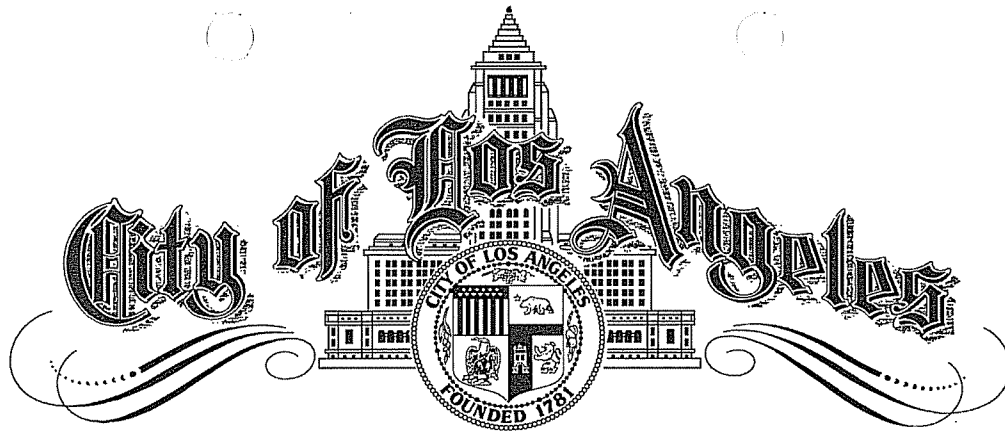




OFFICE OF
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May 19, 2008

The Honorable Antonio Villaraigosa
The Honorable Rockard J. Delgadillo
The Honorable Members of the City Council

Today, I release an operational and compliance audit of the Los Angeles Police Commission's oversight and management of the City's auto impound contracts. The Police Commission is responsible for administering these contracts with private businesses that are designated as Official Police Garages (OPGs).

In terms of providing a needed service, the OPGs operate well for both the City and the public. As in most audits, however, we found room for improvement in areas where monies were owed or where the City could improve its oversight.

Fifteen of the 20 OPGs did not include lien processing fees in their gross revenues, resulting in underpayment of about \$1 million in franchise fees due to the City. We disagree with the OPG Association's assessment that the lien fee should not be considered revenue. All charges paid by a customer result in additional receipts by the OPG, and therefore contribute to gross revenue. Generally Accepted Accounting Principles require businesses to record the recovery of reimbursable expenses as revenue.

Because there are two separate entities involved with the OPG contracts, the Office of Finance and the Police Commission, there have been problems...with fiscal monitoring: inconsistencies in reporting and underpayment of City fees. Clearly, the LAPD needs to provide the needed resources to properly monitor this contract. Since my March 2007 audit of the LAPD's fiscal operations found a division in disarray, the Police Commission probably should turn to outside consultants. Hopefully these issues can be quickly remedied as can the collection of past monies owed the City.

Sincerely,

LAURA N. CHICK
City Controller

MAY 21 2008

AUDITS & GOVERNMENTAL
EFFICIENCY



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May 19, 2008

Mr. Richard Tefank, Executive Director
Los Angeles Police Commission
150 N. Los Angeles St., Room # 150
Los Angeles, CA 90012

Dear Mr. Tefank:

Enclosed is a report entitled "Review of Auto Impound Contracts at the Los Angeles Police Commission." A draft of this report was provided to your office on May 2, 2008. We considered your comments prior to finalizing this report.

Please review the final report and advise the Controller's Office by June 19, 2008 on planned actions you will take to implement the recommendations. If you have any questions or comments, please contact me at (213) 978-7392.

Sincerely,

Farid Saffar, CPA
Director of Auditing

Enclosure

cc: Anthony Pacheco, President, Board of Police Commissioners
Robin Kramer, Chief of Staff, Office of the Mayor
Arif Alikhan, Deputy Chief of Staff, Office of the Mayor
Karen L. Sisson, City Administrative Officer
Karen E. Kalfayan, City Clerk
Gerry F. Miller, Chief Legislative Analyst
Antoinette D. Christovale, Director, Office of Finance
Independent City Auditors



City of Los Angeles Office of the Controller

REVIEW OF AUTO IMPOUND CONTRACTS AT THE LOS ANGELES POLICE COMMISSION

May 19, 2008

Laura N. Chick
City Controller

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REVIEW OF AUTO IMPOUND CONTRACTS AT THE LOS ANGELES POLICE COMMISSION

EXECUTIVE SUMMARY

The Controller's Audit Division has completed an operational and compliance review of the Los Angeles Police Commission's oversight and management of the City's auto impound contracts. The LAPD Commission Investigation Division (CID) is responsible for administering these contracts with private businesses that are designated as an Official Police Garage (OPG). The overall objective of the audit was to ensure that CID manages the OPG contracts in a fair and consistent manner, and that processes are in place to ensure that OPGs comply with their contract requirements.

BACKGROUND

An LAPD auto impound contractor operates as an OPG for a specific LAPD geographic area. The Los Angeles Municipal Code (LAMC) defines an OPG as a towing and garage business selected by the City to remove and store vehicles at the direction of any Police Officer or Traffic Officer employed by the City of Los Angeles including officers of the Port, Airport and Housing Authority. Situations that require OPG services may include the removal, towing and storage of illegally parked vehicles, abandoned vehicles, vehicles disabled as the result of traffic accidents, vehicles seized for evidentiary examination, abated vehicles, and vehicles subject to forfeiture proceedings.

The City currently has 20 OPG contracts in effect that service the 18 LAPD geographical areas. Eighteen of these contracts provide standard duty towing services and two provide heavy duty towing services. The contracts require OPGs to provide services 24-hours a day, 7-days a week, and within a 20-minute response time from when an OPG dispatcher receives a request.

During 2006, OPGs impounded approximately 175,000 vehicles at the City's direction. OPGs charge vehicle owners for towing and storage costs, as well as other fees and taxes, that are paid when their vehicle is redeemed. An OPG may also recover their charges when an unredeemed vehicle is sold at auction or for junk to an auto dismantling yard.

