

CITY OF PALO ALTO

Audit Report

SPECIAL GAS TAX STREET IMPROVEMENT FUND

July 1, 2007, through June 30, 2013

TRAFFIC CONGESTION RELIEF FUND ALLOCATIONS

July 1, 2005, through June 30, 2011

PROPOSITION 1B FUND ALLOCATIONS

July 1, 2007, through June 30, 2013



BETTY T. YEE
California State Controller

April 2016



BETTY T. YEE
California State Controller

April 18, 2016

The Honorable Patrick Burt
Mayor of the City of Palo Alto
250 Hamilton Avenue
Palo Alto, CA 94301

Dear Mayor Burt:

The State Controller's Office audited the City of Palo Alto's Special Gas Tax Street Improvement Fund for the period of July 1, 2007, through June 30, 2013. The audit should have included all years subsequent to the prior audit, which covered through June 30, 2003; however, we were unable to review the records for the period of July 1, 2003, through June 30, 2007, because these records were not available due to the City's seven-year record retention policy. We also audited the Traffic Congestion Relief Fund (TCRF) allocations, recorded in the Capital Improvement Fund, for the period of July 1, 2005, through June 30, 2011, and the Proposition 1B Fund allocations, recorded in the Capital Improvement Fund, for the period of July 1, 2007, through June 30, 2013.

Our audit found that although the city accounted for and expended its Special Gas Tax Street Improvement Fund, TCRF allocations, and Proposition 1B Fund allocations in compliance with requirements, the city understated the fund balance in the Special Gas Tax Street Improvement Fund by \$994,217 as of June 30, 2013, because it transferred the amount to another fund with the intent of using it for street-related expenditures, but the funds were never spent.

If you have any questions, please contact Christopher Lek, Interim Chief, Local Government Audits Bureau, at (916) 284-0120.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/rg

cc: Lalo Perez, Chief Financial Officer
City of Palo Alto

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Audit Report

Summary

The State Controller's Office (SCO) audited the City of Palo Alto's:

- Special Gas Tax Street Improvement Fund for the period of July 1, 2007, through June 30, 2013. The audit should have included all years subsequent to the prior audit, which covered through June 30, 2003; however, we were unable to review the records for the period of July 1, 2003, through June 30, 2007, because these records were not available due to the City's seven-year record retention policy.
- Traffic Congestion Relief Fund (TCRF) allocations recorded in the Capital Improvement Fund, for the period of July 1, 2005, through June 30, 2011.
- Proposition 1B Fund allocations recorded in the Capital Improvement Fund, for the period of July 1, 2007, through June 30, 2013.

Our audit found that although the city accounted for and expended its Special Gas Tax Street Improvement Fund, TCRF allocations, and Proposition 1B Fund allocations in compliance with requirements, the city understated the fund balance in the Special Gas Tax Street Improvement Fund by \$994,217 as of June 30, 2013, because it transferred the amount to another fund with the intent of using it for street-related expenditures, but the funds were never spent.

Background

The State apportions funds monthly from the Highway Users Tax Account in the Transportation Tax Fund to cities 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 Article XIX of the California Constitution and Streets and Highways Code section 2101, a city must deposit all apportionments of highway users taxes in its Special Gas Tax Street Improvement Fund. A city must expend gas tax funds only for street-related purposes. We conducted our audit of the city's Special Gas Tax Street Improvement Fund under the authority of Government Code section 12410.

Chapter 91, Statutes of 2000, (Assembly Bill 2928) as amended by Chapter 636, Statutes of 2000, (Senate Bill 1662) and Government Code section 14556.5, created a Traffic Congestion Relief Fund in the State Treasury for allocating funds quarterly to cities and counties for street or road maintenance, reconstruction, and storm damage repair. Cities must deposit funds received into the city account designated for the receipt of State funds allocated for transportation purposes. The city recorded its TCRF allocations in the Capital Improvement Fund. We conducted our audit of the city's TCRF allocations under the authority of Revenue and Taxation Code section 7104.

