,675 to \$163,943.

The city's characterization of the audit finding in its response is incorrect. The \$597,550 amount cited as an audit finding was actually the amount that city excluded from its claims for care and maintenance costs incurred for FY 2004-05 through FY 2006-07 for "non-reimbursable activities." The amounts are accurately labeled as claimed costs in the table that appears on page 13 of the revised draft audit report. We reduced the amount that the city excluded from its claims for care and maintenance costs by \$315,590; from \$597,550 to \$281,952. From the bulleted list cited on page 2 of the city's response, we determined that the activities of cleaning cages and kennels were eligible for reimbursement under the mandated program and adjusted the city's excluded costs accordingly. This information is included in the narrative of the audit finding for salaries and benefits on page 13 of the revised draft report.

The city also states that it disagrees with the reductions contained in the revised draft report. However, the city has not provided any specific information as to why it disagrees with the reductions for contract services and indirect costs.

The city also argues that the Appellate Court case stating that Saturday is not a business day should not be applied retroactively to the city's claims for the audit period. We disagree. The reasoning behind our disagreement is included in our response for Finding 2.

For the Care and Maintenance cost component of this mandated program, allowable cost calculations are based on the number of stray or abandoned animals that die during the increased holding period or are ultimately euthanized. As noted in our explanation for Finding 1, the increased holding period has been increased by one additional day as a result of the Appellate Court case. Our original calculations were based, in large part, on the number of animals that were euthanized on day six of the holding period and beyond. As a result of the court decision, we revised the calculations to include only animals that were euthanized on day seven of the holding period and beyond. Our original calculations were based, in large part, on the number of animals that were euthanized on day six of the holding period and beyond. As a result of the court decision, we revised the calculations to include only animals that were euthanized on day seven of the holding period and beyond.

**FINDING 4—  
Unallowable  
necessary and prompt  
veterinary care costs**

The city claimed \$1,239,667 for the cost component of Necessary and Prompt Veterinary Care for the audit period. We determined that \$314,538 is allowable and \$925,129 is unallowable. The costs are unallowable because they were not adequately supported and because the animal data information used to compute claimed costs was incorrect.

The following table summarizes the claimed, allowable, and unallowable costs for the audit period by fiscal year:

	Fiscal Year							Totals
	1999-2000	2000-01	2001-02	2002-03	2004-05	2005-06	2006-07	
Allowable costs	\$ 47,701	\$ 80,334	\$ 57,259	\$ 88,392	\$ 40,852	\$ —	\$ —	\$ 314,538
Claimed costs	233,094	244,891	194,901	207,645	164,716	106,064	88,356	1,239,667
Audit adjustment	<u>\$ (185,393)</u>	<u>\$ (164,557)</u>	<u>\$ (137,642)</u>	<u>\$ (119,253)</u>	<u>\$ (123,864)</u>	<u>\$ (106,064)</u>	<u>\$ (88,356)</u>	<u>\$ (925,129)</u>

The parameters and guidelines allow reimbursement, beginning January 1, 1999, for providing “necessary and prompt veterinary care” for stray and abandoned animals, other than injured cats and dogs given emergency treatment that die during the holding period or are ultimately euthanized during the holding periods specified in Statutes of 1998, Chapter 752.

“Necessary and prompt veterinary care” means all reasonably necessary medical procedures performed by a veterinarian or someone under the supervision of a veterinarian to make stray or abandoned animals “adoptable.” The following veterinary procedures, if performed, are eligible for reimbursement:

- An initial physical examination of the animal to determine the animal’s baseline health status and classification as “adoptable,” “treatable,” or “non-rehabilitatable;”
- A wellness vaccine administered to “treatable” or “adoptable” animals;
- Veterinary care to stabilize and or relieve the suffering of a “treatable” animal; and
- Veterinary care intended to remedy any applicable disease, injury, or congenital or hereditary condition that adversely affects the health of a “treatable” animal or that is likely to adversely affect the animal’s health in the future, until the animal becomes “adoptable.”

Eligible claimants are not entitled to reimbursement for providing “necessary and prompt veterinary care” to the following population of animals:

- Animals that are irremediably suffering from a serious illness or severe injury;
- Newborn animals that need maternal care and have been impounded without their mothers;
- Animals too severely injured to move or where a veterinarian is not available and it would be more humane to dispose of the animal;

- Owner-relinquished animals; and
- Stray or abandoned animals that are ultimately redeemed, adopted, or released to a nonprofit animal rescue or adoption organization.

#### *Veterinary Care Formula*

The parameters and guidelines allow costs to be reimbursed for this cost component using a formula-driven methodology. Only the costs of providing necessary and prompt veterinary care *during the required holding period* to animals that either died during the holding period or were euthanized after the holding period are reimbursable.