In accordance with the terms of their contract, OPGs must remit to the City's Office of Finance the taxes and fees collected on behalf of the City, as well as an additional franchise fee assessed on the OPG's gross revenues. During 2006, OPGs remitted

approximately \$14 million to the City, comprised of the vehicle release fees, City parking occupancy tax, vehicle forfeiture fees, and the franchise fee.

In performing the audit, we interviewed responsible LAPD, CID and OPG personnel; and reviewed contract provisions and applicable policies, procedures, rules, and regulations. Our detailed review of two specific contracted OPGs required that we examine their documentation and interview their personnel; however, our auditee was the CID of the Police Commission. Therefore, our findings and recommendations are addressed to the Police Commission.

SUMMARY OF AUDIT RESULTS

Overall, we noted that City policy was followed in the solicitation, selection, and award of the current OPG contracts. In addition, we found that the OPGs reasonably provided the services as required by the contract. We found that they met the required response time, provided services 24-hours, seven days a week, kept the impounded vehicles and their facilities in accordance with the contract requirements, submitted required reports, and maintained adequate documentation.

The CID of the Police Commission reasonably monitored the OPGs' program operations. However, fiscal monitoring did not occur. Neither the CID as the OPG contract administrator, nor the Office of Finance that (OOF) collected the fees, periodically reviewed the OPGs' fiscal operations to ensure the accuracy of fees remitted.

According to CID, because the Municipal Code specifies that OPGs are to remit all fees directly to OOF, and states that LAPD is responsible for investigating and auditing records related to the sale of forfeited vehicles, CID believed that OOF was to ensure the accuracy of all fees remitted by OPGs. In addition, CID representatives stated that they did not have access to OPGs' financial information, so could not monitor for fiscal compliance¹.

As a result of inadequate financial oversight, the OPGs had varied interpretations of their fiscal requirements which led to inconsistent reporting practices and an underpayment of City fees. Over the five-year life of the contracts, we estimate the City is due more than \$1 million.

Most OPG contracts will expire in 2009. We believe it is imperative that the Police Commission consider the issues presented in this report and address them during the new contract negotiations with OPGs.

¹ CID stated that due to taxpayer confidentiality, OOF would not share the OPGs' fee remittance information. OOF representatives recently clarified that while they cannot provide City tax remittance data, they will share relevant fee information with CID, as pertains to OPGs' fiscal operations and reporting.

KEY FINDINGS

- **15 OPG contractors did not include lien processing fees in their gross revenues, resulting in underpayment of about \$1 million in franchise fees due to the City.**

Most OPGs did not properly include the lien processing fee charged to owners or buyers of a particular vehicle in their gross revenue subject to the City's franchise fee, stating this was a cost recovery charge, rather than a source of revenue. The approximate underpayment due to unreported lien processing fees was \$207,000 for FY 2007. Projected over the entire contract period, the underpayment of OPG franchise fees paid to the City is over \$1 million.

- **City Vehicle Release Fees are not remitted for vehicles sold at auction.**

The City does not currently require the \$48 Vehicle Release Fee, which is assessed to cover City administrative costs for City-directed impounds, to be remitted when unredeemed vehicles are sold at auction. However, it appears that this fee can be collected when the auction proceeds exceed the OPG's total charges, as allowed by the California Vehicle Code. Using conservative estimates based on 2006 data, this could increase revenue to the City by more than \$70,000.

- **Inadequate OPG dispatch and accounting systems and controls provided inaccurate data, resulting in underpaid fees.**

Computerized dispatch and manual accounting systems of a sample OPG were inadequate. For example, we noted that numerous unsupported manual adjustments were made on computer reports generated from the dispatch system before they were recorded in the manual accounting ledger. In addition, some amounts were not included in the accounting records, which were used as a basis to report and remit fees to the City. We also found that inaccurate data was recorded on the quarterly Vehicle Release Fee reporting forms, resulting in a possible underpayment of approximately \$25,000.

Inadequacy of the dispatch and financial systems was also self-reported by other OPGs. For example, one OPG reported that a breakdown in accounting practices resulted in its failure to include the proceeds from some auction sales in their gross receipts, and has estimated that it underpaid City franchise fees by approximately \$28,000 in FY 2007. Another OPG reported that their inadequate dispatch system and insufficient controls over cash receipts allowed a key employee to embezzle approximately \$170,000 over an eighteen-month period. Corresponding underreported and underpaid City fees and parking taxes totaled approximately \$25,000.

- **Lack of fiscal monitoring of OPGs led to inconsistencies in reporting and underpayment of City fees.**

The LAPD CID is charged with the overall oversight of OPGs, including compliance with contractual fiscal requirements. However, City ordinance requires OPGs to remit the required fees directly to the Office of Finance. Neither agency reviews the accuracy of fees remitted by OPGs, which has led to inconsistent interpretation of fiscal requirements among OPGs, and underpayments to the City.

- **Non-adherence to LAPD impound procedures resulted in avoidable City payments to OPGs.**

When a vehicle impounded at the City's direction remains stored by the OPG for an unreasonable amount of time at no fault of the registered owner, the owner pays only a portion of the total charges as determined by an impound hearing officer. LAPD must reimburse the OPG for the balance of the charges. During FY 2007, LAPD reimbursed \$289,000 to various OPGs. Based on our audit sample, we found that 67% of the amount paid by LAPD could have been avoided through the officers' adherence to LAPD internal procedures.

REVIEW OF REPORT

We discussed the findings contained in this report with LAPD CID and the two sample OPGs on April 16 and 21, 2008. We provided a draft report to CID on May 2, 2008 and held an exit conference on May 7, 2008. We considered CID's comments before finalizing the report.

We appreciate and thank the management and staff of CID, LAPD and the OPGs for their cooperation and assistance during the audit.

