

CITY OF GUADALUPE

Audit Report

SPECIAL GAS TAX STREET IMPROVEMENT FUND

July 1, 2015, through June 30, 2016



BETTY T. YEE
California State Controller

October 2018



BETTY T. YEE
California State Controller

October 25, 2018

Cruz Ramos, City Administrator
City of Guadalupe
918 Obispo Street
Guadalupe, CA 93434

Dear Ms. Ramos:

The State Controller's Office audited the City of Guadalupe'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 understated the fund balance by \$62,732 as of June 30, 2016, because it charged costs for non-street services to the fund. We also 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 Loste, Chief, Local Government Audits Bureau, by telephone at (916) 324-7226.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/as

cc: Annette Muñoz, Finance Director
City of Guadalupe
John Lizalde, Mayor
City of Guadalupe

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Audit Report

Summary

The State Controller's Office (SCO) audited the City of Guadalupe'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 understated the fund balance by \$62,732 as of June 30, 2016, because it charged costs for non-street services to the fund. We also 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 cities¹ 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 Fund 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 (GC) 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.

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

To achieve our objective, we:

- Gained a limited understanding of internal control that would have an effect on the reliability of the accounting records of the Special Gas Tax Street Improvement Fund by evaluating various city policies and procedures, interviewing key personnel, completing the 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;

¹Includes towns.

- Verified the accuracy of fund balances by performing a fund balance reconciliation for the period of July 1, 2001, 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;
- 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 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 all of the expenditure transactions that were equal to or greater than the significant item amount (calculated based on materiality threshold), and judgmentally (non-statistically) selecting samples of other transactions for the following categories:
 - Services and Supplies – We tested \$87,463 of \$130,659.
 - Transfers – We tested \$37,100 of \$37,100.

For the selected sample, errors found, if any, were not projected to the intended 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 control 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 an instance of non-compliance for the period of July 1, 2015, through June 30, 2016, as noted in the Schedule and described in the Finding and Recommendation section of this report. The finding requires an adjustment of \$62,732 to the city's accounting records. We also 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 report.
Follow-up on Prior Audit Findings	Our prior audit report, for the period of July 1, 2000, through June 30, 2001, issued on February 7, 2003, disclosed no findings.
Views of Responsible Officials	We issued a draft audit report on January 12, 2018. Annette Muñoz, Finance Director, responded by letter dated January 23, 2018, partially agreeing with the Finding, and agreeing with Observations 2, 3, and 4. The city did not respond to Observations 1 and 5. The city's response is included in this final audit report as an attachment.
Restricted Use	This audit report is solely for the information and use of the City of Guadalupe 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.

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

October 25, 2018

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

	Special Gas Tax Street Improvement Fund ¹
Beginning fund balance per city	\$ 550,091
Revenues	<u>263,460</u>
Total funds available	813,551
Expenditures	<u>(167,759)</u>
Ending fund balance per city	645,792
SCO adjustment: ²	
Finding—Ineligible National Pollutant Discharge Elimination System expenditures	<u>62,732</u>
Ending fund balance per audit	<u>\$ 708,524</u>

¹Cities 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.

²See the Finding and Recommendation section.

Finding and Recommendation

**FINDING—
Ineligible National
Pollutant Discharge
Elimination System
expenditures**

The city charged \$130,659 in services and supplies expenditures. We tested \$87,463 in expenditures and determined that \$62,732 was for ineligible costs related to a National Pollutant Discharge Elimination System (NPDES) water discharge permit. The water discharge permit program does not involve street maintenance, street construction, or street reconstruction; therefore, these are ineligible costs. The error occurred because the city did not have adequate procedures to ensure that expenditures charged to the Special Gas Tax Street Improvement Fund are for street-related activities.

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 and highways....

Recommendation

We recommend that the city:

- Reimburse the Special Gas Tax Street Improvement Fund \$71,507 for the ineligible NPDES expenditures; and
- Establish procedures to ensure that funds expended from the Special Gas Tax Street Improvement Fund are for costs specified in Streets and Highways Code section 2101.

City's Response

The city conducted an audit of the invoices that total \$71,506.50. The city determined there were \$8,775 in eligible costs that were for paving project and street slurry. The revised total for ineligible expenditures is \$62,731.50.

