



Transmitted via e-mail

May 2, 2014

Mr. Thomas Howard, Executive Director
State Water Resources Control Board
P.O. Box 100
Sacramento, CA 95812-0100

Dear Mr. Howard:

Final Report—City of Cathedral City, Proposition 13 Grant Audits

The Department of Finance, Office of State Audits and Evaluations, has completed its audits of the City of Cathedral City's (City) grants 04-055-557-1 and 04-056-557-1, issued by the State Water Resources Control Board.

The enclosed report is for your information and use. The City's response to the draft report observation and our evaluation of the response have been incorporated into this final report. The report will be placed on our website.

We appreciate the assistance and cooperation of the City. If you have any questions regarding this report, please contact Diana Antony, Manager, or Jon Chapple, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: Ms. Leslie Laudon, Manager, Division of Financial Assistance, State Water Resources Control Board
Ms. Jennifer Taylor, Budget Officer, State Water Resources Control Board
Ms. Kim Gossen, Fiscal Unit Manager, State Water Resources Control Board
Mr. Patrick Kemp, Assistant Secretary for Administration and Finance, California Natural Resources Agency
Ms. Julie Alvis, Deputy Assistant Secretary, California Natural Resources Agency
Mr. Bryan Cash, Deputy Assistant Secretary, California Natural Resources Agency
Mr. Kevin Biersack, Accounting Services Manager, City of Cathedral City
Ms. Tami Scott, Administrative Services Director, City of Cathedral City
Mr. William Bayne, Project Director, City of Cathedral City
Mr. Bill Simons, City Engineer, City of Cathedral City

AUDIT REPORT

City of Cathedral City Proposition 13 Bond Program Grant Agreements 04-055-557-1 and 04-056-557-1



City of Cathedral City, Cove Septic Elimination Project

Prepared By:
Office of State Audits and Evaluations
Department of Finance

MEMBERS OF THE TEAM

Diana Antony, CPA
Manager

Jon G. Chapple, CPA
Supervisor

Staff
Andrew J. Kortes
Terrance McDowell Jr.

Final reports are available on our website at <http://www.dof.ca.gov>

You can contact our office at:

Department of Finance
Office of State Audits and Evaluations
915 L Street, 6th Floor
Sacramento, CA 95814
(916) 322-2985

BACKGROUND, SCOPE AND METHODOLOGY

BACKGROUND

In March 2000, California voters approved the Safe Drinking Water, Clean Water, Watershed Protection, and Flood Protection Bond Act (Proposition 13). The \$1.97 billion of bond proceeds finance a variety of natural resource programs.

The City of Cathedral City (City) received two Proposition 13 grants to eliminate septic tanks in the Cove and Dream Homes neighborhood areas. Chapter 700, Statutes of 2001 (AB 358), prohibited the use of septic tanks in these areas as of January 1, 2012. The use of septic tanks for residential and commercial purposes in the community resulted in high concentrations of nitrates, total dissolved solids, bacteria, and viruses in the ground water supply within the upper levels of the Coachella Valley Groundwater Basin.

The State Water Resources Control Board (SWRCB) awarded the City the following grants:

- **Grant 04-055-557-7:** Dream Homes Septic Elimination Project Phase One. The \$848,300 grant was for the installation of a new sewer line resulting in approximately 126 septic tanks eliminated within the Dream Homes neighborhoods.
- **Grant 04-056-557-1:** Cove Septic Elimination Project Phase Two. The \$2.5 million grant was for the installation of a new sewer line resulting in approximately 400 septic tanks eliminated within the Cove area.

SCOPE

In accordance with the Department of Finance's bond oversight responsibilities, we audited grants 04-055-557-1 and 04-056-557-1 for the period July 1, 2004 through December 31, 2007.

The audit objectives were to determine whether the City's grant expenditures claimed were in compliance with applicable laws, regulations, and grant requirements; and to determine whether the grant deliverables were completed as required. We did not assess the efficiency or effectiveness of program operations.

