




May 6, 2019

To: Executive Committee
From: Darrell E. Johnson, Chief Executive Officer 
Subject: Measure M2 Eligibility for the City of Santa Ana

Overview

The Orange County Transportation Authority's Internal Auditor recently prepared an audit of the City of Santa Ana for fiscal year 2017-18. The audit concluded that the City of Santa Ana did not expend sufficient discretionary funds on streets and road purposes to meet the Measure M2 Ordinance maintenance of effort requirement. Based on this information, recommendations are presented related to compliance with the Measure M2 Ordinance.

Recommendations

- A. Find the City of Santa Ana ineligible to receive net Measure M2 revenues.
- B. Suspend payments to the City of Santa Ana of net Measure M2 revenues until the City of Santa Ana can demonstrate compliance with Measure M2 eligibility requirements and the Board of Directors acts to find the City of Santa Ana an "eligible agency."
- C. Authorize the Chief Executive Officer to execute Amendment No. 5 to Contract No. C-5-3564 with Vavrinek, Trine, Day and Company, LLP to revise the scope of work, add an additional task to apply agreed-upon procedures to assess compliance with maintenance of effort expenditure requirements, extend the agreement through June 30, 2020, and authorize staff to deduct fiscal year 2018-19 audit costs from any future net Measure M2 payments to the City of Santa Ana.
- D. Increase the City of Santa Ana's maintenance of effort requirement for fiscal year 2018-19 by the amount of expenditures that were not met as identified in the fiscal year 2017-18 audit.
- E. Authorize the Chief Executive Officer to negotiate and execute a settlement agreement with the City of Santa Ana to correct and remedy the fiscal year 2017-18 audit issues.

Background

The Measure M2 (M2) Ordinance outlines eligibility requirements that each local agency must continually satisfy to receive net revenues from the M2 Program, including local fair share, the Senior Mobility Program, and awards through competitive programs. One of the requirements is that a local agency must continue to invest a certain level of discretionary revenues, such as general funds that support street and road activities, to be deemed eligible for any M2 funding. This requirement is rooted in the California Public Utilities Code (PUC) 180001 that enables local transportation authorities to seek voter approval for sales tax measures. The PUC states the intent of the legislature is that funds generated through a sales tax ordinance “shall supplement existing local revenues used for public transportation purposes and that local governments maintain their existing commitment of local funds for transportation purposes” (PUC 180200).

In the eligibility process, this requirement is referred to as the maintenance of effort (MOE) requirement and was also included in the original Measure M Program. Each jurisdiction is required to maintain a minimum level of local streets and roads discretionary expenditures. The minimum level was based on the average of general fund expenditures for local street maintenance and construction over the period of fiscal year (FY) 1985-86 through FY 1989-90. M2 used a similar benchmark and requires the amount to be adjusted for inflation every three years commensurate with overall growth of the local agency’s general fund revenues.

The local agency demonstrates its commitment to comply with the required MOE through budgeting the appropriate level of discretionary funding as part of the local agency budget process and providing the Orange County Transportation Authority (OCTA) with an expenditure report to validate the commitment at the end of the budget year.

In the 29 years of combined experience of administering the original Measure M and now M2 programs, OCTA has never had an instance in which it had to find a local jurisdiction ineligible to receive net Measure M revenues due to failure to meet the MOE requirement.

The OCTA Board of Directors (Board) makes a determination of eligibility annually based on the information that is provided by each jurisdiction and with support from the Taxpayer Oversight Committee (TOC), which is also charged with reviewing certain submittals. Following the annual eligibility cycle, the TOC directs the internal auditor to carry out audits to confirm that funds have been spent in accordance with the M2 Ordinance and that each jurisdiction had sufficient expenditures to meet the previously self-certified MOE requirement.

Every year, OCTA's Finance and Administration, Internal Audit, and Planning staff, as well as the TOC, have cautioned local agencies that budgeting at or just above the required MOE amount may put the agency's M2 funds at risk if they end up not meeting the requirement due to disallowed costs.