TABLE of RECOMMENDATIONS

RECOMMENDATIONS	PAGE REF.
Section I: IMPACT ON CITY REVENUE	
The CID of the Police Commission should: 1. Pursue recovery of underpayments from OPGs for unreported lien processing fees from contract inception to date. 2. Communicate to OPGs to ensure proper reporting of "gross revenue" that is subject to the 7% franchise fee. 3. Work with the City Attorney to amend the pertinent Ordinance provision and include in the OPG contract the provision of the CA Vehicle Code Section 22850.5(b)(1) that states that the City's administrative cost (Vehicle Release Fee) will be recovered from lien sales when there is an excess amount to cover the OPGs' total charges and administrative costs. 4. Work with the Office of Finance to revise the quarterly report form pertaining to the Vehicle Release Fee to include vehicles sold at auction where sale proceeds exceed OPG total charges and proper administrative costs. 5. Request all OPGs to report all credit card fees and other bank charges that were deducted from gross receipts since contract inception and remit the corresponding 7% franchise fees to the Office of Finance.	13 13 14 15 15
Section II: OPG SYSTEMS CAPABILITY	
The CID of the Police Commission should: 6. Require OPGs to properly prepare their quarterly returns for the Vehicle Release Fee. 7. Request all OPGs to report any lien sale proceeds, including sales to wrecking or dismantling yard, that were not included in their reported gross receipts since contract inception and remit applicable franchise fees to the Office of Finance. 8. Timely inform all OPGs of the recent issues/problems pertaining to financial reporting that were brought to its attention by other OPGs.	18 18 18

RECOMMENDATIONS	PAGE REF.
9. Request all OPGs to self-assess their own dispatch and financial systems and report if they have similar or other related problems. 10. Work with OPGs that have problems/issues in their systems and reporting to ensure that those are properly addressed. 11. Ensure that all OPGs have reliable and adequate computerized dispatch and accounting systems in place that have a capability to track and record all transactions and charges affecting an impounded vehicle. 12. Ensure that all OPGs properly support their quarterly reported fees to the City with a reconciliation of data in the dispatch system with records in the financial system.	18 18 18 19
Section III: FINANCIAL OVERSIGHT	
The CID of the Police Commission should: 13. Ensure that OPGs comply with the contract requirements pertaining to payment of fees to the City through periodic reviews of their fiscal operations. 14. Consider coordinating with LAPD's Fiscal Operations Division and/or outside consultant(s) to conduct adequate fiscal monitoring of OPGs. 15. Work with the Office of Finance to gain access to the financial remittance information pertaining to OPGs, to be used in fiscal monitoring. 16. During the next contract negotiation, include a contract requirement for OPGs to submit financial statements on a fiscal year basis that clearly show all sources of gross revenue, classified between City and non-City tows. The LAPD should: 17. Reinforce the requirements in the LAPD Manual regarding auto impound procedures to ensure an efficient and effective impound process, and minimize City reimbursements of OPG charges.	21 21 21 21 22

INTRODUCTION AND BACKGROUND

An LAPD auto impound contractor operates as an Official Police Garage (OPG) for a specific LAPD geographic area. The Los Angeles Municipal Code (LAMC) defines an OPG as a towing and garage business selected by the City to remove and store vehicles at the direction of any Police Officer or Traffic Officer employed by the City including officers of the Port, Airport and Housing Authority. Situations that may require OPG services include towing and storage of illegally parked vehicles; abandoned vehicles; vehicles disabled as the result of traffic accidents; vehicles seized for evidentiary examination; abated vehicles; and vehicles subject to forfeiture proceedings.

Prior to 1996, the Board of Police Commissioners (Board) designated privately owned businesses as OPGs in each of the 18 geographical areas, which in the Board's judgment were the best qualified to perform these services. This arrangement did not generate revenue for the City in the form of franchise fees; however, OPGs paid permit fees to operate a towing operation. Before an OPG is issued a permit, an OPG must meet certain requirements such as having a physical location with an office and an adjacent yard for vehicle storage, and obtaining appropriate insurance coverage.

As early as 1983, the City Administrative Officer (CAO) recommended that the City let a competitive selection process for the OPG contracts.

History of OPG Contracts

On May 22, 1996, the City Council passed Ordinance No. 171104 adding Section 80.77.4 to the Los Angeles Municipal Code (LAMC) to establish contracting procedures for OPGs. The Board was authorized, subject to the City Council approval, to award OPG contracts for a fixed five-year term for each geographical police area using the City's standardized bid and contract procedures. The ordinance also required the Board to enter into interim written contracts with those individuals or corporations that were doing business as Official Police Garages as of February 28, 1996. These interim contracts were set to expire upon the award of the final contracts.

In December 1996, the City Council approved a Request for Proposal (RFP) for the first four geographic areas, but only awarded one OPG contract. In April 2000, another RFP was released for an additional 18 areas. Proposals were received and submitted to the Bureau of Contract Compliance of the Department of Public Works to ensure that the proposals complied with City requirements. Proposals were then evaluated by a contract selection committee representing several City departments (Department of Transportation, Board of Police Commissioners and the Office of the City Administrative Officer). Subsequently, the involved City departments began work on a more comprehensive OPG contract that would serve as a template for all City OPG contracts. The prototype OPG contract was finally approved by the City Council in February 2004.

Although there were significant delays in the award of the OPG contracts due to delays in the Request for Proposal (RFP) development and release, prototype contract approval and execution, we noted that City policy was followed in the solicitation, selection, and award of current OPG contracts.

As of June 30, 2007, the City had 20 OPG contracts in effect that service the 18 LAPD geographical areas. Eighteen provide standard towing services and two provide heavy-duty towing services. The contracts require OPGs to provide service to the City 24-hours a day, 7 days a week, within a maximum response time of 20 minutes from the time an OPG dispatcher receives a request. Most of these contracts will expire in 2009.

City Oversight of OPG Contracts

Section 80.77.4 of the Los Angeles Municipal Code authorizes the Board of Police Commissioners (Board), subject to City Council approval, to enter into contracts with the OPGs for a fixed term of five years, with a renewal option for an additional five-year period. The Police Commission is responsible for coordinating and monitoring the contractual relationship between the City and the OPGs.

The Commission Investigation Division (CID) of the Police Commission is responsible for regulating the OPGs' towing operations. The CID monitors the quality of service provided, investigates and handles complaints, and conducts company and employee background investigations.

