

CITY OF TEHACHAPI

Audit Report

SPECIAL GAS TAX STREET IMPROVEMENT FUND

July 1, 2015, through June 30, 2016



BETTY T. YEE
California State Controller

October 2018



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California State Controller

October 17, 2018

Hannah Chung, Finance Director
City of Tehachapi
115 South Robinson Street
Tehachapi, CA 93561

Dear Ms. Chung:

The State Controller's Office audited the City of Tehachapi'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 \$1,233 as of June 30, 2016. The city understated the fund balance because it charged an ineligible expenditure to the Special Gas Tax Street Improvement Fund. We also identified two deficiencies in internal control that are not significant to the audit objectives 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: Gregg Garrett, City Manager
City of Tehachapi
Ed Grimes, Mayor
City of Tehachapi

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Audit Report

Summary

The State Controller's Office (SCO) audited the City of Tehachapi'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 \$1,233 as of June 30, 2016. The city understated the fund balance because it charged an ineligible expenditure to the Special Gas Tax Street Improvement Fund. We also identified two deficiencies in internal control that are not significant to the audit objectives 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 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 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 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, 2010, 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 \$94,048 of \$368,827.
 - Labor – We tested \$48,461 of \$172,723.
 - Indirect – We tested \$73,557 of \$73,557.

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 \$1,233 to the city’s accounting records.

We also identified two deficiencies in internal control that are not significant to the audit objectives 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, 2007, through June 30, 2010, issued on April 27, 2012, disclosed no findings.

Views of Responsible Officials

We issued a draft audit report on April 20, 2018. Hannah Chung, Finance Director, responded by email on May 8, 2018, accepting the audit findings and recommendations as presented in the draft audit report.

Restricted Use

This audit report is solely for the information and use of the City of Tehachapi 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 17, 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	\$ —
Revenues	<u>615,107</u>
Total funds available	615,107
Expenditures	<u>(615,107)</u>
Ending fund balance per city	—
SCO adjustment: ²	
Finding—Ineligible expenditure	<u>1,233</u>
Ending fund balance per audit	<u>\$ 1,233</u>

¹Cities (towns) 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 expenditure**

The city charged \$1,233 in ineligible services and supplies expenditures to the Special Gas Tax Street Improvement Fund in FY 2015-16.

The city charged \$368,827 in services and supplies expenditures. We tested \$94,048 and determined that \$1,233 was for ineligible equipment rental costs. The city used the equipment to install Christmas lights. The remaining costs tested were for eligible street-related purposes. 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....

The city provided Journal Entry No. 79, dated June 15, 2017, to reimburse the Special Gas Tax Street Improvement Fund.

Recommendation

We recommend that the city establish procedures to ensure that all expenditures charged to the Special Gas Tax Street Improvement Fund are for eligible costs specified in the Streets and Highways Code.

Observations and Recommendations

**OBSERVATION 1—
Non-compliance with
purchase orders
policy**

The city did not comply with its Municipal Code section 3.04.090 for FY 2015-16. This section requires the city to use purchase orders when purchasing products or services.

We identified this error during our testing of gas tax expenditures. 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 the Streets and Highways Code.

Subsequent to the issuance of the draft report dated June 12, 2017, the city provided a copy of a new purchasing ordinance that it adopted on June 19, 2017.

Recommendation

We recommend that the city implement and monitor the June 19, 2017 purchasing ordinance to ensure that it complies with its Municipal Code section 3.04.090.

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

When reviewing existing city policies and procedures, we noted that the city did not have formal policies and procedures during FY 2015-16 for the following:

- Recording and expending Gas Tax funds
- Maintaining an approved vendor list

Establishing formal policies and procedures would provide detailed guidance to employees, management, and the city council, and would help ensure process consistency during staff turnover. The lack of formal policies and procedures did not have a significant impact on the audit objective.

Recommendation

We recommend that the city establish policies and procedures for the functions identified above to ensure that controls are in place to strengthen financial accountability.

**State Controller's Office
Division of Audits
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<http://www.sco.ca.gov>