

MERCED COUNTY

Audit Report

ROAD FUND

July 1, 2009, through June 30, 2010



JOHN CHIANG
California State Controller

November 2012



JOHN CHIANG
California State Controller

November 13, 2012

The Honorable Hubert "Hub" Walsh, Chair
Board of Supervisors
Merced County
2222 M Street
Merced, CA 95340

Dear Mr. Walsh:

The State Controller's Office (SCO) audited Merced County's Road Fund for the period of July 1, 2009, through June 30, 2010.

We also reviewed road-purpose revenues, expenditures, and changes in fund balances for the period of July 1, 2004, through June 30, 2009. The results of this review are included in our audit report.

The county accounted for and expended Road Fund moneys in compliance with Article XIX of the California Constitution, the Streets and Highways Code, and the SCO's Accounting Standards and Procedures for Counties manual, except for procedural findings identified in this report.

If you have any questions, please contact Steven Mar, Chief, Local Government Audits Bureau, at (916) 324-7226.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

JVB/vb

cc: The Honorable Lisa Cardella-Presto, Auditor-Controller
Merced County
Dana S. Hertfelder, Director of Public Works
Merced County

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Audit Report

Summary

The State Controller's Office (SCO) audited Merced County's Road Fund for the period of July 1, 2009, through June 30, 2010. We also reviewed road-purpose revenues, expenditures, and changes in fund balances for the period of July 1, 2004, through June 30, 2009. This review was limited to performing inquiries and analytical procedures to ensure that (1) highway users tax apportionments and road-purpose revenues were properly accounted for and recorded in the Road Fund; (2) expenditure patterns were consistent with the period audited; and (3) unexpended fund balances were carried forward properly.

Our audit and review disclosed that the county accounted for and expended Road Fund moneys in compliance with Article XIX of the California Constitution, the Streets and Highways Code, and the SCO's Accounting Standards and Procedures for Counties manual.

Background

We conducted an audit of the county's Road Fund in accordance with Government Code section 12410. The Road Fund was established by the county boards of supervisors in 1935, in accordance with Streets and Highways Code section 1622, for all amounts paid to the county out of moneys derived from the highway users tax fund. A portion of the Federal Forest Reserve revenue received by the county is also required to be deposited into the Road Fund (Government Code section 29484). In addition, the county board of supervisors may authorize the deposit of other sources of revenue into the Road Fund. Once moneys are deposited into the Road Fund, it is restricted to expenditures made in compliance with Article XIX of the California Constitution and Streets and Highways Code Sections 2101 and 2150.

Objectives, Scope, and Methodology

The objectives of our audit of the Road Fund were to determine whether:

- Highway users tax apportionments received by the county were accounted for in the Road Fund, a special revenue fund;
- Expenditures were made exclusively for authorized purposes or safeguarded for future expenditure;
- Reimbursements of prior Road Fund expenditures were identified and properly credited to the Road Fund;
- Non-road-related expenditures were reimbursed in a timely manner;
- The Road Fund cost accounting is in conformance with the SCO's Accounting Standards and Procedures for Counties manual, Chapter 9, Appendix A; and
- Expenditures for indirect overhead support service costs were within the limits formally approved in the Countywide Cost Allocation Plan.

Our audit objectives were derived from the requirements of Article XIX of the California Constitution, the Streets and Highways Code, the Government Code, and the SCO's Accounting Standards and Procedures for Counties manual. To meet the objectives, we:

- Gained a basic understanding of the management controls that would have an effect on the reliability of the accounting records of the Road Fund, by interviewing key personnel and testing the operating effectiveness of the controls;
- Verified whether all highway users tax apportionments received were properly accounted for in the Road Fund, by reconciling the county's records to the State Controller's payment records;
- Analyzed the system used to allocate interest and determined whether the interest revenue allocated to the Road Fund was fair and equitable, by interviewing key personnel and testing a sample of interest calculations;
- Verified that unauthorized borrowing of Road Fund cash had not occurred, by interviewing key personnel and examining the Road Fund cash account entries; and
- Determined, through testing, whether Road Fund expenditures were in compliance with Article XIX of the California Constitution and with the Streets and Highways Code, and whether indirect cost allocation plan charges to the Road Fund were within the limits approved by the SCO's Division of Accounting and Reporting, County Cost Plan Unit.

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.

We did not audit the county's financial statements. Our scope was limited to planning and performing audit procedures necessary to obtain reasonable assurance concerning the allowability of expenditures claimed for reimbursement. Accordingly, we examined transactions on a test basis to determine whether they complied with applicable laws and regulations and were properly supported by accounting records. We considered the county's internal controls only to the extent necessary to plan the audit.