Allowable costs are determined by first dividing the eligible costs of providing veterinary care by the number of animals housed in the shelter during the required holding period. The result is the cost per animal for veterinary care. Similar to the care and maintenance formula, the next element of the formula is adding the number of stray and abandoned animals that died of natural causes during the holding period plus those animals that were euthanized after the required holding period. This total number of animals is then multiplied by the cost per animal. The resulting amount represents allowable costs for providing necessary and prompt veterinary care.

During the first four years of the audit period, the city contracted with the Humane Society of Santa Clara Valley for animal control services. Accordingly, costs incurred for these years consisted of contract services costs. The city continued contracting with the Humane Society through September 30, 2004, after which the city opened its own shelter. Costs incurred for veterinary care, beginning on October 1, 2004, consisted of salaries and benefits, materials and supplies, and related indirect costs. During the course of the audit, we made adjustments for salaries and benefits, contract services, and indirect cost amounts incurred by the city. We also adjusted the costs per animal. In addition, we made adjustments to the animal data that was used to claim costs.

#### *Eligible Animals*

For all years of the audit period, the city applied the calculated cost per animal for necessary and prompt veterinary care to the total number of dogs, cats, and other animals that were euthanized after the three-day waiting period. This is an incorrect application of the animal census data within the formula to claim costs for this cost component. The city also misstated the number of incoming stray animals that were housed in the animal shelter during the holding period for all years of the audit period.

We used the detailed animal census data that the city provided to determine the total number of animals housed at the facility during the required holding period, the number of stray and abandoned animals that died of natural causes during the required holding period, and the number of stray and abandoned animals that were ultimately euthanized after the required holding period. The number of eligible animals that we used each year is consistent with the number of animals used in the formulas for acquisition of new facilities and care and maintenance costs. Our

calculations took into consideration that the required holding period does not include Saturday as a business day. This is consistent with an Appellate Court decision dated March 26, 2010.

#### *Contract Services*

The city included \$2,793,555 in contract services costs in its veterinary care formulas for the audit period. We determined that the city underclaimed costs by \$3,288 for FY 2002-03. The costs were underclaimed due to a calculation error the city made when totaling the amount that the city paid the Humane Society for medical services.

The city contracted with the Humane Society of Santa Clara Valley for its animal control services until September 30, 2004. The contract states that the Humane Society provided shelter services and dead animal services to the city. The shelter services portion of the contract consisted of both shelter services and medical services. The medical services component consisted of:

- Provision of veterinary services 24 hours per day to treat and provide veterinarian care to stray, injured, or sick dogs, cats, and other impounded animals;
- Monitor quarantined biting animals; and
- For a fee to be determined by separate agreement, conduct vaccination clinics and have available, free of charge to the public, rabies control information.

The Humane Society's billings during FY 1999-2000 through FY 2001-02 only separated the total charges billed by shelter services and dead animal services. Beginning in FY 2002-03, the Humane Society's invoices separated costs billed for shelter services and medical services. Based on the amounts billed for that year, we determined that 56.62% of the contracted shelter costs in the previous years were for care and maintenance and 43.38% of the costs were for medical services.

We noted that the Humane Society's billings during FY 1999-2000 through FY 2004-05 did not include any details of veterinary services performed or when services were performed. In addition, the billings included in the city's claims did not include, based upon our examination, separate charges for conducting vaccination clinics, which would have been an unallowable activity under the mandated program.

As costs incurred for the quarantine of animals are not reimbursable under the mandated program, the Humane Society performed an analysis and determined that it cost \$200 to quarantine an animal. Accordingly, the city reduced contract services costs included in its veterinary care formulas by \$31,400 for FY 2001-02, \$25,200 for FY 2002-03, and \$2,800 for FY 2004-05 based on the number of animals quarantined at \$200 per animal.

The parameters and guidelines have very detailed requirements for this cost component related to services performed, when they are performed, and how the allowable costs are calculated. The Humane Society did not provide any detailed information related to veterinary care activities performed during the audit period. However, based on corroborating documentation, we included the contract costs in the calculation.

*Costs Incurred for FY 2004-05 through FY 2006-07*

The city included \$824,371 of costs in its veterinary care formulas for FY 2004-05 through FY 2006-07. These costs consisted of \$656,600 for salaries and benefits (adjusted for the cost of spay and neuter surgeries), \$92,426 for materials and supplies, and \$75,345 for indirect costs. We determined that all of these costs are unallowable. The costs are unallowable because they are not adequately supported.

