

# **CITY OF LOMITA**

Audit Report

## **SPECIAL GAS TAX STREET IMPROVEMENT FUND**

*July 1, 2015, through June 30, 2016*



**BETTY T. YEE**  
California State Controller

June 2017



**BETTY T. YEE**  
California State Controller

June 12, 2017

The Honorable Mark Waronek  
Mayor of the City of Lomita  
24300 Narbonne Avenue  
Lomita, CA 90717

Dear Mayor Waronek:

The State Controller's Office audited the City of Lomita's Special Gas Tax Street Improvement Fund for the period of July 1, 2015, through June 30, 2016.

Our audit found that the city accounted for and expended its Special Gas Tax Street Improvement Fund in compliance with requirements, except that it understated the fund balance by \$25,285 as of June 30, 2016. The city understated the fund balance because it charged ineligible expenditures to the fund. In addition, we identified procedural findings.

If you have any questions, please contact Efren Lose, Interim Chief, Local Government Audits Bureau, by telephone at (916) 324-7226.

Sincerely,

*Original signed by*

JEFFREY V. BROWNFIELD, CPA  
Chief, Division of Audits

JVB/rg

cc: Ryan Smoot, City Manager  
City of Lomita  
Susan Kamada, Administrative Services Director  
City of Lomita

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# Audit Report

## Summary

The State Controller's Office (SCO) audited the City of Lomita's Special Gas Tax Street Improvement Fund for the period of July 1, 2015, through June 30, 2016.

Our audit found that the city accounted for and expended its Special Gas Tax Street Improvement Fund in compliance with requirements, except that the city understated the fund balance by \$25,285 as of June 30, 2016. The city understated the fund balance because it charged ineligible expenditures to the fund. In addition, we identified procedural findings.

## Background

The State apportions funds monthly from the Highway Users Tax Account (HUTA) in the Transportation Tax Fund to cities and counties for the construction, maintenance, and operation of local streets and roads. The highway users taxes derive from State taxes on the sale of motor vehicle fuels. In accordance with Article XIX of the California Constitution and Streets and Highways Code, a city must deposit all apportionments of highway users taxes in its Special Gas Tax Street Improvement Fund. A city must expend gas tax funds only for street-related purposes. We conducted our audit of the city's Special Gas Tax Street Improvement Fund under the authority of Government Code section 12410.

## Objectives, Scope, and Methodology

Our audit objectives were to determine whether the city accounted for and expended its Special Gas Tax Street Improvement Fund in compliance with Article XIX of the California Constitution and the Streets and Highways Code.

We audited the city's Special Gas Tax Street Improvement Fund for the period of July 1, 2015, through June 30, 2016.

To meet the objectives, we:

- Gained a limited understanding of internal controls that would have an effect on the reliability of the accounting records of the Special Gas Tax Street Improvement Fund by interviewing key personnel, completing the internal control questionnaire, reviewing the city's organization chart, and assessing the reliability of computer-processed data;
- Conducted a risk assessment to determine the nature, timing, and extent of substantive testing;
- Performed analytical procedures to determine and explain the existence of unusual or unexpected account balances;
- Verified the accuracy of the fund balances by performing a fund balance reconciliation for the period of July 1, 2013, through June 30, 2015, and by recalculating the trial balance for the period of July 1, 2015, through June 30, 2016;

- Verified whether the components of and changes to the fund balances were properly computed, described, classified, and disclosed by scheduling and analyzing the Special Gas Tax Street Improvement Fund account balances;
- Reconciled the fund revenue recorded in the city ledger to the balance reported in the SCO's apportionment schedule for fiscal year (FY) 2015-16 to determine whether HUTA apportionments received by the city were completely accounted for;
- Reviewed city accruals and adjustments for validity and eligibility;
- Analyzed the system used to allocate interest and determined whether the interest revenue allocated to the Special Gas Tax Street Improvement Fund was fair and equitable, by interviewing key personnel and recalculating a sample of interest allocations;
- Reviewed the fund cash and liabilities accounts for unauthorized borrowing to determine whether unexpended HUTA funds were available for future street-related expenditures and protected from impairment; and
- Verified whether the expenditures incurred during the audit period were supported by proper documentation and eligible in accordance with the applicable criteria by testing 100% of the expenditure transactions that were equal to or greater than the significant item amount (calculated based on materiality threshold), and selecting samples of other transactions for the following categories based on our judgment (for the selected sample, errors found will not be projected to the intended population):
  - Services and Supplies – We tested, reviewed, and recalculated \$83,539 of \$287,845 in total services and supplies expenditures.
  - Labor – We tested, reviewed, and recalculated \$13,337 of \$308,855 in total labor costs.