Senate Bill 1266, Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, was introduced as Proposition 1B and approved by the voters on November 7, 2006, for a variety of transportation priorities, including the maintenance and improvement of local transportation facilities. Proposition 1B funds transferred to cities and counties shall be deposited into an account that is designated for the receipt of State funds allocated for streets and roads. The city recorded its Proposition 1B Fund allocations in the Capital Improvement Fund. A city also is required to expend its allocations within four years following the end of the fiscal year in which the allocation was made and to expend the funds in compliance with Government Code section 8879.23. We conducted our audit of the city's Proposition 1B allocations 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, TCRF allocations, and Proposition 1B Fund allocations in compliance with Article XIX of the California Constitution, the Streets and Highways Code, Revenue and Taxation Code section 7104, and Government Code section 8879.23.

To meet the audit objective, we performed the following procedures:

Special Gas Tax Street Improvement Fund

- Reconciled the fund revenue recorded in the city ledger to the balance reported in the SCO's apportionment schedule to determine whether Highway Users Tax Account (HUTA) funds received by the city were completely accounted for in the Gas Tax Fund.
- Judgmentally selected sample expenditure transactions and verified proper documentation and eligibility to determine whether HUTA funds were expended in accordance with the criteria above.
- Analyzed and tested sample transactions to determine whether recoveries of prior HUTA fund expenditures were identified and credited to the Special Gas Tax Street Improvement Fund.
- Reviewed the fund cash and liabilities accounts for unauthorized borrowing to determine whether unexpended HUTA funds were available for future street-related expenditures.
- Interviewed city employees and reviewed policies and procedures to gain an understanding of the city's internal controls and accounting systems related to this engagement.

Traffic Congestion Relief Fund (TCRF) Allocations

- Reconciled the TCRF revenue recorded in the city ledger to confirm that the TCRF allocations received by the city agreed with the SCO's apportionment schedule.

- Judgmentally selected sample expenditure transactions and verified proper documentation and eligibility to determine the city's compliance with the criteria above.
- Reconciled the City's "Schedule of Expenditures as Reported in the Streets and Roads Annual Report" with the SCO's "Average Annual Expenditures Computation of Discretionary Funds" to determine compliance with the maintenance-of-effort (MOE) requirement.

Proposition 1B Fund Allocations

- Reconciled the Proposition 1B revenue recorded in the city ledger to confirm that the Proposition 1B allocations received by the city agreed with the SCO's apportionment schedule.
- Judgmentally selected sample expenditure transactions and verified proper documentation and eligibility to determine the city's compliance with the criteria above.

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 city's financial statements. We limited our audit scope to planning and performing the audit procedures necessary to obtain reasonable assurance that the city accounted for and expended its Special Gas Tax Street Improvement Fund, TCRF allocations, and Proposition 1B Fund allocations in accordance with the requirements of the Streets and Highways Code, Revenue and Taxation Code section 7104, and Government Code section 8879.23. Accordingly, we examined transactions, on a test basis, to determine whether the city expended funds for street purposes. We considered the city's internal controls only to the extent necessary to plan the audit.

Conclusion

Our audit found that the City of Palo Alto 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 for the period of July 1, 2007, through June 30, 2013, except as noted in Schedule 1 and described in the Finding and Recommendation section of this report. The finding required an adjustment of \$994,217 to the city's accounting records.
- TCRF allocations recorded in the Capital Improvement Fund in compliance with Article XIX of the California Constitution, the Streets and Highways Code, and Revenue and Taxation Code section 7104 for the period of July 1, 2005, through June 30, 2011.

- Proposition 1B Fund allocations recorded in the Capital Improvement Fund in compliance with Government Code section 8879.23 for the period of July 1, 2007, through June 30, 2013.

Follow-Up on Prior Audit Findings

Our prior audit report, issued on April 21, 2004, disclosed no findings.