The Board establishes the fees and rates charged for the removal and storage of vehicles. For example, the 2007 approved OPG rates for a standard vehicle include the following:

2007 Approved OPG Charges for Standard Vehicles

\$ 101.50	Tow Rate
\$ 31.50	Storage Rate per Day
\$ 3.15	Parking Tax per Day (applied as 10% of Storage Rate)
\$ 48.00	City Admin Fee (VRF)

Note: Information presented as example only; other rates also in effect for heavy duty or other vehicles as well as miscellaneous charges.

The City does not compensate OPGs for services rendered at the direction of an authorized City employee. Generally, the owner of an impounded vehicle is responsible for such charges.² The law provides that charges for towing and storage become a lien against the impounded vehicle, and must be paid by an owner prior to the vehicle's release. Unredeemed vehicles are sold at auction.

² However, an authorized City employee may direct a vehicle owner not be assessed if there was no probable cause to impound a vehicle. In these cases, the City becomes liable for charges incurred on a City-directed impound.

The OPG collects all applicable charges from the person who redeems an impounded vehicle. The OPG must, in turn, remit to the City the collected VRF and the Parking Occupancy Tax (POT). In addition, the OPG must remit to the City a franchise fee equal to seven percent of all revenues generated from its activities as an OPG. All fees are remitted directly to the City's Office of Finance.

In calendar year 2006, OPGs impounded approximately 175,000 vehicles: 113,000 at the direction of the Los Angeles Police Department, and an estimated 62,000 from the Los Angeles Department of Transportation. During 2006, the City received approximately \$14 million from OPGs, including revenues from the vehicle release fees, franchise fees, City parking occupancy taxes, and vehicle forfeiture fees.

Notable Accomplishments

According to CID, the current official police garage system is one of the most highly regulated and scrutinized models of its kind. Considered superior to the process commonly used by other cities, other municipalities routinely request information on the Police Commission's management of official police garages in Los Angeles and attempt to replicate them. Finally, the Police Commission established rules and regulations under which the service would be rendered, to ensure that a standard of quality for towing services was well established and maintained.

OBJECTIVES, SCOPE AND METHODOLOGY

The overall objective of this audit was to ensure that the Police Commission properly awarded the auto impound contracts in a fair and consistent manner, and that processes are in place to ensure OPG contractors comply with contract requirements. Specific objectives of the audit were to determine whether the Commission Investigation Division of the Police Commission:

1. Conducted the selection and award of auto impound contracts in accordance with City policies and procedures, including timeliness of award or renewal.
2. Ensures that the auto impound contractors provide the services in accordance with the contract provisions.
3. Ensures that the auto impound contractors remit the correct amount of fees to the City.
4. Properly monitors the selected auto impound contracts to ensure compliance with contract provisions.

This audit was conducted in accordance with Generally Accepted Government Auditing Standards and covered the period from July 1, 2006 to June 30, 2007. We also reviewed selected bank records from January 1, 2006, and proposal information that dates from the respective contracts' inception. We conducted our fieldwork between January and March 2008.

In performing our review, we reviewed OPG contract provisions and pertinent laws, regulations, policies and procedures. We interviewed responsible LAPD and OPG personnel; observed OPG sites, performed spot inventories of impounded vehicles, observed auction sales, and reviewed and analyzed OPG records pertaining to OPG activities.

Our review of the LAPD auto impound contracts required that we examine OPG documentation and interview OPG personnel; however, our auditee was the Commission Investigation Division of the Los Angeles Police Commission (CID). Therefore, findings and recommendations are addressed to CID.

AUDIT FINDINGS AND RECOMMENDATIONS

SECTION I: IMPACT ON CITY REVENUE

The City's contract requires OPGs to pay several kinds of fees to the City, as mandated by the Los Angeles Municipal Code (LAMC). In addition to the City business taxes and Parking Occupancy Taxes, OPGs are also required to collect and remit a City Vehicle Release Fee for every redeemed vehicle, and to pay a gross receipts (franchise) fee.

LAMC Section 80.77.4.D requires that "each OPG shall pay to the general fund of the City a fee equal to seven percent (7%) of all revenue generated as a result of its activities as an Official Police Garage, *including but not limited to* revenues generated from the towing and storage of vehicles and the sales of lien vehicles."

It further states that "the fees...shall be paid quarterly. Each operator of an Official Police Garage shall, on or before the last day of the calendar month following the close of each calendar quarter, make a statement to the Office of Finance, on forms provided by the Office of Finance, of the total amount of fees imposed by this section. At the time the statement is filed, the full amount of said fees shall be remitted to the Office of Finance."

For this report, we consider this fee as a "franchise fee."

The OPGs remit their fees directly to the Office of Finance (OOF) using simplified OOF forms on a quarterly basis. OPGs are not required to submit financial statements or audits of their financial operations to the City.

Finding # 1: 15 OPG contractors did not include lien processing fees in their gross revenues, resulting in underpayment of about \$1 million in franchise fees due to the City.

When an OPG has towed and stored a vehicle and has not been paid for these services, the charges become a lien against the vehicle. The lien holder (OPG) can satisfy the lien by getting a court judgment or by selling the vehicle through a lien sale, typically through an auction.

After a vehicle has been in storage for 72 hours (3 days), an OPG can start the lien sale process. Initial requirements for a lien sale includes conducting a DMV vehicle title search, mailing notifications to registered and legal owners, and preparing the lien sale package containing required forms.

Section 3074 of the California Civil Code, as well as the CA Vehicle Code Section 22851.12, allows the lien holder (OPG) to charge a fee for lien sale preparations not to exceed seventy dollars (\$70) for a vehicle with a value determined to be \$4,000 or less, or not to exceed \$100 for a vehicle with a value determined to be greater than \$4,000. Therefore, if an owner redeems a vehicle after this process has begun, he/she will be charged an additional \$70 or \$100 fee. The OPG will also recover this charge from a buyer at an auction sale.

Based on our review of two sample OPGs, we found that while one OPG did include these fees in the total revenue subject to the franchise fee, another did not. For this one contractor, during FY 2007, unreported lien processing fees amounted to approximately \$281,000, and resulted in an underpayment of approximately \$20,000 in City franchise fees.

