



May 5, 2025

To: Executive Committee

From: Darrell E. Johnson, Chief Executive Officer

Subject: Measure M2 Eligibility for the City of Huntington Beach

Overview

The Orange County Transportation Authority's Internal Auditor issued results of an independent auditor's report on applying agreed-upon procedures related to the City of Huntington Beach's compliance with the Measure M2 requirements for fiscal year 2023-24. The independent auditor's report found that the City of Huntington Beach had used Measure M2 Local Fair Share funds for expenses that were deemed unallowable per the Measure M2 Ordinance No. 3. Based on this information, recommendations to address the independent auditor's report and findings are presented.

Recommendations

- A. Seek reimbursement of \$29,249 from the City of Huntington Beach and find the City of Huntington Beach ineligible to receive Measure M2 net revenues for five years pursuant to Section 10.4 of Ordinance No. 3.
- B. Authorize the Internal Auditor to engage independent auditor services to apply agreed-upon procedures to review the City of Huntington Beach's Measure M2 Local Fair Share program and other expenditures for fiscal year 2024-25, fiscal year 2025-26, fiscal year 2026-27, fiscal year 2027-28, and fiscal year 2028-29, to enable the City of Huntington Beach to reestablish eligibility and authorize staff to deduct the review costs from any future net Measure M2 payments to the City of Huntington Beach.
- C. Authorize the Chief Executive Officer to negotiate and execute an agreement with the City of Huntington Beach to formalize the required actions to reestablish eligibility and other terms.

Background

In July 2006, the Orange County Transportation Authority (OCTA) Board of Directors (Board) approved and adopted the Renewed Measure M (M2) Ordinance No. 3 (M2 Ordinance). The M2 Ordinance became effective on November 8, 2006, after voters approved the one-half cent sales tax for transportation improvements. OCTA is designated as responsible for administering M2 and ensuring that OCTA's commitment to voters is followed, including numerous specific requirements, safeguards, and transparency provisions.

The M2 Ordinance requires local jurisdictions to annually submit an expenditure report that details all M2 net revenues, interest earned, expenditures, and expenditures of earned interest. Local jurisdictions' expenditure reports are signed by their respective Finance Director, adopted by the City Council/Board of Supervisors, and submitted to OCTA within six months of the local jurisdiction's fiscal year (FY) end.

Annually, the Audit Subcommittee (Subcommittee) of the Taxpayer Oversight Committee selects specific local jurisdictions for application of agreed-upon procedures (AUP) by OCTA's independent auditing firm. The AUP includes testing of expenditures for compliance with program requirements, review of indirect costs for adequate support and reasonableness, testing to ensure allocation of interest, and testing of the annual expenditure reports for accuracy. The independent auditing firm's report helps determine local jurisdictions' level of compliance with certain M2 Ordinance provisions.

For FY 2023-24, one of the local jurisdictions selected by the Subcommittee for review of the M2 Local Fair Share (LFS) program funding was the City of Huntington Beach (City). Crowe, LLP (Crowe), OCTA's independent auditing firm, conducted interviews of City finance and program-related staff, and applied the AUP. The results of the effort were presented to the Finance and Administration Committee on April 23, 2025, and to the Board on April 28, 2025. Crowe reported one notable finding: the City reported LFS expenditures of \$29,249 that were not allowable per the M2 Ordinance. The City acknowledged the error and indicated that they have made a journal entry to refund the unallowed LFS amount. However, this does not satisfy the Measure M2 Ordinance provision that the funds must be repaid to OCTA.

OCTA continues to provide reminders and guidance through guidelines, eligibility workshops, individual meetings and annual M2 Finance Director Workshops. Despite these efforts, this is the second time that a city has had an AUP report finding that LFS expenditures were not allowable.

Discussion

Continued investment in Orange County's transportation improvements is the cornerstone of M2. The M2 LFS program provides 18 percent of M2 net revenues to eligible local jurisdictions for use on allowable transportation planning and implementation activities. OCTA, as the M2 administrator, is accountable to the taxpayers on the uses of M2 revenues.

Crowe's AUP report, along with the City's response, is included as Attachment A; specifically, the finding pertains to Procedure 8. The City erroneously applied payroll charges of \$29,249 to LFS for an employee who does not work in transportation; therefore, the use of LFS for this purpose is deemed unallowable, per the M2 Ordinance.

The M2 Ordinance includes specific language to address safeguards related to the unauthorized use of M2 net revenues. Section 10.4 of the M2 Ordinance (Attachment B) states:

“No Net Revenues shall be used by a jurisdiction for other than transportation purposes authorized by the Ordinance. Any jurisdiction which violates this provision must fully reimburse the Authority for the Net Revenues misspent and shall be deemed ineligible to receive Net Revenues for a period of five (5) years.”

The expenditures identified in Crowe's findings are not authorized by the M2 Ordinance. OCTA staff has carefully reviewed, considered, and consulted with legal counsel on how to address this matter. To ensure OCTA maintains compliance with the M2 Ordinance and continues to uphold public trust, staff recommends the Board adhere to the provisions of Section 10.4 of the M2 Ordinance by:

- Seeking reimbursement from the City for the disallowed expenditures in the amount of \$29,249 (to be paid to OCTA by June 30, 2025) and,
- Finding the City ineligible to receive M2 net revenues for a period of five years, which would also exclude the City from participating in M2 competitive programs.

When the City is found ineligible, OCTA cannot remit M2 net revenues to the City. For previous M2 ineligibility findings involving other jurisdictions, the Board has suspended payments and held funds in reserve for that local jurisdiction. If the Board chooses to hold funds in reserve, the LFS and Senior Mobility Program funds will be withheld within the source programs and would only be released to the City once it has reestablished eligibility and demonstrated it was fulfilling M2

eligibility requirements throughout the five-year ineligibility period. This can be verified through future AUP reviews of FY 2024-25, FY 2025-26, FY 2026-27, FY 2027-28, and FY 2028-29 expenditures. Costs incurred for these reviews are to be paid for by the City through a reduction in future M2 net revenues.

During the period of ineligibility, M2 net revenues the City has received to date can still be utilized. If requested, the City may be allowed to incur M2-eligible expenditures, at risk, and be able to apply the expense to future M2 net revenues. Should the City be approved for this option, these expenditures must be clearly identified in accounting records and included in annual M2 expenditure report submittals.

Pending Board action on this item, OCTA will work with the City to enter into an agreement that details the specific requirements and time frames for submittals to support the re-establishment of the City's eligibility. OCTA is committed to delivering the M2 promises made to voters and does not take this responsibility lightly. This includes adhering to the safeguards in the M2 Ordinance, which ensures transparency and accountability of taxpayer dollars.

Summary

A recent report conducted by an independent auditing firm disallowed LFS expenditures that were reported in the City's FY 2023-24 M2 Expenditure Report. The M2 Ordinance has specific language related to funds used for unauthorized purposes. Recommendations to address Crowe's report findings are presented for Board consideration and approval.

Attachments

- A. Crowe LLP, Independent Accountants' Report on Applying Agreed-Upon Procedures, City of Huntington Beach
- B. Orange County Local Transportation Authority Ordinance No. 3, Safeguards of Use of Revenues Excerpt, Pages 5-6

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