Reimbursement is limited to the four specific activities identified above in the detailed language contained in the parameters and guidelines for this cost component. Although we concur that shelter staff performed reimbursable activities, the methodology employed by the city assumes that all medical costs incurred by its animal shelter are reimbursable after adjusting for the costs of spay and neuter surgeries. However, this methodology does not account for unallowable services and eligible services performed on ineligible animals. In addition, costs included in the veterinary care formula are allowable only for costs incurred for the treatment of eligible animals during the required holding period.

If the city performs a time study during the current period to determine costs incurred to perform the activities of conducting an initial physical exam of an animal to determine its baseline health status, as well as the cost of the administration of a wellness vaccine to treatable and adoptable animals, we will adjust the audit findings as appropriate. In addition, if the city is able to document actual costs incurred for eligible care performed on eligible animals during the required holding period for veterinary care to stabilize and/or relieve the suffering of a treatable animal and/or veterinary care intended to remedy any applicable disease, injury, or hereditary condition, we will adjust the audit findings as appropriate.

The following table summarizes the audit adjustment related to the cost component of necessary and prompt veterinary care after applying the mandate formula:

	Fiscal Year								Total
	1999-2000	2000-01	2001-02	2002-03	2004-05 <sup>1</sup>	2004-05 <sup>2</sup>	2005-06	2006-07	
<b>Allowable costs:</b>									
Costs incurred	\$ 505,397	\$ 604,442	\$ 698,466	\$ 768,138	\$ 220,400	\$ —	\$ —	\$ —	
Number of animals	÷ 12,355	÷ 11,135	÷ 11,564	÷ 11,115	÷ 3,032	÷ 10,544	÷ 16,154	÷ 15,991	
Cost per animal	\$ 40.91	\$ 54.28	\$ 60.40	\$ 69.11	\$ 72.69	\$ —	\$ —	\$ —	
Eligible animals	× 1,166	× 1,480	× 948	× 1,279	× 562	× 3,416	× 4,437	× 4,837	
Total allowable costs	\$ 47,701	\$ 80,334	\$ 57,259	\$ 88,392	\$ 40,852	\$ —	\$ —	\$ —	\$ 314,538
<b>Claimed costs:</b>									
Costs incurred	\$ 505,397	\$ 604,442	\$ 698,466	\$ 764,850	\$ 220,400	\$ 283,684	\$ 275,249	\$ 265,438	
Number of animals	× 13,393	× 11,877	× 12,783	× 2,520	× 3,433	× 9,928	× 15,441	× 16,529	
Cost per animal	\$ 37.7358	\$ 50.8918	\$ 54.6400	\$ 61.0900	\$ 64.2000	\$ 8.5743	\$ 17.83	\$ 16.06	
Eligible animals	× 6,177	× 4,812	× 3,567	× 3,399	× 780	× 4,012	× 5,950	× 5,502	
Total claimed costs	\$ 233,094	\$ 244,891	\$ 194,901	\$ 207,645	\$ 50,076	\$ 114,640	\$ 106,064	\$ 88,356	1,239,667
Audit adjustment	\$ (185,393)	\$ (164,557)	\$ (137,642)	\$ (119,253)	\$ (9,224)	\$ (114,640)	\$ (106,064)	\$ (88,356)	\$ (925,129)

<sup>1</sup> Costs for July 1, 2004, through September 30, 2004, are for animal shelter services provided under contract by the Humane Society of Santa Clara Valley.

<sup>2</sup> Costs for October 1, 2004, through June 30, 2005, are from the operations of the city’s new animal shelter.

Recommendation

We recommend that the city establish and implement procedures to ensure that claimed costs include only eligible costs, are based on actual costs, and are properly supported.

City’s Response

The City has separated its response to the two types of costs for the “veterinary care cost” component. The City has conducted a time study it requests be used to address the two sub-components described in item 2, below. The City has included a clarification of what it believes is a misunderstanding on the City’s calculation it used to claim the veterinary costs for the other two components in item 1, below.

1. Component for veterinary care to stabilize and or relieve the suffering of a “treatable” animal; and veterinary care intended to remedy any applicable disease, injury, or congenital or hereditary condition that adversely affects the health of a “treatable” animal or that is likely to adversely affect the animal’s health in the future, until the animal becomes “adoptable.”
  - a. The City believes the Controller’s is mistaken in its allegation that beginning with October 1, 2004, the City’s calculation of eligible animals receiving veterinary costs was wrong because it was an “incorrect application of the animal census data within the formula to claim costs for this cost component.” The City’s methodology to deduct its spay and neutering and costs and then applying the average cost to only those strays that died or were ultimately euthanized is proper and the Controller should reduce its proposed disallowance accordingly.
2. An initial physical examination of the animal to determine the animal’s baseline health status and classification as “adoptable,”

“treatable, or non-rehabilitatable; and a wellness vaccine administered to “treatable” or adoptable” animals.