Further review noted that 15 (including the sample) of the 20 OPG contractors did not include the lien processing fees in their gross receipts as reported to the Office of Finance. Presented below are the FY 2007 lien processing fees collected from the 15 OPG contractors that did not include these amounts in their gross receipts subject to the 7% franchise fee.

OPG Contract No.	Unreported Lien Fees	Impact on Franchise Fee
1	\$277,705	\$19,439
2		
3	\$54,271	\$3,799
4	\$184,155	\$12,890
5	\$103,444	\$7,241
6	\$281,427	\$19,700
7		
8	\$322,367	\$22,566
9	\$182,165	\$12,751
10	\$258,702	\$18,109
11	\$170,129	\$11,909
12	\$362,996	\$25,410
13	\$222,728	\$15,591
14	\$160,245	\$11,217
15	\$378,815	\$26,517
TOTALS	\$2,959,149	\$207,139

The unreported lien fees include an insignificant amount of receipts related to non-City tows. The majority of OPG revenues are generated from City-directed tows. For example, our analysis of a sample OPG's revenues for FY 2007 showed that approximately 5% of total revenue came from non-City tows.

When projected over the entire five-year contract period, the impact of not including lien processing fees in OPG gross revenue results in underpaid franchise fees totaling more than one million dollars ($\$207,000 \times 5 = \$1,035,000$.)

The OPGs did not include the lien processing fees in their gross revenue subject to the franchise fee because they considered it a reimbursement of their costs for conducting a proper lien sale. We noted that for FY 2007, a sample OPG's direct costs related to the lien processing function were approximately 52% of the total lien fees they collected. While company representatives stated that the full cost also includes labor and overhead associated with this function, we consider all such costs part of the OPG's general business operations.

We disagree with the OPGs' assessment that the lien fee should not be considered revenue. The State Codes allowing OPGs to charge customers a lien processing fee provide an additional revenue source that is related to a key OPG function, lien sales, and should be considered similar to towing or storage charges. While the State and local regulations permitting the charge recognize that OPGs must incur operational costs to process a lien sale, these are not "pass-through" costs that are paid directly to a third party. Rather, all charges paid by a customer result in additional receipts by the OPG, and therefore contribute to gross revenue. Generally Accepted Accounting Principles (GAAP) require businesses to record the recovery of reimbursable expenses as revenue.

In addition, GAAP requires that revenue from service transactions should be recognized when the service has been performed. In this case, when the "sale" is made, (i.e., when vehicles are redeemed or sold) the OPGs' earnings process is complete; the revenue is realized and should be recorded as such.

As stated in section 80.77.4.D of the LA Municipal Code, "Each Official Police Garage shall pay to the general fund of the City a fee equal to 7% of all revenues generated as a result of its activities as an Official Police Garage..."

It should be noted that OPGs include the collections of lien processing fees when reporting their gross receipts for City business tax purposes. In addition, an Office of Finance representative stated that they have no documented ruling that lien processing fees should not be included in the OPG gross receipts subject to the 7 % franchise fee.

Recommendations:

The CID of the Police Commission should:

- 1. Pursue recovery of underpayments from OPGs for unreported lien processing fees from contract inception to date.**
- 2. Communicate to OPGs to ensure proper reporting of "gross revenue" that is subject to the 7% franchise fee.**

Finding # 2: City Vehicle Release Fees are not remitted for vehicles sold at auction.

Under Section 22850.5 of the California Vehicle Code (Vehicle Code), a government agency such as the City is allowed to impose a charge equal to its administrative costs relating to the removal, impound, storage and release of the vehicles. However, the Vehicle Code also states: "The charges shall only be imposed on the registered owner...and shall not include any vehicle...sold at a lien sale...unless the sale is sufficient in amount to pay the lien holder's total charges and proper administrative costs."

Los Angeles Municipal Code (LAMC) Section 80.77.1 requires that each OPG collect \$48 from every person who redeems a vehicle that was impounded at the direction of the City. This "Vehicle Release Fee" (VRF) represents a reimbursement to the City for costs of impounding.

When auction proceeds exceed the lien holder (OPG) charges, OPGs apply the excess first to any unpaid traffic citations, and remit the remaining amount to the CA Department of Motor Vehicles, in accordance with Section 3073 of the CA Civil Code. The OPGs did not remit the \$48 VRF from the excess amounts for remittance to the City. In addition, the Office of Finance quarterly reporting form for the VRF excludes vehicles sold through lien sales in the vehicles subject to the VRF.

The City has not considered the exception in the exclusion section of the Vehicle Code on the recovery of the administrative costs of a government agency. There is an opportunity for the City to recover additional revenue through VRF for some vehicles sold at auction. For 2006, OPGs reported that approximately 63,000 vehicles were sold through lien sales, but stated that OPGs recovered their total costs on only 1,527 vehicles. However, even using this conservative figure, the City could recover an additional \$73,000 in VRF fees annually.

According to CID, the requirement to remit the VRF to the City for auctioned vehicles when lien sale proceeds exceed total charges including administrative costs will require an amendment to the Ordinance.

Recommendations:

The CID of the Police Commission should:

- 3. Work with the City Attorney to amend the pertinent Ordinance provision and include in the OPG contract the provision of the CA Vehicle Code Section 22850.5(b)(1) that states that the City's administrative cost (Vehicle Release Fee) will be recovered from lien sales when there is an excess amount to cover the OPGs' total charges and administrative costs.**

4. **Work with the Office of Finance to revise the quarterly report form pertaining to the Vehicle Release Fee to include vehicles sold at auction where sale proceeds exceed OPG total charges and proper administrative costs.**

Finding # 3: An OPG underpaid franchise fees by deducting bank charges from gross revenue.

Based on our review of a sample OPG's financial records, we found that the OPG deducted credit card fees and other bank charges from its gross receipts subject to the franchise fee as reported to the Office of Finance.

The OPG underpaid the City approximately \$2,400 for fiscal year 2007 by deducting bank charges that include credit card fees, from their gross receipts that are subject to the 7% franchise fee. Over the entire five-year contract term, this OPG may have underpaid the City approximately \$12,000 ($\$2,400 \times 5$) due to this deduction.