SCO Comment

Based on our review of additional documentation provided by the city, we revised the draft report finding by \$8,774, from \$71,507 to \$62,732.

During our initial review of the billings by an engineering firm, the billings did not identify the costs relating to street-related work. The city provided additional supporting documentation regarding the questioned engineering services, which identified the cost of street-related services.

Observations and Recommendations

OBSERVATION 1— Expired service contracts

During our review of service contracts, we found three expired gas tax service contracts. Each service contract indicated that the contract could be extended only by written agreement. However, for the three expired contracts, the city made a verbal agreement with each contractor to extend the service period until terminated by either party.

Recommendation

We recommend that the city establish procedures to closely monitor contracts for expiration and ensure that contracts are properly executed through a written agreement.

SCO Comment

The city did not address this observation in its response to the draft audit report.

OBSERVATION 2— General Fund cash impairment

During FY 2015-16, the city's General Fund cash account reported month-end negative balances for all 12 months. As the city pools the cash from all of its funds, a negative balance in the General Fund cash potentially impairs the other funds, including restricted funds such as the Special Gas Tax Street Improvement Fund. This is because the city might inadvertently use the restricted funds' available balances to pay for the city's operating costs. As of the end of audit field work, the city had not demonstrated that it has restored the financial health of the General Fund. Consequently, the General Fund is inadvertently affecting the integrity of the Special Gas Tax Street Improvement Fund.

Streets and Highways Code section 2118 states:

When the State Controller determines it to be necessary, he may require a county or city to deposit money received from the Highway Users Tax Fund in a separate bank account.

Recommendation

We recommend that the city establish a separate bank account for the state gas tax fund money. This account should be used to record all deposits and expenditures against the money. The bank account shall remain open until the city provides evidence that, over a reasonable period of time, it has restored the financial health of its General Fund.

City's Response

The City will establish a separate bank account for the state gas tax money until the General Fund is in a consistent positive position.

**OBSERVATION 3—
Lack of policies and
procedures**

Our audit procedures involved obtaining and evaluating various city policies and procedures. During our review, we noted that the city could benefit from establishing the following policies:

- General Fund/other fund reserves
- Grants
- Debt
- Risk management
- Budget
- Long range financial planning
- Capital
- Local vendor
- Debarment and suspension
- Unclaimed check
- Computer disaster

Establishing formal policies would provide detailed guidance to employees, management, and the city council, and would help ensure process consistency and accountability during staff turnover.

Recommendation

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

City's Response

The City will continue to work on updating and establishing the policies listed in the audit.

**OBSERVATION 4—
Non-compliance with
GC section 41004**

The city did not comply with GC section 41004 for FY 2015-16. This section requires the city treasurer to submit to the city clerk a monthly written report and an accounting of all receipts, disbursements, and fund balances.

Compliance with GC section 41004 increases the accountability of receipts, disbursements, and fund balances.

We identified this error when reviewing the city's cash and fund balance controls. The city did not have procedures in place to ensure compliance with the above requirement. The city's non-compliance with this requirement does not affect the Special Gas Tax Street Improvement Fund compliance with Article XIX of the California Constitution and Streets and Highways Code.

Recommendation

We recommend that the city establish procedures to ensure compliance with GC section 41004.

City's Response

The City has commenced the reporting of fund balances to the city clerk. Receipts and disbursements have historically been reported.

**OBSERVATION 5—
Ability to continue as
a going concern**

The independent auditor's report for FY 2015-16 noted in the Emphasis of Matters section that the financial statements were prepared assuming that the city will continue as a going concern; however, revenue shortfalls and interfund borrowing raise doubts about the city's ability to continue as a going concern. The independent auditor's statement reads:

The accompanying financial statements have been prepared assuming that the City will continue as a going concern. As discussed in Note 19 to the financial statements, the City has experienced decreased revenues and key budgeted revenue sources are unknown. Management projects continued budget shortfalls unless significant costs reduction or other measures are taken. The City has borrowed from other funds to reduce the negative cash balance and sustain its basic operations. These conditions raise substantial doubt about the city's ability to continue as a going concern. Management's plans regarding those matter are described in Note 19. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

Recommendation

We recommend that the city take appropriate steps and develop an action plan to balance the General Fund budget and monitor its cash flow closely.

SCO Comment

The city did not address this observation in its response to the draft audit report.