We did not audit the city's financial statements. We limited our audit scope to planning and performing audit procedures necessary to obtain reasonable assurance that the city accounted for and expended its Special Gas Tax Street Improvement Fund in accordance with the criteria. We considered the city's internal controls only to the extent necessary to plan the audit.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

**Conclusion**

Our audit found that the City of Lomita accounted for and expended its Special Gas Tax Street Improvement Fund in compliance with Article XIX of the California Constitution and the Streets and Highways Code for the period of July 1, 2015, through June 30, 2016, except as noted in Schedule 1 and described in the Findings and Recommendations section of this report. The findings require an adjustment of \$25,285 to the city's accounting records. In addition, we identified procedural findings.

**Follow-Up on Prior Audit Findings**

Our prior audit report, issued on February 3, 2014, disclosed no findings.

**Views of Responsible Officials**

We issued a draft audit report on May 8, 2017. Ryan Smoot, City Manager, responded by letter dated May 12, 2017, agreeing with the audit results. The city's response is included in this final audit report as an attachment.

**Restricted Use**

This report is solely for the information and use of the City of Lomita 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, CPA  
Chief, Division of Audits

June 12, 2017

**Schedule 1—  
Reconciliation of Fund Balance  
July 1, 2015, through June 30, 2016**

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	Special Gas Tax Street Improvement Fund <sup>1</sup>
Beginning fund balance per city	\$ 232,816
Revenues	<u>459,195</u>
Total funds available	692,011
Expenditures	<u>(596,700)</u>
Ending fund balance per city	<u>95,311</u>
SCO adjustments: <sup>2</sup>	
Finding 1—Ineligible expenditures	<u>25,285</u>
Ending fund balance per audit	<u>\$ 120,596</u>

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<sup>1</sup>The city receives apportionments from the State HUTA, pursuant to Streets and Highways Code sections 2103, 2105, 2106, 2107, and 2107.5. The basis of the apportionments varies, but the money may be used for any street-related purpose. Streets and Highways Code section 2107.5 restricts apportionments to administration and engineering expenditures, except for cities with populations of fewer than 10,000 inhabitants. Those cities may use the funds for rights-of-way and for the construction of street systems. The city must deposit its HUTA apportionments in its Special Gas Tax Street Improvement Fund.

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

# Findings and Recommendations

**FINDING 1—  
Ineligible non-street-  
related consulting and  
membership fees  
expenditures**

During FY 2015-16, the city charged the Special Gas Tax Street Improvement Fund \$17,349 for consulting fees relating to National Pollutant Discharge Elimination System (NPDES) water discharge permit program and \$7,936 for South Bay Cities Council of Government (SBCCG) membership fees. The NPDES water discharge permit program and SBCCG membership do not involve street maintenance, street construction, or street reconstruction; consequently, these expenditures are ineligible gas tax fund expenditures.

Streets and Highways Code section 2101 states, in part:

... all moneys in the Highway Users Tax Account in the Transportation Tax Fund and hereafter received in the account are appropriated for...  
(a) The research, planning, construction, improvement, maintenance, and operation of public streets.

Recommendation

The city should reimburse the Special Gas Tax Street Improvement Fund \$25,285 for the ineligible NPDES water discharge permit program and SBCCG membership fees. Additionally, the city should ensure that charges to the Special Gas Tax Street Improvement Fund are for costs specified in Streets and Highways Code section 2101.

City's Response

Management agrees with the recommendation and has reimbursed the Special Gas Tax Street Improvement Fund \$25,285 for the ineligible NPDES water discharge permit program and the SBCCOG Watershed Management Program (was not for membership fees). Management will ensure that charges to the Special Gas Tax Street Improvement Fund are for costs specified in the Streets and Highways Code section 2101.

SCO's Comment

The city agreed with our recommendation and stated that it has reimbursed \$25,285 to the Special Gas Tax Street Improvement Fund.

**FINDING 2—  
Lack of formal  
policies and  
procedures**

Our audit included evaluating various city policies and procedures. We noted that the city could benefit from establishing or updating the following policies:

- Financial Fraud
- General Fund/Other Fund Reserves
- Debt
- Grants
- Accounting and Financial Reporting
- Risk Management and Internal Controls



- Budget
- Revenues
- Local Vendor
- Long Range Financial Planning
- Debarment and Suspension
- Computer Disaster

Although the city has informal policies and procedures, the city will benefit from more formal and comprehensive policies approved by the city council. Establishing formal policies would provide detailed guidance to employees, management, and the city council, and help ensure process consistency and accountability, even during staff turnover.

#### Recommendation

We recommend the city establish and update formal policies in its manual.