- a. Attached is a time study completed by the City. Please review and make the necessary adjustments to the revised audits. The results of the time study are as follows:
  - i. Initial physical examinations:
    1. Cats: 4.60 minutes
    2. Dogs: 6.62 minutes
    3. Other: 2.0 minutes
  - ii. Administer wellness vaccine:
    1. Cats: 1.0 minutes
    2. Dogs: 1.36 minutes
    3. Other: 1.00 minutes

The City appreciates the Controller’s willingness to allow the City to complete the time study so late in this audit period. If there is a need for any further documentation the City is prepared to comply.

The June 2, 2010 revised computation for this component changed the allowable claim amount from \$541,673 to \$314,538 or a reduction of \$227,135. Once again, the City believes this reduction is incorrect to the extent those costs are related to the retro-active application of the appellate court case. The court case finding that Saturday should not be counted as a business day does not have any material effect of the City’s calculation of the veterinary care costs of stray dogs and cats that were euthanized.

#### SCO’s Comment

The finding and recommendation remain unchanged. However, the city has recently submitted raw time study data related to the activities of conducting an initial physical exam of an animal and the administration of a wellness vaccine to treatable or adoptable animals. We determined that the time study was properly conducted and will continue working with city representatives to obtain sufficient information in order to determine the appropriate amounts of allowable costs for the audit period.

We issued a revised draft report on May 10, 2010. In that report, we determined that \$541,673 is allowable and \$697,994 is unallowable for the cost component of Necessary and Prompt Veterinary Care. The costs are unallowable because they were not adequately supported and because the animal data information used to compute claimed costs was incorrect.

As a result of the change in the increased holding period due to the Appellate Court decision cited in Finding 2, we increased the audit adjustment by \$227,135; from \$697,994 to \$925,129.

In its response, the city states (under bullet point 1) that we are mistaken that the city used an incorrect application of the animal census data within the formula for this component. Instead of explaining why our analysis of animal census data is incorrect, the city states that its methodology of deducting costs for spaying and neutering, and applying average costs to the number of eligible animals is proper. We disagree.

The city provided worksheets during the course of the audit detailing how it calculated claimed costs for this cost component. In its worksheets, the city applied average costs incurred per animal for veterinary care to the number of dogs, cats, and other animals that died/were euthanized “after the 3 day waiting period.” The parameters and guidelines state that reimbursable costs for this cost component apply to the holding periods specified in Statutes of 1998, Chapter 752. The holding period specified is four business days after the day of impoundment (total of five business days), not the three-day waiting period noted on the city’s worksheets. Our calculations of eligible animals were based on this criteria.

The city believes that its methodology, beginning October 1, 2004, of deducting costs for spaying and neutering from total medical costs incurred and applying the average costs to the number of eligible animals, is proper. We disagree. Reimbursable costs for this cost component only apply to eligible medical procedures performed on stray and abandoned animals, other than injured cats and dogs given emergency treatment during the holding periods specified in Statutes of 1998, Chapter 752. The costs are reimbursable only to the extent that they apply to animals that die during the holding period or are ultimately euthanized (i.e., euthanized after the holding period). While the city properly deducted costs incurred for spaying and neutering, which are ineligible costs, the city’s methodology assumes that 100% of the remaining veterinary costs incurred were performed on eligible animals during the specified holding periods. The city has not yet provided any evidence supporting the extent to which it incurred veterinary costs for eligible animals during the specified holding periods. If the city is able to provide this information, we will modify the audit finding as appropriate.

In its response under bullet point 2, the city cites the average time increments spent to perform the activities of conducting an initial physical examination and administering a wellness vaccine. We have not yet received from the city the analysis of its time study data supporting the time increments mentioned in its response. As noted above, we determined that the time study was properly conducted and will continue working with city representatives to obtain sufficient information in order to determine the appropriate amounts of allowable costs for the audit period.

The city also believes that the Appellate Court case stating that Saturday is not a business day should not be applied retroactively to the city’s claims for the audit period. We disagree. The reasoning behind our disagreement is included in our response for Finding 2.

**FINDING 5—  
Overstated offsetting  
revenues**

The city included \$348,763 of offsetting revenues in its claims for the audit period. The offsets included \$186,870 for FY 1999-2000 and \$145,293 for FY 2000-01 that were made for “excess license revenue.” We determined that the city was not required to offset these amounts on its claims.