Credit card fees and other bank charges are operating expenses and should not be deducted from gross receipts. Gross receipts should be based on total payments as remitted by customers.

Recommendations:

The CID of the Police Commission should:

5. **Request all OPGs to report all credit card fees and other bank charges that were deducted from gross receipts since contract inception and remit the corresponding 7% franchise fees to the Office of Finance.**

SECTION II: OPG SYSTEMS CAPABILITY

OPGs generally maintain two separate information systems – a dispatch system and a financial system.

The dispatch system creates and maintains a record for each impounded vehicle from the time it is received in an OPG facility until it is redeemed or sold at auction. The record includes information such as description of the impounded vehicle (license plate number and/or Vehicle Identification Number), name of vehicle owner, date and the time of impound, date and time of release, and accumulated charges based on towing, storage, etc.

When a vehicle is redeemed, an invoice is generated from the dispatch system. The invoice shows all accumulated charges from the time the vehicle was received until its release. A person redeeming an impounded vehicle can pay in cash, check or credit card. Unclaimed or unredeemed vehicles may be sold at auction.

Payments received upon a vehicle's release as captured through the dispatch system are summarized and recorded, usually daily, in the accounting system. One of the sample OPGs used a computerized accounting system while the other used a manual system.

Finding # 4: Inadequate OPG dispatch and accounting systems and controls provided inaccurate data, resulting in underpayments to the City.

A good dispatch system accurately tracks all vehicles received at an OPG facility and the related charges. A good financial system has the ability to capture all receipts, which can then be tied to charges reflected in the dispatch system, and related disbursements. Information from these systems should be adequately supported and easily reconciled.

Our review of the computerized dispatch and manual accounting systems of a sample OPG showed that the systems were inadequate to properly account for all transactions. In addition, we became aware of financial control problems at two other OPGs resulting in underreported fees paid to the City.

Based on our testwork at one sample OPG, we found that the bookkeeper had to make numerous manual corrections on the computer generated reports from the dispatch system prior to recording the financial information in the accounting system. Based on our review of sample daily Payments Received Reports for the months of June 2007 and February 2007, these manual adjustments included additional receipts, missing receipts, missing receipts that were deposited and recorded at a later date, and errors in amounts received or mode of payment. The bookkeeper explained that dispatchers who received the payments sometimes made mistakes in recording the amounts of payment received and in recording the mode of payment. She also explained that there

were times when dispatchers prepared manual invoices when the system was down, and she manually added the receipts for those invoices on the computer-generated Payments Received Report.

We noted the bookkeeper also had to make several manual adjustments on the General Ledger Distribution Summary Report to classify total receipts into payments by credit card and by cash or check; charges for non-City tows; and other recurring transactions.

Because of the numerous manual adjustments of unexplained and unsupported transactions, financial information was inconsistently recorded and there remains a high probability that errors cannot be detected.

Below are the deficiencies we noted in the review of the sample OPG's dispatch and accounting systems:

a) Unreported Vehicle Release Fee

We reviewed a sample month to determine if the total amount of the City Administration Fee (VRF) shown in the dispatch system's computer generated reports matched the financial record. We found that the OPG did not record the VRF for five vehicles amounting to \$240 (\$48 x 5) for the sample month. The OPG bookkeeper validated that they overlooked to record the receipts in the accounting system.

b) Inaccurate data on the quarterly Vehicle Release Fee Reporting Forms

A sample OPG reported inaccurate data on their quarterly returns for VRF. In all quarters of FY 2007, the beginning inventory of each quarter did not match the ending inventory of the previous quarter. We recalculated the number of impounded vehicles subject to VRF using the ending inventory of the previous quarter as the beginning inventory of the current quarter. We noted that the OPG underreported the number of vehicles subject to VRF in three quarters and over reported in one quarter. The net dollar effect of the discrepancies for the four quarters of FY 2007 was approximately \$25,000.

We found that the sample OPG did report the amounts of VRF collected as shown in their financial record. However, because the dispatch and financial systems are not linked, and we found instances of unrecorded VRFs, we could not fully rely on the accuracy of the financial record. In reporting the number of impounded vehicles subject to VRF in the OOF VRF form, the OPG simply divided the amount reported as collected by \$48, and force-balanced the vehicle numbers by adjusting the beginning inventories.

The information presented in the quarterly report for VRF submitted to OOF serves as a second -level check on the amount of VRF collected by the OPGs as reflected in their financial records. The discrepancies noted between the amounts of VRF remitted as reflected in the financial records, and the calculated amount based on the erroneous

number of vehicles subject to the VRF as reported in the quarterly returns, may impact the accuracy of the VRF fees remitted to the City if deficiencies are not corrected.

Other Reported Problems by OPGs

Weaknesses in dispatch and financial systems lead to a weak control environment that can make an organization susceptible to error or intentional misstatement, including fraud.

- a) An OPG brought to CID's and auditors' attention that they did not include proceeds from lien sales for payments due on invoices billed after the auction in their reported gross receipts subject to the 7% franchise fee. These payments were primarily from wrecking or dismantling yards that purchased unsold cars in bulk, and from customers who bought vehicles valued over \$4,000 and claimed the vehicles 10 days later, as required by law (long lien sales). The OPG estimates it underpaid City franchise fees by approximately \$28,000 in FY 2007.
- b) Another OPG's dispatch system allowed for invoice adjustments after a customer payment had been made, and due to insufficient controls over cash receipts, a key employee was able to embezzle approximately \$170,000 over an eighteen-month period. Corresponding underreported and underpaid City fees and parking taxes totaled approximately \$25,000.