Conclusion

Our audit and review disclosed that the county accounted for and expended Road Fund moneys in compliance with Article XIX of the California Constitution, the Streets and Highways Code, and the SCO's Accounting Standards and Procedures for Counties manual, except for the items described in the Findings and Recommendations section of this report.

**Follow-up on Prior
Audit Findings**

Our prior audit report, issued on September 28, 2005, disclosed no findings.

**Views of
Responsible
Official**

We discussed the audit results with county representatives during an exit conference on October 10, 2012. Shermaene Roemhildt, DPW Deputy Director-Administration, agreed with the audit results. Ms. Roemhildt further agreed that a draft audit report was not necessary and that the audit report could be issued as final. Ms. Roemhildt provided responses to the audit findings and recommendations in an e-mail on October 12, 2012. The responses are included after each finding in this report.

Restricted Use

This report is solely for the information and use of Merced County, the Merced County Board of Supervisors, 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
Chief, Division of Audits

November 13, 2012

**Schedule 1—
Reconciliation of Road Fund Balances
July 1, 2009, through June 30, 2010**

	<u>Amount</u>
Beginning fund balance per county	\$ 8,209,249
Revenues	<u>27,338,742</u>
Total funds available	35,547,991
Expenditures	<u>(22,277,820)</u>
Ending fund balance per county	13,270,171
Total SCO audit adjustment	<u>—</u>
Ending fund balance per audit	<u><u>\$ 13,270,171</u></u>

Findings and Recommendations

FINDING 1— High clearing account variance

The fiscal year (FY) 2009-10 Annual Road Report (ARR), Schedule 7 (Clearing Account Activity) presented high variances for labor (+5.54%), equipment (-73.44%), and general road overhead (-50.34%).

The SCO's Accounting Standards and Procedures for Counties manual, Chapter 9A, sections 14–23 prescribes the method used in the development and operation of the labor, equipment, and general road overhead clearing accounts. Per section 24, the acceptable range for labor variances should be +/-5% and +/-10% for the equipment, general and overhead variances.

Recommendation

The county should analyze its clearing accounts and correct the respective applied labor rates, equipment rental rates and, overhead rates for FY 2010-11. In addition, the county should monitor its variances quarterly during the year in order to meet the SCO Manual variance parameters.

County's Response

Since this audit, Merced County has continued to monitor and finesse the variances for labor, equipment and general road overhead. The equipment variance has been reduced from a high of 73.44% down to 1.14% at the close of last fiscal year. The general road overhead has gone from 50.34% to 10.9%. We will continue to monitor the variances to keep them in the acceptable ranges.

FINDING 2— Activity listings finding

Review of the activity listing shows that 20% of overhead charges are applied to non-productive activities such as holiday, vacation, and sick hours. These are non-productive and should not have overhead charges. In addition, the review also disclosed that the county is assessing 20% overhead to administrative activities.

The SCO's Accounting Standards and Procedures for Counties manual Chapter 9, Appendix A, section 11, outlines work types that should be maintained for expenditure cost centers.

Recommendation

The Department of Public Works should analyze and review the activity and project listings for FY 2011-12.

County's Response

The activity codes related to overhead charges on non-productive activities and administrative activities have been fixed to remove overhead charges to these categories.

**FINDING 3—
Cost center ledger
record error finding**

Our review of Administration Cost Center #300 shows that non-administration costs are charged to this cost center instead of to another appropriate cost center such as maintenance or non-road reimbursable projects.

The SCO's Accounting Standards and Procedures for Counties manual Chapter 9, Appendix A, section 25, outlines expenses that should be included in Administration Cost Center.

Recommendation

The Department of Public Works should analyze and correct the administration cost center subaccounts for FY 2011-12.

County's Response

Merced County continues to review this cost center to determine what costs are going in and move any inappropriate costs to the correct cost centers.

**FINDING 4—
Equipment rental
finding**

The Department of Public Works used Caltrans' equipment rental rates during FY 2009-10 instead of calculating them based on a 3-year average. Utilizing the Caltrans' rental rates caused overcharges to road and non-road projects during the FY 2009-10.

The SCO Manual, Chapter 9, Appendix A, section 17, prescribes the method used to calculate equipment rental rates.

Recommendation

The Department of Public Works should follow SCO guidelines to develop equipment rental rates for upcoming years.

County's Response

Merced County has corrected this by reviewing equipment rates and adjusting them to appropriate levels. This resulted in a reduction from a high variance of 73.44% down to just 1.14% at the Fiscal Year ending June 30, 2012.

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