The remaining offsetting revenue of \$16,600 was included in the city’s claim for FY 2004-05. The claim states that the amount represents 7.5% for “other contracting cities.” However, the cities are not identified on the claim and no documentation was provided enabling us to determine how this amount was calculated. We noted that various cities contracted with the City of San José for animal shelter services during FY 2004-05 through FY 2006-07, as noted below. These cities also filed mandated cost claims with the State for a portion of the contract costs paid. These claim amounts may or may not be revenue offsets applicable to the City of San José’s claims for those years.

The following table summarizes overstated offsetting revenues:

	Fiscal Year			Total
	1999-2000	2000-01	2004-05	
Audit adjustment	\$ 186,870	\$ 145,293	\$ 16,600	\$ 348,763

*Requirement for Revenue Offsets—Licensing Activities*

Offsetting revenues are reported when revenues received exceed expenditures incurred for the operation of an animal shelter. When this happens, a portion of the revenues received are used to fund mandated activities. Accordingly, outside revenues received should be applied first to general operating expenses before being applied to mandated expenses.

We reviewed the city’s contract with the Humane Society of Santa Clara Valley and noted that there is a separate section (Section 5) that addresses activities for animal licensing. The Humane Society collected applicable fees and completed license applications for animals adopted and then referred owners to the city for licensing. The city provided worksheets for FY 1999-2000 and FY 2000-01 showing the amount of licensing revenues received less the administrative costs incurred to process animal licenses. As the revenues received exceeded expenses incurred for licensing activities, the city offset the “excess” amount on its Animal Adoption Program claims. However, the city’s analysis did not include the other general operating expenses incurred pursuant to its contract with the Humane Society. When these expenditures are included, it is clear that total revenues received by the city did not exceed general operating expenses incurred for the operation of an animal shelter. Therefore, no offsetting revenue was required to be reported in the city’s claims for excess license revenue.

*Contracts with Other Cities*

The city had contracts with four other cities (Los Gatos, Saratoga, Milpitas, and Cupertino) during the audit period to provide animal shelter services. These cities also filed mandated cost claims with the State for the Animal Adoption Program.

The following table summarizes the mandated cost claims filed under the Animal Adoption Program by these four cities during the audit period:

Contracting City	Fiscal Year			Totals
	2004-05	2005-06	2006-07	
Los Gatos	\$ 23,086	\$ 2,900	\$ 2,885	\$ 28,871
Saratoga	22,733	2,064	1,252	26,049
Milpitas	31,136	32,002	14,209	77,347
Cupertino	—	2,174	2,259	4,433
Totals	<u>\$ 76,955</u>	<u>\$ 39,140</u>	<u>\$ 20,605</u>	<u>\$ 136,700</u>

We noted that a significant portion of the claims for FY 2004-05 represented recoveries for capital contributions made to the City of San José for construction of a new cat kennel facility (\$20,121 each for the cities of Saratoga and Los Gatos based on capital contributions of \$300,000 each). The remaining costs claimed in that year and all of the costs claimed in the subsequent two years by these two cities were for the cost categories of care and maintenance of animals and necessary and prompt veterinary services. Costs claimed by the City of Milpitas were for the cost components of care and maintenance, necessary and prompt

veterinary care, and holding period. Costs claimed by the City of Cupertino were for the cost components of care and maintenance (dogs and cats only) and holding period.

We were unable to determine if any contract revenues received by the City of San José were for mandated activities. Therefore, we request that the City of San José identify, in writing, what portion of its mandated costs, if any, was funded by the contracting cities.

If the City of San José determines that a portion of the contract revenues received in any of the applicable three years was used to fund mandated activities, we will offset the related portion on the City of San José's Animal Adoption Program claims and allow the corresponding amounts for claiming by the contracting cities on their Animal Adoption Program claims. However, if the City of San José does not respond or determines that none of the contract revenue received was used for mandated activities (meaning that all of the revenue was used for the general operating expenses of its shelter), we will reduce the Animal Adoption Program claims filed by the contracting cities to \$0.

### Recommendation

We recommend that the city determine the amount of applicable offsetting revenues that it received during the audit period. We also recommend that the city establish and implement procedures to ensure that offsetting revenues are included in the city's claims to the extent that revenues received from contracting cities were used to fund mandated activities.

### City's Response

The City agrees that license revenues did not exceed expenditures incurred for the operation of the animal shelter and should not have been used to offset mandated costs.

### SCO's Comment

The city concurs with our determination that license revenues received were not an applicable offset to the city's claims for FY 1999-2000 and FY 2000-01.