At the direction of the TOC, the OCTA Internal Auditor prepared an audit that was presented to the Board on April 8, 2019, which indicated that the City of Santa Ana (City) did not have sufficient expenditures for FY 2017-18 to meet its MOE requirement (Attachment A). This will impact the City's eligibility determination and the disbursement of net Measure M revenues to the City. It should be noted that the City has provided a response to the audit that is also included in Attachment A.

Discussion

In June 2017, the City provided the required MOE certification that stated it budgeted sufficient expenditures for FY 2017-18, consistent with the following requirement:

“The Authority shall not allocate any net revenues to any jurisdiction for any fiscal year until that jurisdiction has certified to the Authority that it has included in its budget for that fiscal year an amount of local discretionary funds for streets and roads purposes, at least equal to the level of its maintenance of effort requirement.”

The City met this MOE requirement based on the submittal and self-certification. The next submittal required from the City related to MOE and eligibility was the expenditure report, which was submitted to OCTA on November 29, 2018, and was formally approved by the City Council through a resolution on December 18, 2018. The City was required to spend \$7,755,107 using discretionary revenues toward streets and roads-related costs. According to the expenditure plan that was submitted, the City spent \$8,207,411 to meet this requirement.

However, the audit could not verify the indirect cost methodology for ten transactions, totaling \$715,626, to confirm that those costs are eligible MOE expenditures. The City, in its response to the audit, agreed that it could not produce the original allocation methodology that is being applied and has indicated it will engage a third party to implement updated internal service charges. After deducting these unverifiable expenditures, the City did not meet the MOE requirement for FY 2017-18. The City responded that it has graffiti abatement charges, which were not submitted toward the MOE requirement, and believes they would be eligible to meet the MOE obligation. On April 15, 2019, staff met with the City to review the City's audit response, as well as any potential follow-up items. Based on the discussion at the meeting, staff believes the audit findings should remain unchanged.

Under this circumstance, the following M2 Ordinance requirement applies:

“A determination of non-eligibility of a jurisdiction shall be made only after a hearing has been conducted and a determination has been made by the Authority’s Board of Directors that the jurisdiction is not an eligible jurisdiction.”

Because the audit determined that the City did not provide sufficient verifiable expenditures in its expenditure report to meet the MOE requirement, and in order to be consistent with the requirements of the M2 Ordinance and comply with the intent of the authorizing state statute, it is recommended that the Board find the City ineligible to receive Measure M revenues. Specific recommendations include:

- Find the City ineligible to receive net M2 revenues;
- Suspend payments to the City of net M2 revenues;
- Deduct FY 2018-19 audit costs from any future net M2 payments to the City;
- Increase the City’s MOE requirement for FY 2018-19 by the amount that the City fell short in meeting the required MOE for FY 2017-18, as identified in the FY 2017-18 audit; and
- Execute a settlement agreement with the City to correct and remedy the audit issues.

Based on these recommendations, net M2 payments would be suspended until such time that the City has re-established eligibility. These funds will be held in reserve for the City. The City will be required to demonstrate through a future OCTA audit of financial reports, (the audit would be paid for by the City), that it has met the MOE required for FY 2018-19, plus made up for the underrun in MOE expenditures from FY 2017-18. As the M2 Ordinance and eligibility guidelines do not include precise terms and conditions related to re-establishing eligibility, OCTA would execute an agreement with the City that further details specific requirements and timeframes.

Summary

A recent audit indicated that the City of Santa Ana did not meet Measure M2 eligibility requirements. Recommendations are presented in response to the audit, consistent with the intent of the Measure M2 Ordinance.

Attachment

- A. Vavrinek, Trine, Day & Co., LLP, Certified Public Accounts, Independent Accountants' Report on Applying Agreed-Upon Procedures - City of Santa Ana

Prepared by:



Adriann Cardoso
Department Manager,
Capital Programming
(714) 560-5915

Approved by:



Kia Mortazavi
Executive Director, Planning
(714) 560-5741