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



CITY OF GUADALUPE
918 Obispo Street
P.O. Box 908
Guadalupe, CA 93434
Tel (805) 356-3895
Fax (805) 343-0542
Finance Department

January 23, 2018

CERTIFIED MAIL-RETURN RECEIPT REQUESTED

Efren Loste Chief, Local Government Audits Bureau
State Controller's Office, Division of Audits
P.O. Box 942850
Sacramento, CA 94250-5874

Dear Mr. Loste:

This correspondence is in response to the January 12, 2018 letter from the State Controller's Office that references the draft audit for the Special Gas Tax Street Improvement Fund for the City of Guadalupe.


Finding 1: Ineligible National Pollutant Discharge Elimination System Expenditures: The City conducted an audit of the invoices that total \$71,506.50. The City determined there were \$8,775 in eligible costs that were for a paving project and street slurry. The revised total for ineligible expenditures is \$62,731.50 (see enclosure).

Finding 2: General Fund Cash Impairment: The City will establish a separate bank account for the state gas tax money until the General Fund is in a consistent positive position.

Finding 3: Lack of Policies and Procedures: The City will continue to work on updating and establishing the policies listed in the audit.

Finding 4: Non-compliance with Government Code section 41004. The City has commenced the reporting of fund balances to the city clerk. Receipts and disbursements have historically been reported.

Sincerely,


Annette Muñoz
Finance Director
City of Guadalupe

Encl

cc: Cruz Ramos, City Administrator, City of Guadalupe

City of Guadalupe
MS4 Charges
Fiscal Year 15-16

Check#	Invoice #	Inv Date	Vendor	Amount	Acct charged	Drainage		MS4		Permit/ Slurry	Total	Comments
						Transfer to	Transfer to	Mo report	Transfer to			
						71.4454.2150	71.4454.2150	01.4405.2150	12.4425.2150			
825334	2015-024	8/4/15	Elkhorf	2,437.50	20.4430.2150	2,437.50	0.00	0.00	0.00	0.00	2,437.50	SOCAG mtg with PE for 2015 Pavement project.
825334	2015-024	8/4/15	Elkhorf	975.00	20.4430.2150	0.00	0.00	0.00	975.00	0.00	975.00	MS4
825334	2015-024	8/4/15	Elkhorf	1,237.50	20.4430.2150	0.00	0.00	0.00	1,237.50	0.00	1,237.50	MS4
825406	610482015	8/19/15	Co-wi-58	3,224.00	20.4430.2150	0.00	0.00	0.00	3,224.00	0.00	3,224.00	MS4
825478	91115	9/9/15	Elkhorf	1,125.00	20.4430.2150	0.00	1,125.00	0.00	0.00	0.00	1,125.00	Paving project, drainage project
825478	91115	9/9/15	Elkhorf	1,350.00	20.4430.2150	0.00	0.00	0.00	1,350.00	0.00	1,350.00	MS4 charges 9 hrs
825478	91115	9/9/15	Elkhorf	900.00	20.4430.2150	0.00	0.00	0.00	900.00	0.00	900.00	MS4 charges
825549	2015-037	10/9/15	Elkhorf	4,275.00	20.4430.2150	4,275.00	0.00	0.00	0.00	0.00	4,275.00	Originally Measure A for drainage projects
825549	2015-037	10/9/15	Elkhorf	2,590.00	20.4430.2150	0.00	0.00	0.00	2,590.00	0.00	2,590.00	MS4 charges 8 hrs
825549	2015-037	10/9/15	Elkhorf	2,590.00	20.4430.2150	0.00	0.00	0.00	0.00	0.00	2,590.00	11st Street Drainage Project, Railroad to Peralta
825673	2015-040	11/2/15	Elkhorf	3,000.00	20.4430.2150	0.00	0.00	0.00	3,000.00	0.00	3,000.00	MS4 charges
825673	2015-040	11/2/15	Elkhorf	5,325.00	20.4430.2150	0.00	0.00	0.00	0.00	0.00	5,325.00	West Main drainage project.
825673	2015-040	11/2/15	Elkhorf	3,075.00	20.4430.2150	0.00	0.00	0.00	3,075.00	0.00	3,075.00	MS4
825673	2015-040	11/2/15	Elkhorf	640.00	20.4430.2150	0.00	0.00	0.00	0.00	0.00	640.00	11st Street Drainage Project, Railroad to Peralta
825673	2015-040	11/2/15	Elkhorf	825.00	20.4430.2150	0.00	0.00	0.00	0.00	0.00	825.00	MS4 charges
825791	120215	12/1/15	Elkhorf	2,775.00	20.4430.2150	2,775.00	0.00	0.00	0.00	0.00	2,775.00	TTAC/TIAC, mtg, El Nino Storm Water tech guide
825791	120215	12/1/15	Elkhorf	760.00	20.4430.2150	0.00	0.00	0.00	0.00	0.00	760.00	11st Street Drainage Project, Railroad to Peralta
825915	2016-001	1/6/16	Elkhorf	2,325.00	20.4430.2150	0.00	0.00	0.00	2,325.00	0.00	2,325.00	Drainage proj,ERT mtg,MS4, mo report
825915	2016-001	1/6/16	Elkhorf	2,045.00	20.4430.2150	0.00	0.00	0.00	2,045.00	0.00	2,045.00	MS4 charges
Sub total Part 1						40,084.00	14,812.50	5,490.00	75.00	19,706.50	0.00	40,084.00