#### City's Response

Management agrees with the recommendation. Management understands the need for policies and is in the process of establishing the listed policies.

#### SCO's Comment

The city agreed with our recommendation and stated that it is in the process of establishing the listed policies.

### **FINDING 3— Non-compliance with Government Code section 41004**

The city did not comply with Government Code (GC) section 41004, which requires the city treasurer to submit to the city clerk a monthly written report and an accounting of all receipts, disbursements, and fund balances.

GC section 41004 states:

Regularly, at least once each month, the city treasurer shall submit to the city clerk a written report and accounting of all receipts, disbursements, and fund balances. He shall file a copy with the legislative body.

#### Recommendation

We recommend that the city comply with GC section 41004 and ensure that the city treasurer submit to the city clerk a monthly written report and an accounting of all receipts, disbursements, and fund balances.

#### City's Response

Management agrees with the recommendation and is in the process of establishing a procedure to ensure that the City Treasurer submit to the City Clerk a monthly written report and an accounting of all receipts, disbursements, and fund balances.

SCO's Comment

The city agreed with our recommendation and stated that it is in the process of establishing a procedure to ensure compliance with GC section 41004.

**FINDING 4—  
Unsupported payroll  
cost allocation  
methodology**

The city charged a percentage of public works street employees' time instead of using actual time. The percentage of time used was based on estimates developed during the budget process, with no substantiating records of the determination of the percentage. In addition, the public works department does not keep time sheets or work logs that identify the street work performed by its staff.

All payroll expenditures charged to the Special Gas Tax Street Improvement Fund must be for actual street-related work. Payroll records should specify the date and street activity performed by public works street employees.

Recommendation

We recommend that employees paid out of the Special Gas Tax Street Improvement Fund complete a time sheet clearly identifying the street projects worked on. Alternatively, the public works department should keep work logs that identify the work performed by the employee.

The city must analyze its payroll cost allocation methodology and develop and document a cost allocation plan that equitably distributes payroll charges to various programs. Unsupported payroll cost allocations can result in unallowable expenditures.

City's Response

Management agrees with the recommendation and has established a new procedure starting July 1, 2017 that employees paid out of the Special Gas Tax Street Improvement Fund will complete a timesheet clearly identifying the street projects worked on.

SCO's Comment

The city agreed with our recommendation and stated that it has established a new procedure for employees who are paid out of the Special Gas Tax Street Improvement Fund; the procedure includes requiring the employee to complete a timesheet clearly identifying the street projects worked on.

**Attachment—  
City of Lomita’s Response to  
Draft Audit Report**

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**CITY COUNCIL**

MARK WARONEK  
MICHAEL G. SAVIDAN  
JIM GAZELEY  
HENRY SANCHEZ JR.  
BEN TRAINA



**CITY OF LOMITA**

**ADMINISTRATION**

RYAN SMOOT  
CITY MANAGER

May 12, 2017  
State Controller's Office  
P.O. Box 942850  
Sacramento, CA 95816

Dear Mr. Loste:

This letter is in response to the audit of the Special Gas Tax Street Improvement Fund for the period of July 1, 2015 through June 30, 2016. Here are our responses for the list of findings:

**Finding 1 – Ineligible non-street related consulting and membership fees expenditures**

Management agrees with the recommendation and has reimbursed the Special Gas Tax Street Improvement Fund \$25,285 for the ineligible NPDES water discharge permit program and the SBCCOG Watershed Management Program (was not for membership fees). Management will ensure that charges to the Special Gas Tax Street Improvement Fund are for costs specified in the Streets and Highways Code section 2101.

**Finding 2 – Lack of formal policies and procedures**

Management agrees with the recommendation. Management understands the need for policies and is in the process of establishing the listed policies.

**Finding 3 – Non-compliance with Government Code section 41004**

Management agrees with the recommendation and is in the process of establishing a procedure to ensure that the City Treasurer submit to the City Clerk a monthly written report and an accounting of all receipts, disbursements, and fund balances.

**Finding 4 – Unsupported payroll cost allocation methodology**

Management agrees with the recommendation and has established a new procedure starting July 1, 2017 that employees paid out of the Special Gas Tax Street Improvement Fund will complete a timesheet clearly identifying the street projects worked on.

State Controller's Office

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If you have any questions, please do not hesitate to contact me or Susan Kamada, Administrative Services Director, at (310) 325-7110.

Sincerely,

A handwritten signature in black ink, appearing to read "Ryan Smoot". The signature is fluid and cursive, with a large initial "R" and "S".

Ryan Smoot  
City Manager

**State Controller's Office  
Division of Audits  
Post Office Box 942850  
Sacramento, CA 94250-5874**

**<http://www.sco.ca.gov>**