

City of Palo Alto  
*Office of the City Auditor*

Asset Capitalization Review –  
Construction in Progress

August 10, 2021



## Agenda

- Project background
- Audit review/approval
- Questions & discussion

*The CAO thanks the Administrative Service Department of their work on this audit activity – **THANK YOU!***

## Project background

Objectives for the audit activity include:

- Identify the cause of the \$12.6M capital asset adjustment made during FY2020
- Determine whether adequate controls are in place to ensure that costs are properly categorized and recorded in accordance with the accounting policy and relevant accounting standards

### Information Gathering

The CAO evaluated the CIP adjustment worksheets, FY2016-FY2021 Adopted Capital budgets and interviewed accountants.

### Analysis

The CAO interviewed key personnel to identify system capabilities, system configuration and project setup in SAP.

### Control Review and Recommendations

Finally, the CAO evaluated controls and identified opportunities for improvement.

## Findings

The cause of the **\$12.6M** adjustment made to the CIP account in FY2020 to remove improperly capitalized costs was incomplete execution of a key internal control, a periodic review and correction of the costs in the CIP account, in previous years.

### Identified Fixed Assets

- Public Art
- Software, machine, and installation service that improved parking
- Newly installed streetlights
- Building automation

### CIP Balances – Governmental Fund / Internal Service Fund


As of	6/30/2015	6/30/2016	6/30/2017	6/30/2018	6/30/2019	6/30/2020
Balance	\$39,333K	\$46,527K	\$62,661K	\$69,343K	\$104,465K	\$139,365K

# Recommendations

#	Observation	Recommendation
1	The Office of Management Budget sets up Capital projects using WBS Elements to track Design and Construction tasks. All costs are tracked as capital costs.	Explore use of technology/SAP to segregate capital costs and expenses.
2 & 3	All costs are settled to the construction in progress account on a monthly basis whether or not costs are capitalized, causing more costs to be reviewed and removed from the CIP account than necessary.	<p>Costs recorded in the CIP account should be reviewed periodically to ensure expenses are removed and costs for the completed assets are reclassified in a timely manner.</p> <p>Improved internal controls for more frequent review of capital improvement adjustments for accounts. The accounting team should implement a mechanism to receive the status of project completion and assets place in service from the responsible departments in a timely manner.</p>
4	The Fixed Asset Policy for General Fund and Internal Service Fund has not been reviewed and updated since March 2012 and includes. The Enterprise Fixed Asset Policy has not been updated since March 2014	Accounting should enhance the construction in progress section in each policy to provide guidance regarding the process to the accounting team and the responsible parties.

## Next Steps

- Approval by the Policy Services Committee
- Present the report to City Council
  - Council's acceptance of the report acts as a finalization of the audit
- Periodic review of findings to ensure recommended findings are accepted and adopted



*Questions & discussion*





Thank you!

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