The City's management is responsible for ensuring accurate financial reporting and compliance with applicable laws, regulations, and grant requirements. SWRCB and the California Natural Resources Agency are responsible for the state-level administration of the bond programs.

METHODOLOGY

To determine whether grant expenditures were in compliance with applicable laws, regulations, and the grant requirements; and if the grant deliverables were completed as required, we performed the following procedures:

- Interviewed key personnel to obtain an understanding of the grant-related internal controls.
- Examined the grant files, the grant agreements, and applicable policies and procedures.
- Reviewed the City's accounting records, vendor invoices, and payment requests.
- Selected a sample of expenditures to determine if costs were allowable, grant-related, incurred within the grant period, supported by accounting records, and properly recorded.
- Performed procedures to determine if other revenue sources were used to reimburse expenditures already reimbursed with grant funds.
- Conducted site visits to verify project existence.
- Evaluated whether a sample of grant deliverables required by the grant agreements were met.

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

The results of the audits are based on our review of documentation, other information made available to us, and interviews with staff directly responsible for administering grant funds.

Except as noted below, the grant expenditures claimed were in compliance with the requirements of the grant agreements and grant deliverables were completed as required. The Schedules of Claimed and Questioned Amounts are presented in Table 1.

Table 1: Schedules of Claimed and Questioned Amounts

Grant Agreement 04-055-557-1		
Task	Claimed	Questioned
Personnel Services	\$ 41,000	-
Operating Expenses	4,000	\$ 600
Professional and Consulting Services	266,000	133,000
Construction	537,300	-
Total Grant Costs	848,300	133,600
Match Funds ¹	149,700	-
Total Project Costs	\$ 998,000	\$ 133,600

Grant Agreement 04-056-557-1		
Task	Claimed	Questioned
Personnel Services	\$ 62,274	-
Operating Expenses	10,000	\$ 7,500
Travel	3,000	2,000
Professional and Consulting Services	414,726	282,208
Construction	2,010,000	-
Total Grant Costs	2,500,000	291,708
Match Funds ²	499,997	-
Total Project Costs	\$ 2,999,997	\$ 291,708

Observation 1: The City Did Not Maintain Records for Audit

The City did not maintain documentation to support \$133,600 and \$291,708 of costs for grant 04-055-557-1 and 04-056-557-1, respectively. The City followed its seven-year documentation retention policy. As a result, documentation to support the expenditure claims for periods prior to July 2005 were unavailable for audit.

¹ City significantly exceeded its budgeted match contributions but only claimed \$149,700.

² City significantly exceeded its budgeted match contributions but only claimed \$499,997.

Grant agreement, Exhibit C, section 4, requires the City to maintain records and supporting documentation for a minimum of 23 years after final payment.

Recommendations:

- A. SWRCB will determine the final disposition of the questioned costs and whether any amounts should be returned to the state or offset against other costs, including match contributions. As noted in the footnotes above, the City significantly exceeded its match contributions.
- B. The City should ensure staff is aware of specific grant requirements, especially those conflicting with standard City policies and procedures, so that records and supporting documentation are maintained in accordance with the grant agreements.



February 24, 2014

Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations
State of California, Department of Finance
915 L Street
Sacramento, CA 95814-3706

RE: Draft Audit Report – City of Cathedral City, Proposition 13 Grant Audits

Dear Mr. Sierra:

We are in receipt of the Department of Finance, Office of State Audits and Evaluations' draft audit report covering the City of Cathedral City's Proposition 13 Grants (04-055-557-1 and 04-056-557-1) for the period July 1, 2004 through December 31, 2007. This letter is the City's response to the observation and questioned costs included in that report.

We generally concur with the auditors' overall observation as to records prior to July 2005 not being available for audit as per the City's seven-year documentation retention policy. However, this overall observation applies only to vendor invoices and the related check copies. Journal entries for personnel services charged to each grant were available and provided to the auditors for the period prior to July 2005 when requested by them. Appropriate supporting documentation was attached to each journal entry. The auditors took no exception to personnel services costs claimed under either grant.