Recommendations:

The CID of the Police Commission should:

- 6. Require OPGs to properly prepare their quarterly returns for the Vehicle Release Fee.**
- 7. Request all OPGs to report any lien sale proceeds, including sales to wrecking or dismantling yard, that were not included in their reported gross receipts since contract inception and remit applicable franchise fees to the Office of Finance.**
- 8. Timely inform all OPGs of the recent issues/problems pertaining to financial reporting that were brought to its attention by other OPGs.**
- 9. Request all OPGs to self-assess their own dispatch and financial systems and report if they have similar or other related problems.**
- 10. Work with OPGs that have problems/issues in their systems and reporting to ensure that those are properly addressed.**
- 11. Ensure that all OPGs have reliable and adequate computerized dispatch and accounting systems in place that have a capability to track and record all transactions and charges affecting an impounded vehicle.**

12. Ensure that all OPGs properly support their quarterly reported fees to the City with a reconciliation of data in the dispatch system with records in the financial system.

SECTION III: FINANCIAL OVERSIGHT

We found that neither the Commission Investigation Division (CID) of the Police Commission nor the Office of Finance (OOF) provides the necessary fiscal oversight for OPG operations. In addition, the LAPD can minimize reimbursements to OPGs by more diligently complying with its own Auto Impound Procedures.

Finding # 5: Lack of fiscal monitoring of OPGs led to inconsistencies in reporting and underpayment of City fees.

The Los Angeles Police Commission is charged with the overall oversight of the OPGs. The CID of the Commission manages the contractual relationship between the City and the OPGs, coordinates and oversees the contract selection process, monitors the quality of services provided by the OPGs, investigates and handles complaints against the OPGs from the public and the City, and conducts OPG employees' background investigations.

The OPG contracts require they remit various fees to the City such as the Vehicle Release Fee (VRF) and Gross Receipts Fee (7% franchise fee), in accordance with City ordinances. The contract also stipulates certain penalties if an OPG fails to comply with these requirements.

However, OPGs are mandated by the Los Angeles Municipal Code (LAMC) sections 80.77.1(d) and 80.77.4.D to remit the VRF and the 7% franchise fee directly to the Office of Finance (OOF). Even though CID is the contract administrator, CID has no knowledge if OPGs are fully complying with the fee requirements of the contract. CID representatives stated that they could not ensure adequate fiscal compliance because they did not have the information that was filed with OOF. Prior to May 2008, OOF had been reluctant to provide OPG financial information to CID. In addition, CID stated they would need to hire staff with expertise in financial analysis to verify OPGs' compliance.

Office of Finance representatives stated that their role as a revenue authority limits their function relative to OPGs as a collection agent for their self-reported fees. Finance also stated that their function is not regulatory, and therefore cannot be considered as enforcement of applicable financial provisions of an entity's contract. While OOF auditors do conduct field audits of businesses to ensure compliance with City tax requirements, their focus is on the business's payment of taxes, and not on contract compliance.

The Office of Finance acknowledged that the CID needs OPG remittance information to properly monitor OPGs' fiscal compliance with their contracts. Finance is agreeable to working with the CID to allow some access to the OOF information system pertaining to OPGs' remittances of VRF and franchise fees.

City fees that are unique to OPG, such as the VRF and the 7% franchise fee, are directly attributed to the City's contract. As contract administrator, the Police Commission should ensure OPGs comply with the fiscal requirements of their agreement. Emphasis on additional accountability such as requiring audited financial statements and increased fiscal monitoring should also be considered.

Because there was no dedicated City agency fiscally monitoring the OPGs, inconsistencies in financial reporting and underpayment of fees occurred.

Recommendations:

The CID of the Police Commission should:

- 13. Ensure that OPGs comply with the contract requirements pertaining to payment of fees to the City through periodic reviews of their fiscal operations.**
- 14. Consider coordinating with LAPD's Fiscal Operations Division and/or outside consultant(s) to conduct adequate fiscal monitoring of OPGs.**
- 15. Work with the Office of Finance to gain access to the financial remittance information pertaining to OPGs, to be used in fiscal monitoring.**
- 16. During the next contract negotiation, include a contract requirement for OPGs to submit financial statements on a fiscal year basis that clearly show all sources of gross revenue, classified between City and non-City towns.**

Finding # 6: Non-adherence to LAPD impound procedures resulted in avoidable City payments to OPGs.

Generally, LAPD officers in various geographic areas of the City initiate the impound process. Also, there are two key LAPD employees that monitor impounded vehicles within each geographic area, an Area Vehicle Control Coordinator, a sworn employee, and a Vehicle Control Clerk, a civilian employee. The LAPD Manual provides the duties and responsibilities of the impounding officer and each of these employees.

For each impound, LAPD impounding officers must perform certain procedures as stated in the Manual. For example, officers must complete necessary reports, notify registered and legal owners of impounded vehicles within the required timeframe, place a hold on vehicles that were impounded in violation of certain provisions of the California Vehicle Code, and notify the Scientific Investigation Division when fingerprints are needed for vehicles used in a crime.

A Vehicle Control Clerk's duties include maintaining a log for all impounded vehicles, notifying the registered and legal owners in writing when they have not been notified by the impounding officer, notifying appropriate supervisors when a vehicle has been held for two business days, and other duties.

On a weekly basis, an Area Vehicle Coordinator is to review vehicle impound reports and vehicles that have been stored in excess of five days. The Coordinator verifies if proper notifications have been made to all interested persons (person reporting, present owner, registered and legal owners), verifies the status of any holds placed on the vehicle, and ensures all notifications and verifications are documented on the vehicle impound report.

When properly adhered to, the duties required of each responsible LAPD personnel provide an added control over the impound process, and help ensure an efficient operation. Errors or oversights would be caught early in the impound process.

Normally, the owner of an impounded vehicle is responsible for paying the OPG towing and storage charges. However, if an authorized City employee directs that the fee not be assessed against the owner (such as when it is determined that probable cause to impound did not exist), the City will pay such fees to which the OPG was legally entitled.

LAPD may directly reimburse an OPG for certain fees which have accrued when a vehicle remains stored for an unreasonable amount of time, at no fault of the registered or current owner. For example, if the registered owner of a towed vehicle did not receive timely notification regarding the status or location of the vehicle due to LAPD administrative error, or an impounded vehicle was held for investigation longer than two business days.