Views of Responsible Officials

We issued a draft audit report on November 24, 2015. David Ramberg, Assistant Director, Administrative Services Department, responded by letter dated January 7, 2016, requesting language clarification. The SCO has clarified the report accordingly. The city's response is included in this final audit report as an attachment.

Restricted Use

This report is intended for the information and use of the City of Palo Alto's management 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, CPA
Chief, Division of Audits

April 18, 2016

**Schedule 1—
Reconciliation of Fund Balance
July 1, 2012, through June 30, 2013**

	Special Gas Tax Street Improvement Fund <u>Highway Users Tax Allocations</u> ^{1,2,3}
Beginning fund balance per city	\$1,060,734
Revenues	<u>1,465,896</u>
Total funds available	2,526,630
Expenditures	<u>(1,942,490)</u>
Ending fund balance per city	<u>584,140</u>
SCO adjustment: ⁴	
Finding—Ineligible expenditures	<u>994,217</u>
Ending fund balance per audit	<u><u>\$1,578,357</u></u>

¹ The city receives apportionments from the State Highway Users Tax Account, 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. The audit period was July 1, 2007, through June 30, 2013; however, this schedule includes only the period of July 1, 2012, through June 30, 2013.

² Government Code section 14556.5 created a Traffic Congestion Relief Fund (TCRF) in the State Treasury for allocating funds quarterly to cities and counties for street and road maintenance, reconstruction, and storm damage repair. The TCRF allocations were recorded in the Capital Improvement Fund. The audit period was July 1, 2005, through June 30, 2011. The city did not receive any TCRF revenues and did not incur any TCRF expenditures during FY 2012-13; therefore, it is not included in this schedule.

³ Senate Bill 1266, Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, introduced as Proposition 1B, provided funds for a variety of transportation priorities. The audit period was July 1, 2007, through June 30, 2013. The city did not receive any Proposition 1B revenues and did not incur any Proposition 1B expenditures during FY 2012-13; therefore, it is not included in this schedule.

⁴ See the Finding and Recommendation section.

Finding and Recommendation

**FINDING—
Ineligible expenditures**

During fiscal year 2008-09, the city transferred out \$994,217 from the Special Gas Tax Street Improvement Fund to the Stanford Research Park Fund, with the intent of using the funds for street-related expenditures. However, the funds were never spent.

Streets and Highways Code section 2101 specifies that the Highway Users Tax apportionments are to be expended only for the construction, maintenance, and operation of public streets and roads and related administrative costs.

As a result, the transfer of \$994,217 is unallowable.

Recommendation

The city should return \$994,217 into the Special Gas Tax Street Improvement Fund. In addition, the city should establish procedures to ensure that all costs charged to the Special Gas Tax Street Improvement Fund are for street-related projects and are properly documented.

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



ADMINISTRATIVE SERVICES

250 Hamilton Avenue, 4th Floor
Palo Alto, CA 94301
650.329.2692

Mike Spalj
Chief, Local Government Audits Bureau
State Controller's Office, Division of Audits
Post Office Box 942850
Sacramento, CA 94250-5874

January 7, 2016

Dear Mr. Spalj:

The City of Palo Alto Administrative Services Department received the State Controller's Office draft audit of the City of Palo Alto's Special Gas Tax Street Improvement Fund for the period of July 1, 2007, through June 30, 2013. We have reviewed the audit and have the following requests, respectfully:

- 1) Page 1 Summary – "...because these records were not available." I request the addition of "due to the City's 7-year record retention policy."
- 2) Page 1 Summary – "...used the gas tax revenues for non-street-related expenditures." I request that this read "transferred the amount to another fund with the intent of using it for street-related expenditures, but the funds were never spent."
- 3) Page 6 Finding – same comment as above.

I would be happy to discuss these if you have any questions. Thank you for the opportunity to provide feedback on the draft audit

Thank you.

A handwritten signature in blue ink, appearing to read "David Ramberg".

David Ramberg
Assistant Director, Administrative Services Department

Cc: Lalo Perez, Director Administrative Services/CFO



CityOfPaloAlto.org

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