

# **CITY OF SANTA MARIA**

Audit Report

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

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



**BETTY T. YEE**  
California State Controller

August 2019



**BETTY T. YEE**  
California State Controller

August 26, 2019

Jason Stilwell, City Manager  
City of Santa Maria  
110 East Cook Street  
Santa Maria, CA 93434

Dear Mr. Stilwell:

The State Controller's Office audited the City of Santa Maria's Special Gas Tax Street Improvement Fund to determine whether the city accounted for and expended its Special Gas Tax Street Improvement Fund in compliance with requirements 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, and that no adjustment to the fund is required. However, we identified deficiencies in internal control that are not significant to the audit objective, but warrant the attention of management.

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

Sincerely,

*Original signed by*

JIM L. SPANO, CPA  
Chief, Division of Audits

JLS/as

cc: The Honorable Alice Patino, Mayor  
City of Santa Maria  
Mary Harvey, Director  
Finance Department  
City of Santa Maria

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# Audit Report

## Summary

The State Controller's Office (SCO) audited the City of Santa Maria's Special Gas Tax Street Improvement Fund to determine whether the city accounted for and expended its Special Gas Tax Street Improvement Fund in compliance with requirements 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, and that no adjustment to the fund is required. However, we identified deficiencies in internal control that are not significant to the audit objective, but warrant the attention of management.

## Background

The State apportions funds monthly from the Highway Users Tax Account (HUTA) in the Transportation Tax Fund to cities<sup>1</sup> 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 Streets and Highways Code, cities must establish individual Special Gas Tax Street Improvement Funds for the deposit of their HUTA fund apportionments. Additionally, cities must expend their HUTA fund apportionments only for street-related purposes in accordance with Article XIX of the California Constitution and Streets and Highways Code. We conducted our audit of the city's Special Gas Tax Street Improvement Fund under the authority of Government Code section 12410.

## Objective, Scope, and Methodology

Our audit objective was 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 Streets and Highways Code.

The audit period was July 1, 2015, through June 30, 2016.

To achieve our objective, 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 an internal control questionnaire, and reviewing the city's organization chart;
- 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;

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<sup>1</sup>Includes towns.

- Verified the accuracy of fund balances by performing a fund balance reconciliation for the period of July 1, 2009, through June 30, 2015, and by recalculating the trial balance for the period of July 1, 2015, through June 30, 2016;
- Verified that the components of and changes to 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 all interest allocations for the audit period;
- Reviewed the fund cash and receivables accounts for unauthorized borrowing to determine whether unexpended HUTA funds were available for future street-related expenditures and protected from impairment; and
- Verified that the expenditures incurred during the audit period were supported by proper documentation and eligible in accordance with the applicable criteria, by testing all expenditure transactions that were equal to or greater than the significant item amount (calculated based on materiality threshold), and judgmentally selecting non-statistical samples of other transactions for the following categories:
  - Services and Supplies – We tested \$235,198 of \$863,281.
  - Transfers – We tested \$64,868 of \$643,076.

For the selected samples, errors found, if any, were not projected to the intended (total) population.

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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

**Conclusion**

Our audit found that the City of Santa Maria accounted for and expended its Special Gas Tax Street Improvement Fund in compliance with Article XIX of the California Constitution and Streets and Highways Code for the period of July 1, 2015, through June 30, 2016. However, we identified deficiencies in internal control that are not significant to the audit objective, but warrant the attention of management. These deficiencies are described in the Observations and Recommendations section of this audit report.

**Follow-up on Prior Audit Findings**

Our prior audit report for the period of July 1, 2008, through June 30, 2009, issued on September 22, 2010, disclosed no findings.

**Views of Responsible Officials**

We issued a draft report on April 23, 2019, which included a \$23,315 finding resulting in an understatement of the fund balance by the same amount. Jason Stilwell, City Manager, responded by letter dated May 2, 2019 (Attachment), disagreeing with the finding. On May 20, 2019, Mary Harvey, Director of Finance, followed up with an email that provided documentation showing that aerial photography is an eligible activity. As a result, we have removed the finding from this final audit report.

**Restricted Use**

This audit report is solely for the information and use of the City of Santa Maria 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 audit report, which is a matter of public record and is available on the SCO website at [www.sco.ca.gov](http://www.sco.ca.gov).