As to the questioned costs themselves, we do not agree with the specific dollar amounts questioned under each of the grants as discussed below.

Grant Agreement 04-055-557-1 (Questioned Costs - \$133,600) – Reimbursement requests were prepared by the City's contracted grants management consultant. During the entrance conference, it was explained to the auditors that the amounts included on each reimbursement request were based on percentage estimates of completion, not actual costs incurred during the period. At that time, we provided the auditors with a reconciliation worksheet that identified the actual costs attributable to the grant. The table on the following page identifies the amounts by category as per the final invoice submitted (claims based on estimates) and the City's reconciliation (actual costs incurred) provided to the auditors.

Grant Agreement 04-055-557-1	Claimed (As Reported on Invoices)	Claimed (As Reconciled by City Staff)
Personnel services	\$ 41,000	\$ 41,000
Operating expenses	4,000	1,159
Professional and consulting services	266,000	268,841
Construction	537,300	537,300
Total grant costs	\$ 848,300	\$ 848,300

The following table identifies the total costs questioned by the auditors and the revised total questioned costs based on the aforementioned reconciliation worksheet provided to the auditors. The auditors based their questioned costs total of \$133,600 on the estimated amounts included on the reimbursement requests through June 2005 (expenditures to date on Invoice No. 3). However, based on the reconciliation we provided to them at the time of audit as to the actual costs incurred, the amounts incurred prior to July 2005 were significantly less than the estimates reported. As such, we believe the questioned costs should have been \$89,814 based on the reconciled expenses.

Grant Agreement 04-055-557-1	Questioned (As Reported on Invoices)	Questioned (As Reconciled by City Staff)
Operating expenses	\$ 600	\$ 51
Professional and consulting services	133,000	89,763
Total grant costs	\$ 133,600	\$ 89,814

As to the questioned costs themselves, the professional and consulting services questioned costs (as reconciled) of \$89,763 were related to one vendor. Although individual invoices were not available for this vendor prior to July 2005, the first invoice paid subsequent to that period (payment with a July 26, 2005 check date) includes an "invoiced to date" amount of \$89,768 (see attached). The difference of \$5 (\$89,768 vs. \$89,763) is the result of this minor amount being charged to a funding source other than the grant being audited. Furthermore, subsequent to June 2005, total costs attributed to the grant for this same vendor were \$154,197, for which proper documentation was provided to the auditors. They took no exception to costs claimed subsequent to June 2005. We believe that although individual invoices for professional and consulting services for this vendor were not available prior to July 2005, the preponderance of evidence shows that the costs were incurred, paid, eligible, and allowable for grant purposes. Therefore, we believe questioned costs of \$89,763 should be accepted.

As to the questioned operating expenses of \$51 (as reconciled), we no longer have the documentation to support the delivery charges incurred.

Finally, as noted by the auditors in their audit report, the "City significantly exceeded its budgeted match contributions ..." Match funds totaled \$5.88 million compared to the \$149,700 required under the grant. As such, we believe the questioned costs, if any, that remain should be offset against these excess match funds.

Grant Agreement 04-056-557-1 (Questioned Costs - \$291,708) – Reimbursement requests were prepared by the City’s contracted grants management consultant. During the entrance conference, it was explained to the auditors that amounts included on each reimbursement request were prepared based on percentage estimates of completion, not actual costs incurred during the period. At their request, we provided them with worksheets related to personnel services, professional and consulting services, and construction costs that identified the actual costs attributable to the grant beginning July 1, 2005.

The following table identifies the total costs questioned by the auditors and the revised total questioned costs based on the aforementioned worksheets provided to the auditors. The auditors based their questioned costs total of \$291,708 on the estimated amounts included on the reimbursement requests through June 2005 (expenditures to date on Invoice No. 3). However, based on the categorical reconciliations we provided to the auditors at the time of audit as to the actual costs incurred, the amounts incurred prior to July 2005 were significantly less than the estimates reported. As such, we believe the questioned costs should have been \$137,607 based on the reconciled expenses.