However, the city has not yet responded to the portion of this audit finding related to contract revenues received from the cities of Los Gatos, Saratoga, Milpitas, and Cupertino. As we noted in the body of the audit finding, the city did not provide any support for the offsetting revenues. Therefore, we reported no offsetting revenues in the audit report. Consequently, any revenues received by the cities of Los Gatos, Saratoga, Milpitas, and Cupertino are applied entirely to the general operating expenses of the city shelter.

**OTHER ISSUES**

In its response to the revised draft audit report, the city commented on the presentation of our audit findings, the amount of time given to respond to the draft report, and the proper application of statute to the time period within which the city’s claims could be audited. We will address the city’s comments in the order that they appear in its response.

**ISSUE 1—  
Audit presentation**

City’s Response

Due to the number of years that were audited, the Controller’s changes in its findings, and the way the findings were presented in summary format, it is very difficult to match the individual fiscal year claims filed with the detail findings of the May 10, 2010 draft. In order for the City to be more specific in its response the many findings, it would be preferable if the Controller would issue the audit findings separately for each of the seven claims filed and address the specific reasons for the disallowance in each claim.

SCO’s Comment

We concur that it is difficult to match the details of the audit findings to a particular fiscal year’s claim based on the summary information provided in the audit report. We have attempted to provide as much clarity as possible concerning the nature of the findings as this format will allow. However, we do not agree with the city’s suggestion that we should issue separate audit findings for each of the seven claims included in the audit period. For the most part, the reasons for unallowable costs within each cost component of the mandated program are the same for each year of the audit period. By using the format that the city proposes, we would be repeating this information over and over again unnecessarily. Instead, we have already communicated our willingness to work with city representatives and provide whatever detailed information may be required in order for them to determine the propriety of our audit findings.

**ISSUE 2—  
Time period to  
respond**

City’s Response

The City has attempted to provide the Controller with its response within the short time it has been given to respond to the revised draft. While the short period of time given to local agencies to respond to the Controller audits is not unique to the City, the Controller is normally willing to extend that limitation. It is our understanding the League of California Cities and California State Association of Counties Advisory Committee on State Mandates has been meeting with the Controller to seek a change in what particularly large agencies see as an overly limited time to provide its response. That time period is based on the Controller’s policy and not statute. In the future, for audits of this magnitude, we recommend the Controller consider provide additional time to respond.

SCO’s Comment

The city suggests that we consider providing additional time to respond to audits of this magnitude. Ordinarily, we work with auditees concerning their requests to extend the time period within which to respond to the audit findings. However, we were up against a time constraint for which this audit had to be issued. We have already

communicated our willingness to work with city representatives in order to adjust the audit findings as appropriate based on additional information provided by the city in support of its claims.

**ISSUE 3—  
Time period subject  
to audit**

City's Response

The City appreciates the cooperation of the Controller's staff during this very lengthy audit. This audit, covering so many years, for such a comprehensive and complicated state mandate program, has been difficult for all parties. The City believes it was inappropriate for the Controller to apply the statute that extended the period for which a claim can be audited to this program. The City, and it expects most, if not all local agencies, believes the retro-active application of the statutory change in the time period the state can audit claims from three years after a claim is filed to three years after the state makes its first payment is unfair. It is particularly questionable for the state to make such a drastic change in a budget trailer bill which does not allow for any public input or consideration by a policy committee of the legislature. It was that statutory change that allowed the Controller to conduct this audit for so many years.

SCO's Comments

In its response, the city states its belief that it is inappropriate to apply the statute that extended the period for which a claim can be audited for this mandated program. Specifically, the city is referring to Government Code section 17558.5, subsection (a), which was amended by Statutes of 2002, Chapter 1128, Section 14.5 and was effective as of January 1, 2003. The statute states:

A reimbursement claim for actual costs filed by a local agency or school district pursuant to this chapter is subject to the initiation of an audit by the Controller no later than three years after the date that the actual reimbursement claim is filed or last amended, whichever is later. However, if no funds are appropriated or no payment is made to a claimant for the program for the fiscal year for which the claim is filed, the time for the Controller to initiate an audit shall commence to run from the date of initial payment of the claim.

The city goes on to state that since this version of the statute was adopted by the legislature within a budget trailer bill without public input or consideration by a policy committee of the legislature, it is inappropriate for us to apply the provisions of the statute.

We disagree with the city's conclusion. This is not the proper forum for disagreements with the adoption of statutes by the State legislature. This issue should be addressed to the appropriate legislative body. We believe the audit period included in this audit is in compliance with the applicable version of Government Code section 17558.5, subsection (a).