*Original signed by*

JIM L. SPANO, CPA  
Chief, Division of Audits

August 26, 2019

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

	Special Gas Tax Street Improvement Fund <sup>1,2</sup>
Beginning fund balance per city	\$ 3,339,785
Revenues	<u>2,237,838</u>
Total funds available	5,577,623
Expenditures	<u>(1,506,357)</u>
Ending fund balance per city	<u>\$ 4,071,266</u>
Ending fund balance per audit	<u><u>\$ 4,071,266</u></u>

<sup>1</sup>Cities receive 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. Cities must establish individual Special Gas Tax Street Improvement Funds for the deposit of their HUTA fund apportionments. The city established the Gas Tax and Local Street Fund for the deposit of its HUTA fund apportionments.

<sup>2</sup>The fund balance shown in the Schedule is for HUTA funds only. The city's Gas Tax and Local Street Fund balance at June 30, 2016, was \$4,516,030, which includes non-HUTA funds.

# Observations and Recommendations

## **OBSERVATION 1— Lack of Documented Policies and Procedures**

During our review of the various written city policies and procedures, we noted that the city had not established formal policies that:

- Clarify procedures for grant administration;
- Set forth long-term financial planning for the city;
- Set policies that address a range of issues related to city expenditures, including personnel, outsourcing, and funding long-term liabilities;
- Set policies that establish an efficient and effective revenue system to guarantee the generation of adequate public resources to meet expenditure obligations;
- Clarify procedures for dealing with debarred and suspended vendors;
- Clarify procedures for unclaimed checks; and
- Protect the integrity of the city's information system in case of a disaster.

The Government Finance Officers Association recommends that governments formally adopt financial policies. Adopting comprehensive formal policies would provide detailed guidance to employees, management, and the city council and ensure consistency and accountability during staff turnover.

### Recommendation

We recommend that the city adopt formal policies and procedures for the items noted above, to ensure that controls are in place to strengthen financial accountability.

### City's Response

The City recognizes the importance of establishing financial policies and procedures and acknowledges that this area can be improved. The City has numerous policies and procedures that are accessible to employees on the City's Intranet. In fact, the City has established procedures for three of the seven policies and procedures specifically noted in the observation. As for the remaining four policies, the City has informal procedures that have been in practice for many years. The City, like many municipalities, has experienced staffing shortages due to budget constraints and attrition, which makes it difficult to establish new policies and update existing ones. The City will continue to review, update, and establish formal written policies and procedures to improve the City's overall financial internal control.



SCO Comment

The observation remains as stated.

As indicated, our audit procedures involved obtaining and evaluating various city policies and procedures. During the audit process and at the exit conference held on March 5, 2019, we requested to review the policies and procedures for the areas identified in the Observation. As of the date of this report, we have not been provided with any documents that validate the city's response.

**OBSERVATION 2—  
Expired Service  
Contract**

During our testing of expenditures and performing a review of source documents, we found an expired tree trimming services contract. Per the contract terms, the contract can only be extended by written agreement:

4.04 Termination: This agreement shall terminate one year from the date of execution unless extended as set forth in this section. The City, with the agreement of Contractor, is authorized to extend the term of this Agreement beyond the termination date, as needed, under the same terms and conditions set forth in this agreement. Any such extension shall be in writing and be an amendment to this agreement.

Contrary to the contract language, the city only made a verbal agreement with the contractor to extend the service period after the contract term expired.

Additionally, the city's Municipal Code, Title 3, Chapter 3-4, Article III, section 3-4.30 states:

The purchases and contracts for supplies, services, equipment, and construction projects, except as otherwise provided in this chapter, which are equal to or in excess of "formal bidding" requirement amount specified in the Purchasing Guidelines, shall be by written contract with the lowest responsible bidder pursuant to the procedures prescribed in the article.

Recommendation

We recommend that the city:

- Establish a contract monitoring system;
- Ensure that expired contracts are renewed in writing; and
- Ensure that contracts are in compliance with the city's purchasing requirements for contract services.

City's Response

The city agreed with the observation.

**OBSERVATION 3—  
Payment of Non-  
Itemized Invoices**

During our review of source documents, we found invoices related to two consultant-services contracts. These invoices did not include itemized listings of costs incurred, although these contracts indicate that the consultants' bills would include an itemized listing of costs incurred. The consultant-services contracts state:

II. Invoice Procedures

C. Consultant's bills shall be substantiated by appropriate documentation, and include an itemized listing of personnel, sub consultants and other direct costs incurred.

