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Controller Releases Stockton Audits

SACRAMENTO – State Controller John Chiang today released a series of audits focusing on the City of Stockton. The Controller found significant weaknesses in the City's [fiscal management practices and internal controls](#) which, if left unaddressed, will continue to invite wasteful spending and abuse of public resources. The audits also found that the City misused cash in its [gas tax fund](#), and is unlawfully holding former [redevelopment agency \(RDA\) assets](#).

"Stockton is not Bell – we found no evidence that corruption and self-dealing drove this city into insolvency," said Chiang. "Instead, many of Stockton's problems can be tracked to poor decision-making that was not only ill-informed by weak accounting and fiscal management systems, but failed to heed downward-trending data that should have curbed spending and borrowing decisions."

The Controller initiated the audits after receiving multiple requests from officials and Stockton residents seeking an independent review of the City's accounting practices. Findings and observations in the three audits include the following:

- 1 Civic leaders should have revisited their spending and borrowing decisions – or mitigated the risks associated with them – by taking information about revenue and expenditure trends, housing contractions, and other readily-available data into account earlier than they did.
- 1 Serious weaknesses exist in most aspects of the City of Stockton's administrative and internal accounting control system. Of the 79 general accounting controls reviewed, 48 -- or 60.8% -- were found inadequate.
- 1 Most of the City Auditor's Office planned audit activities were not carried out and few audit reports were issued. Moreover, the Controller's Office found few, if any, of the reports that were released address issues of substance.
- 1 The City is unlawfully holding \$1,361,531 in RDA assets. After the dissolution of RDAs, the former agencies' assets were to be transferred to "successor" agencies. The successor agencies would then use those assets to retire RDA debt. At the dissolution of Stockton's RDA, the City inappropriately transferred assets from the RDA to the City, instead of the successor agency.
- 1 The City has not produced required financial statements and financial transaction reports in a timely manner, such as the City's Financial Transactions report, which was delivered to the State 19 months late. The failure to develop timely, accurate financial reports can result in unnecessary expenses and delay other reviews. This series of audits, for example, experienced numerous delays because of Stockton's failure to report financial information in a timely manner.
- 1 Of the financial reports that the City did produce on time, many included several discrepancies that raise questions regarding their reliability. Without good accounting and reporting standards in place, the lack of transparency invites fraud, waste, and ill-informed spending decisions.
- 1 The City's commingling of taxpayer dollars resulted in the cash impairment of some funds. The City's gas tax fund, for example, was impaired by commingling its resources with other City funds. Also, the operating costs of the General Fund were paid for by funds from the City's investment pool, without regard for the source of funds, again resulting in cash impairment.
- 1 The City Council and leadership staff have failed to properly manage contract awards, oversight, and payment, and competitive bidding requirements have not been followed regularly.
- 1 The City has a decentralized fiscal management system that, without adequate oversight and internal controls, can result in abuse or misuse of public funds. Many of the findings identified in the Controller's audits were caused by poor oversight over the decentralized system.
- 1 This poor management structure led to an estimated loss of \$8.6 million in State and Federal grants. This was caused by City departments failing to include proper cost estimates in their proposals, and invalid explanations of estimated costs.
- 1 The City may have violated its own policy when issuing bonds.

"I recognize the all too clear challenges facing the City of Stockton," said Chiang. "The purpose of these audits is to shine a light on serious, but solvable, problems that must be addressed by City leadership in order for Stockton to restore its financial integrity."

The Controller's reports now require the City to immediately separate its gas tax dollars from other accounts, and to establish a separate bank account for its gas tax fund. The City must provide the State Controller's Office with proof that a separate bank account has been established, and that bank account shall remain open until the City provides evidence that it has restored the financial health of the General Fund.

The City must also reverse the transfer of \$1,361,531 in redevelopment assets by sending those assets to the Stockton RDA's successor agency. The successor agency can then use those dollars to retire debt absorbed by the dissolved RDA.

The Controller further calls upon the City to develop a comprehensive plan to address the internal control deficiencies identified in his report, in order to reduce or prevent further threat to the City's financial situation.

Read the [Controller's correspondence](#) with the City at the conclusion of the audits.

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