**Attachment—  
City's Response to  
Draft Audit Report**

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June 14, 2010

Jeffrey V. Brownfield  
Chief, Division of Audits  
California State Controller  
300 Capitol Mall, Suite 318  
Sacramento, CA 95814

RE: Revised Draft Audit Report Issued May 10, 2010 & June 2, 2010 Revisions

Dear Mr. Brownfield:

The City of San Jose has reviewed the revised draft audit report issued on May 10, 2010, which replaces the previously issued draft report dated February 20, 2009. It has also reviewed the written comments submitted on June 2, 2010 by e-mail from the State Controller's Division of Audits which makes revisions to the May 10, 2010 draft report. That report is for the State Controller audit of the costs claimed by the City of San Jose for the legislatively mandated Animal Adoption Program (Chapter 752, Statutes of 1998 and Chapter 313, Statutes of 2004) for the period of July 1, 1999, through June 30, 2007. This letter contains the City's response to each of the Controller's five findings.

Due to the number of years that were audited, the Controller's changes in its findings, and the way the findings were presented in summary format, it is very difficult to match the individual fiscal year claims filed with the detail findings of the May 10, 2010 draft. In order for the City to be more specific in its response the many findings, it would be preferable if the Controller would issue the audit findings separately for each of the seven claims filed and address the specific reasons for the disallowance in each claim.

The City has attempted to provide the Controller with its response within the short time it has been given to respond to the revised draft. While the short period of time given to local agencies to respond to the Controller audits is not unique to the City, the Controller is normally willing to extend that limitation. It is our understanding the League of California Cities and California State Association of Counties Advisory Committee on State Mandates has been meeting with the Controller to seek a change in what particularly large agencies see as an overly limited time to provide its response. That time period is based on the Controller's policy and not statute. In the future, for audits of this magnitude, we recommend the Controller consider provide additional time to respond.

**Finding 1: Misclassified policies and procedures**

**CONTROLLER:** Determined that the \$36,907 the City costs claimed in its FY1999-2000 claim were misclassified and should have been included in the formula for claiming Acquiring Space and Facilities costs instead.

**CITY RESPONSE:** Agree with the Controller' finding that the costs are better included under the Acquiring Space and Facilities component and support the Controller's finding.

**FINDING 2: Misstated acquiring space and facilities costs**

**CONTROLLER:** In the May 10, 2010, revised report the Controller determined that the City understated costs by the net amount of \$117, 287 and the allowable costs was \$2,417,393. The June 2, 2010 e-mail recalculated those costs based on a recent appellate court case which found that Saturday is not a business day and instead found that the allowable cost was \$1,906,126 or \$511,267 less.

**CITY RESPONSE:** The City believes the calculation in the May 10, 2010 is nearly correct and the change contained in the June 2, 2010 e-mail is incorrect. The City does not believe the court case, filed March 26, 2010 should be applied retroactively to the year in which the costs were incurred, namely the 1999-2000 through 2004-05 fiscal years.

The City also questions the Controller challenge of the \$36,239 in salaries and benefits which the Controller disallowed based on variances between the City's PeopleSoft and FAMIS systems included in the FY 1999-2000 and FY 2000-2001 claims by purporting they were not adequately supported.

**FINDING 3: Unallowable care and maintenance costs**

**CONTROLLER:** In the May 10, 2010 draft report the Controller determined that for the seven years of the audit the City claimed \$533,686 for care and maintenance \$362,000 is allowable and that \$171,675 is unallowable. The Controller alleges the unallowable costs occurred because the City misstated animal census data, misstated the number of animals that died of natural causes during the holding period and those that were euthanized after the holding period, claimed ineligible costs, understated eligible costs, and understated indirect costs. The Controller, on page 13 of the May 10, 2010 report, determined that the City overstated the non-reimbursable activities by \$315,598 relating to the following unrelated activities:

- Cleaning adoptable rabbit and small animal cages
- Cleaning adoptable cat cages
- Cleaning adoptable dog kennels
- Adoption counseling
- Euthanasia

- Intake of owned animals

The Controller goes on to say, costs for reimbursable activities were overstated because the activities of adoption counseling and euthanasia are the only costs that should have been excluded.

**CITY RESPONSE:** The City disagrees with the reductions contained in the May 10, 2010 report as well as the slight increase in those reductions contained in the June 2, 2010 adjustment. The only claim years where the claimed amounts by the City for this component were reduced over-all were for the four year period where the City contracted with the Humane Society of Santa Clara Valley (FY 1999-2000 through FY 2002-03). However, the Controller disallowed \$597,550 of the \$2,259,528 in costs it determined were allowable for the above "bulleted" reasons. The City disagrees with that calculation.

While the June 2, 2010 e-mail calculation increases the Care and Maintenance component's allowable cost from \$362,001 to \$369,743 or \$7,732, to the extent that calculation is based on the retro-active application of the recent court case, we believe the City is not entitled to that increase.