Check#	Invoice #	Inv Date	Vendor	Amount	Acct charged	Drainage		MS4		Permit/ Slurry	Total	Comments
						Transfer to	Transfer to	Mo report	Transfer to			
						71.4454.2150	71.4454.2150	01.4405.2150	12.4425.2150			
826043	2016-010	2/3/16	Elkhorf	2,475.00	20.4430.2150	0.00	0.00	0.00	1,425.00	150.00	2,475.00	Drain proj, 2016 paving/slurry project, MS4, mo rpt
826043	2016-010	2/3/16	Elkhorf	6,187.50	20.4430.2150	0.00	0.00	0.00	3,472.50	2,900.00	6,187.50	MS4, 2016 paving project, 4th St drainage repairs
826159	2016-017	3/1/16	Elkhorf	4,650.00	20.4430.2150	1,275.00	0.00	150.00	2,175.00	1,050.00	4,650.00	MS4, 4th St site visit, 2016 paving/slurry, TPAC, TTAC, mo rpt
826256	2016-024	4/1/16	Elkhorf	3,220.00	20.4430.2150	0.00	1,230.00	0.00	1,670.00	2,280.00	3,220.00	MS4, 2016 paving project, 4th Street drainage repairs
826256	2016-024	4/1/16	Elkhorf	4,425.00	20.4430.2150	1,650.00	0.00	150.00	460.00	2,175.00	4,425.00	MS4, Statewide street assessment, 2016 paving/slurry, TPAC/IPAC, mo report
826398	2016-028	5/3/16	Elkhorf	490.00	20.4430.2150	0.00	0.00	0.00	490.00	0.00	490.00	MS4
826398	2016-028	5/3/16	Elkhorf	3,450.00	20.4430.2150	1,125.00	0.00	0.00	300.00	2,025.00	3,450.00	MS4, 2016 paving/slurry proj, TPAC/IPAC, ATP Cycle3
826651	2016-043	6/3/16	Elkhorf	770.00	20.4430.2150	0.00	0.00	0.00	770.00	0.00	770.00	MS4
826651	2016-043	6/3/16	Elkhorf	3,675.00	20.4430.2150	1,200.00	0.00	150.00	0.00	3,325.00	3,675.00	2016 Pvmnt maint proj, 2016 Pavment rehab proj, field mtg for Guad ped crossing, PDT mtg, TPAC/IPAC mtg, mo report
826655	2016-048	7/2/17	Elkhorf	1,800.00	20.4430.2150	1,800.00	0.00	150.00	0.00	1,050.00	3,000.00	2016 Pavment maint proj, 2016 Pavment rehab proj, field mtg for Guad ped crossing, PDT mtg, TPAC/IPAC mtg, mo report
Sub total Part 2						32,342.50	7,050.00	675.00	10,952.50	9,695.00	32,342.50	
Streets w/s						1,525.00	0.00	0.00	0.00	0.00	1,525.00	
SCO Total						71,506.50	21,862.50	9,460.00	75.00	30,659.00	71,426.50	
Additional Street						(8,775.00)	(9,695.00)	(800-120)			9,695.00	
Final Total						62,731.50					62,731.50	

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

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