Although the services are gas tax eligible and the expenditures are therefore allowable, invoices that do not include itemized costs expose the city to overcharges for services.

Recommendation

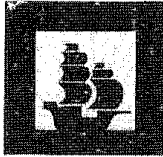
We recommend that the city follow invoice procedures as indicated in service contracts to ensure that the city is paying only for services stated in its contracts.

City's Response

The city agreed with the observation.

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

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CITY OF SANTA MARIA  
OFFICE OF THE CITY MANAGER  
City Manager, Ext. 2200  
Human Resources, Ext. 2203

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May 2, 2019

Efren Loste, Chief  
Local Government Audits Bureau  
State Controller's Office  
Division of Audits  
P.O. Box 942850  
Sacramento, CA. 94250

RE: City of Santa Maria  
Audit Report, Special Gas Tax Street Improvement Fund  
July 1, 2015 through June 30, 2016

Dear Mr. Loste:

Enclosed is the City of Santa Maria's response to the draft audit report of compliance in relation to the City's Special Gas Tax Street Improvement Fund. We appreciate the opportunity to respond to your findings and observations before the audit report is finalized.

If you have any questions about the City's response, please do not hesitate to contact Mary Harvey, Director of Finance, at (805) 925-0951 extension 2214.

Sincerely,

**JASON STILWELL**  
City Manager

Enclosure

cc: Mary Harvey, Director of Finance, City of Santa Maria  
Kevin McCune, Director of Public Works, City of Santa Maria

**City of Santa Maria Response to Audit Finding and Observations in  
Special Gas Tax Street Improvement Fund Audit Report Dated April 2019**

Response to Finding – Ineligible expenditures:

The City of Santa Maria (City) disagrees with the audit finding that \$20,315 charged for aerial mapping is an ineligible non-street service or supply. The City's Public Works Department (PW) utilizes aerial photography through the City's GIS programs in several ways. The aerial photography is heavily used by PW staff to complete in house design of capital projects. This includes the design of paving, sidewalk, ADA ramps, traffic control, curb, gutter, and other roadway drainage facilities. The aerial photography also allows our permitting staff to review and issue permits that involve work within the City street right of way. Furthermore, PW inspectors use aerial photography in the field as a resource to verify and confirm pre-existing roadway conditions, roadway striping, and any other roadway facilities that may have been impacted by construction projects. Lastly, the PW Streets Division staff regularly use the aerial photography for review, analysis, and confirmation of right of way concrete and roadway facilities.

In summary, aerial mapping is a tool used to assist in street maintenance, street construction, and street reconstruction. Therefore, it is an eligible gas tax expenditure, and for this reason, the City requests this finding be removed from the audit report.

Response to Observation 1 – Lack of policies and procedures:

The City recognizes the importance of establishing financial policies and procedures and acknowledges that this area can be improved. The City has numerous formal policies and procedures that are accessible to employees on the City's Intranet. In fact, the City has established procedures for three of the seven policies and procedures specifically noted in the observation. As for the remaining four policies, the City has informal procedures that have been in practice for many years. The City, like many municipalities, has experienced staffing shortages due to budget constraints and attrition, which makes it difficult to establish new policies and update existing ones. The City will continue to review, update, and establish formal written policies and procedures to improve the City's overall financial internal control.

Response to Observation 2 – Expired Service Contract:

The City acknowledges that the tree trimming contract reviewed during the audit was not extended in writing as required by City policy. The City is in the process of developing a contract monitoring system to ensure that contracts meet City policies and purchasing guidelines. Training has been provided to educate employees on City policies and procedures and specifically pertaining to contracts and the employees' responsibility when entering into and maintaining contracts. The City will continue to provide training to employees and is pursuing a technology-based system to assist with managing contracts city-wide.

Response to Observation 3 – Payment of non-itemized invoices:

The City affirms that invoices related to two consultant service contracts did not contain the itemized detail as required by the respective contracts. The City has and will continue to work with staff to reinforce the importance of requiring vendors to provide itemized invoices. The City understands the importance of adhering to the terms of a contract and obtaining proper documentation prior to making payment of invoices.

**State Controller's Office  
Division of Audits  
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Sacramento, CA 94250**

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