Grant Agreement 04-056-557-1	Questioned (As Reported on Invoices)	Questioned (As Reconciled by City Staff)
Operating expenses	\$ 7,500	\$ 7,500
Travel	2,000	2,000
Professional and consulting services	282,208	128,107
Total grant costs	\$ 291,708	\$ 137,607

The reduction in questioned costs of \$154,101 (\$291,708 - \$137,607) was determined based on the difference between the estimated costs reported on Payment Request Nos. 4 through 7 and the actual costs incurred during those same time periods as shown in the table below.

Grant Agreement 04-056-557-1 Professional and Consulting Services	Actual Costs Incurred (Per Worksheet)	Costs Reported (As Reported on Invoices)	Additional Allowable Costs
Payment Request No. 4	\$ 61,570	\$ 40,000	\$ 21,570
Payment Request No. 5	67,711	40,000	27,711
Payment Request No. 6	114,327	32,800	81,527
Payment Request No. 7	43,011	19,718	23,293
Total costs – Request Nos. 4 - 7	\$ 286,619	\$ 132,518	\$ 154,101

The auditors were provided with the professional and consulting services worksheet totaling \$286,619. It was from this worksheet that they selected their sample items. Documentation was provided and they took no exception to costs incurred. Therefore, we believe questioned professional and consulting services costs of \$154,101 should be accepted since the costs were incurred, paid, eligible, and allowable for grant purposes.

Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations
February 24, 2014
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As to the revised questioned professional and consulting services of \$128,107 (as reconciled by the City), grant funds were spent on allowable project costs. The vendors for which these costs were incurred were the same vendors that incurred costs after June 2005. The auditors took no exception to costs claimed for these vendors for the periods subsequent to June 2005. We believe the costs were incurred, paid, eligible, and allowable for grant purposes. However, due to the multitude of funding sources involved in this project, any project-to-date amounts on invoices post-June 2005 would not be enough to substantiate the grant-specific charges. In addition, we no longer have the specific documentation to support the charges incurred based on the City's record retention policy.

As to the questioned operating expenses of \$7,500 and travel of \$2,000, we no longer have the documentation to support the charges incurred.

Finally, as noted by the auditors in their audit report, the "City significantly exceeded its budgeted match contributions ..." Match funds in excess of \$32.0 million were spent compared to the \$499,997 required under the grant. As such, we believe the questioned costs, if any, that remain should be offset against these excess match funds.

We appreciate the Department of Finance, Office of State Audits and Evaluations giving the City the opportunity to respond to the draft audit report. If you have any questions regarding the City's response, please contact me at (760) 770-0354.

Sincerely,

Original Signed By

Tami E. Scott
Administrative Services Director

EVALUATION OF RESPONSE

We reviewed the City of Cathedral City's (City) response dated February 24, 2014. Exhibits included in the response were reviewed but omitted from the final report for brevity. The City generally agreed with our observation that audit documentation was not available for periods prior to July 2005. Further, the City acknowledges reimbursement claims submitted through June 2005 reported estimated costs, and not actual project costs. The City contends a reconciliation of amounts reported prior to July 2005 shows actual project costs are significantly less than the reported estimated costs. Given this, the City argues, Finance should question costs based on the actual project costs (as determined in the City's reconciliation), and not the estimated project costs (which were reported for reimbursement to the State Water Resources Control Board (SWRCB)).

Our audit questioned all operating, travel, and professional/consulting service expenditures reported for reimbursement prior to July 2005, because the City was not able to provide documentation and/or accounting records to support the claimed expenditures. Our audit questioned costs actually reported to SWRCB, and for which the City received reimbursement, regardless of whether the costs were estimated or actual. Any reconciliation of project expenditures, for which the City claimed reimbursement and received payment, should be addressed directly with SWRCB.

Because we did not receive adequate supporting documentation relating to the periods prior to July 2005, our recommendation that SWRCB should determine the final disposition of the questioned costs remains unchanged.