#### **FINDING 4: Unallowable necessary and prompt veterinary care costs**

**CONTROLLER:** Determined that \$541,673 of the \$1,239,667 is allowable and \$697,994 is unallowable. The costs are unallowable because they were not adequately supported and because the animal data information used to compute claimed costs was incorrect.

**CITY RESPONSE:** The City has separated its response to the two types of costs for the "veterinary care cost" component. The City has conducted a time study it requests be used to address the two sub-components described in item 2, below. The City has included a clarification of what it believes is a misunderstanding on the City's calculation it used to claim the veterinary costs for the other two components in item 1, below.

1. Component for veterinary care to stabilize and or relieve the suffering of a "treatable" animal; and veterinary care intended to remedy any applicable disease, injury, or congenital or hereditary condition that adversely affects the health of a "treatable" animal or that is likely to adversely affect the animal's health in the future, until the animal becomes "adoptable."
  - a. The City believes the Controller's is mistaken in its allegation that beginning with October 1, 2004, the City's calculation of eligible animals receiving veterinary costs was wrong because it was an "incorrect application of the animal census data within the formula to claim costs for this cost component." The City's methodology to deduct its spay and neutering and costs and then applying the average cost to only those strays

that died or were ultimately euthanized is proper and the Controller should to reduce its proposed disallowance accordingly.

2. An initial physical examination of the animal to determine the animal's baseline health status and classification as "adoptable," "treatable," or non-rehabilitatable; and a wellness vaccine administered to "treatable" or adoptable" animals.
  - a. Attached is a time study completed by the City. Please review and make the necessary adjustments to the revised audits. The results of the time study are as follows:
    - i. Initial physical examinations:
      1. Cats: 4.60 minutes
      2. Dogs: 6.62 minutes
      3. Other: 2.0 minutes
    - ii. Administer wellness vaccine:
      1. Cats: 1.00 minutes
      2. Dogs: 1.36 minutes
      3. Other: 1.00 minutes

The City appreciates the Controller's willingness to allow the City to complete the time study so late in this audit period. If there is a need for any further documentation the City is prepared to comply.

The June 2, 2010 revised computation for this component changed the allowable claim amount from \$541,673 to \$314,538 or a reduction of \$227,135. Once again, the City believes this reduction is incorrect to the extent those costs are related to the retro-active application of the appellate court case. The court case finding that Saturday should not be counted as a business day does not have any material effect on the City's calculation of the veterinary care costs of stray dogs and cats that were euthanized.

#### **FINDING 5: Overstated offsetting revenues**

**CONTROLLER:** Determined that the City was not required to off-set the \$186,870 for FY 1999-2000 and \$145,293 for FY 2000-01 of offsetting revenues that were made for "excess license revenue." The Controller questioned the \$16,600 for FY 2004-05 and \$345,763 to off-set the City's claim for revenue received and concluded the claim amounts "may or may not be revenue offsets applicable to the City for those years.

**CITY RESPONSE:** The City agrees that license revenues did not exceed expenditures incurred for the operation of the animal shelter and should not have been used to offset mandated costs.

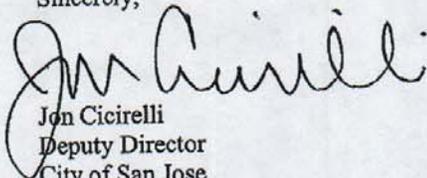
**SUMMARY:**

The City appreciates the cooperation of the Controller's staff during this very lengthy audit. This audit, covering so many years, for such a comprehensive and complicated state mandate program, has been difficult for all parties. The City believes it was inappropriate for the Controller to apply the statute that extended the period for which a claim can be audited to this program. The City, and it expects most, if not all local agencies, believes the retro-active application of the statutory change in the time period the state can audit claims from three years after a claim is filed to three years after the state makes its first payment is unfair. It is particularly questionable for the state to make such a drastic change in a budget trailer bill which does not allow for any public input or consideration by a policy committee of the legislature. It was that statutory change that allowed the Controller to conduct this audit for so many years.

The City understands the Controller must complete this audit within the two-year statutory deadline, and therefore cannot extend the time for the City to respond to the draft audit. However, due to unusual nature of this audit, namely the number of years audited, the fact that the City contracted for services for approximately four of the seven years, the retroactive application of a March 2010 appellate court ruling, and a myriad of other factors, the City expects to seek a re-opening of the audit later this year.

The City looks forward to the Controller's consideration of the various points it has raised in response to the draft audit report and anticipates restoration of most, if not all the disallowances the City has challenged.

Sincerely,



Jon Cicirelli  
Deputy Director  
City of San Jose  
Animal Care and Services

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