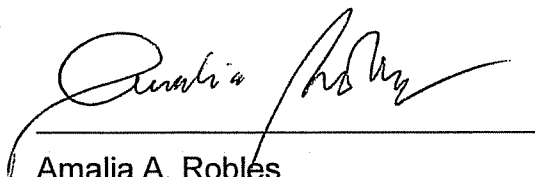
During fiscal year 2007, the LAPD paid approximately \$289,000 to various OPGs as reimbursements for towing and storage of impounded vehicles at LAPD's direction. Payments ranged from \$4,000 to \$72,000 for each OPG.

Based on our review of seven invoices paid by the LAPD to a sample OPG, we noted that LAPD could have avoided or reduced payments for five invoices by approximately \$4,000, which was 67% of the total reimbursed amount. Justifications for the request for reimbursements showed that these were caused by an LAPD officer erroneously putting a 30-day hold on a vehicle, failure to properly review documents presented by the vehicle owner, improper notification to the vehicle owner, and inadequate or untimely action of the responsible LAPD officer.

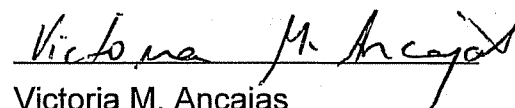
Recommendation:

- 17. The LAPD should reinforce the requirements in the LAPD Manual regarding auto impound procedures to ensure an efficient and effective impound process, and minimize City reimbursements of OPG charges.**

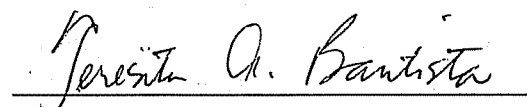
Respectfully submitted,



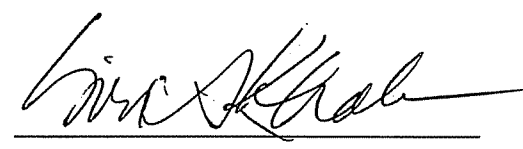
Amalia A. Robles
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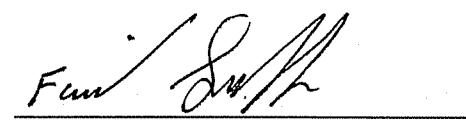


Teresita A. Bautista
Internal Auditor III



Siri Atma Khalsa, CPA
Deputy Director of Auditing

March 28, 2008



Farid Saffar, CPA
Director of Auditing

Ranking of Recommendations

Finding No.	Description of Finding	Ranking Code	Recommendations
Section I – Impact on City Revenue			
1.	<i>15 OPG contractors did not include lien processing fees in their gross revenues, resulting in underpayment of about \$1 million in franchise fees due to the City.</i>	U	1. Pursue recovery of underpayments from OPGs for unreported lien processing fees from contract inception to date.
		U	2. Communicate to OPGs to ensure proper reporting of “gross revenue” that is subject to the 7% franchise fee.
2.	<i>City Vehicle Release Fees are not remitted for vehicles sold at auction.</i>	U	3. Work with the City Attorney to amend the pertinent Ordinance provision and include in the OPG contract the provision of the CA Vehicle Code Section 22850.5(b)(1) that states that the City's administrative cost (Vehicle Release Fee) will be recovered from lien sales when there is an excess amount to cover the OPGs' total charges and administrative costs.
		U	4. Work with the Office of Finance to revise the quarterly report form pertaining to the Vehicle Release Fee to include vehicles sold at auction where sale proceeds exceed OPG total charges and proper administrative costs.

3.	<i>An OPG underpaid franchise fees by deducting bank charges from gross revenue.</i>	U	5. Request all OPGs to report all credit card fees and other bank charges that were deducted from gross receipts since contract inception and remit the corresponding 7% franchise fees to the Office of Finance.
Section II – OPG SYSTEMS CAPABILITY			
4.	<i>Inadequate OPG dispatch and accounting systems and controls provided inaccurate data, resulting in underpayments to the City.</i>	N	6. Require OPGs to properly prepare their quarterly returns for the Vehicle Release Fee.
		U	7. Request all OPGs to report any lien sale proceeds, including sales to wrecking or dismantling yard, that were not included in their reported gross receipts since contract inception and remit applicable franchise fees to the Office of Finance.
		N	8. Timely inform all OPGs of the recent issues/problems pertaining to financial reporting that were brought to its attention by other OPGs.
		N	9. Request all OPGs to self-assess their own dispatch and financial systems and report if they have similar or other related problems.
		N	10. Work with OPGs that have problems/issues in their systems and reporting to ensure that those are properly addressed.
		N	11. Ensure that all OPGs have reliable and adequate computerized dispatch and

			accounting systems in place that have a capability to track and record all transactions and charges affecting an impounded vehicle.
		N	12. Ensure that all OPGs properly support their quarterly reported fees to the City with a reconciliation of data in the dispatch system with records in the financial system.
Section III – FINANCIAL OVERSIGHT			
5.	<i>Lack of fiscal monitoring of OPGs led to inconsistencies in reporting and underpayment of City fees.</i>	N	13. Ensure that OPGs comply with the contract requirements pertaining to payment of fees to the City through periodic reviews of their fiscal operations.
		N	14. Consider coordinating with LAPD's Fiscal Operations Division and/or outside consultant(s) to conduct adequate fiscal monitoring of OPGs.
		U	15. Work with the Office of Finance to gain access to the financial remittance information pertaining to OPGs, to be used in fiscal monitoring.
		N	16. During the next contract negotiation, include a contract requirement for OPGs to submit financial statements on a fiscal year basis that clearly show all sources of gross revenue, classified between City and non-City tows.

6.	<i>Non-adherence to LAPD impound procedures resulted in avoidable City payments to OPGs.</i>	N	17. The LAPD should reinforce the requirements in the LAPD Manual regarding auto impound procedures to ensure an efficient and effective impound process, and minimize City reimbursements of OPG charges.
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DESCRIPTION OF RECOMMENDATION RANKING CODES

U - Urgent - The recommendation pertains to a serious or materially significant audit finding or control weakness. Due to the seriousness or significance of the matter, immediate management attention and appropriate corrective action is warranted.

N – Necessary - The recommendation pertains to a moderately significant or potentially serious audit finding or control weakness. Reasonably prompt corrective action should be taken by management to address the matter. The recommendation should be implemented within six months.