



**May 6, 2024**

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

### **Overview**

In 2023, the Orange County Transportation Authority Board of Directors found the City of Cypress ineligible to receive Measure M2 net revenues due to an insufficient investment of discretionary funds in fiscal year 2021-22 for streets and roads purposes to meet the Measure M2 maintenance of effort requirement. A recent accounting of the City of Cypress' Measure M2 maintenance of effort expenditures for fiscal year 2022-23 found that the City of Cypress has met its minimum maintenance of effort expenditure requirement, including the shortfall amount. The Orange County Transportation Authority Board of Directors is being asked to consider reinstating the City of Cypress' Measure M2 eligibility status.

### **Recommendations**

- A. Authorize the Chief Executive Officer to negotiate, execute, and amend the settlement agreement with the City of Cypress to reduce the term to deliver the maintenance of effort requirement to one year and remove an audit requirement for fiscal year 2023-24.
- B. Approve the City of Cypress eligible to receive Measure M2 net revenues upon execution of the amended settlement agreement.
- C. Direct staff to reinitiate payments to the City of Cypress for Measure M2 net revenues, which were held during its period of ineligibility (less fiscal year 2022-23 audit costs) within ten days of execution of the amended settlement agreement.

### **Background**

The Measure M2 (M2) Ordinance outlines eligibility requirements that each local jurisdiction must continually satisfy to receive net revenues from the M2 Program. One of the requirements is that a local jurisdiction 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). This requirement is referred to as maintenance of effort (MOE).

In June 2021, the City of Cypress (City) provided MOE certification to the Orange County Transportation Authority (OCTA) as part of its M2 eligibility verification package submittal. The certification stated that the City had budgeted sufficient expenditures for fiscal year (FY) 2021-22, 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.”

Per M2 MOE requirements, the City was required to spend \$3,607,878 using discretionary revenues toward streets and roads-related costs. According to the expenditure report for FY 2021-22 that was approved by the city council and submitted to OCTA, the City spent \$3,892,903 toward the MOE requirement. However, an independent review of the City’s expenditures, through the annual eligibility process conducted in coordination with the TOC and Internal Audit, identified ineligible direct charges and found that indirect costs allocated to MOE could not be verified based on a reasonable methodology. After the removal of ineligible direct costs and unsupported indirect costs, the City did not meet the MOE requirement for FY 2021-22. Consistent with M2 Ordinance requirements, on May 22, 2023, the OCTA Board of Directors (Board) found the City ineligible to receive M2 net revenues. As part of that action, the OCTA Board specified that the following actions be completed by OCTA staff in conjunction with the finding of ineligibility.

- Suspend payments to the City of net M2 revenues;
- Deduct audit costs related to this eligibility finding from any future net M2 payments to the City;
- Require the City to demonstrate supplemental investment of discretionary transportation funds equal to the amount of discretionary investment that was short of the MOE benchmark in FY 2021-22 (approximately \$1.38 million) as a condition of accessing suspended funds upon being found an eligible jurisdiction, and

- Authorize the Chief Executive Officer to negotiate and execute an agreement with the City outlining the process to re-establish eligibility.

***Discussion***

Throughout fall 2023 and early 2024, OCTA worked with City staff to implement and address the required actions. An independent accounting firm, BCA Watson Rice, LLP (auditors), applied agreed-upon procedures (AUP) to the City's M2 MOE-related expenditures for FY 2022-23 to determine whether the City had met its obligation under the settlement agreement. The auditors reported that, based on the AUP, the City had incurred expenditures sufficient to meet its obligations under the settlement agreement, which included the City's MOE requirement plus the shortfall amount in MOE expenditures identified in FY 2021-22. These findings were presented to the Finance and Administration Committee on April 24, 2024, and will be presented to the Board on May 13, 2024.

**Other Eligibility Requirements**

M2 includes 13 eligibility requirements that all 35 local agencies are required to comply with in order to receive M2 net revenues and agencies must submit required documents by June 30. The City submitted all required M2 eligibility verification documents prior to June 30, 2023.

These documents were received and reviewed by OCTA staff, the Taxpayer Oversight Committee's (TOC) Annual Eligibility Review Subcommittee, and the full TOC. In February 2024, M2 eligibility findings for FY 2023-24 were advanced to the OCTA Regional Transportation Planning Committee and Board for consideration and approval. However, due to the City's ineligibility, the Board elected to only receive and file the City's M2 eligibility verification documents until the resolution of the prior year's MOE shortcomings had been remedied.

Based on the results of the AUP of the City's MOE expenditures for FY 2022-23, the City has met its obligation under the settlement agreement, and it is recommended that the City now be found eligible again to receive M2 net revenues and the suspended M2 funds that were being held in reserve during the period of the City's ineligibility (less the FY 2022-23 AUP costs). These actions, if approved by the Board, would conclude the City's period of M2 ineligibility and would also place the City back on an eligibility review cycle consistent with all other eligible Orange County local agencies.

**Amendment to the Agreement**

At the time the settlement agreement was executed, the City indicated that they may need more than one year to make up for the MOE underrun. The settlement agreement was structured to respond to this possibility and provides the City two years to deliver the MOE underrun. However, the City was able to both make up for the MOE shortfall found for FY 2021-22 and deliver its current year MOE in FY 2022-23. Staff is recommending that the settlement agreement be amended so that the City can move forward and be found eligible without having to wait another year. The proposed amendment would also remove the requirement to conduct another AUP of City MOE expenditures for FY 2023-24 and would put the City back into the regular review cycle.

**Summary**

Auditors have applied AUP to the City's M2 MOE-related expenditures for FY 2022-23 and have reported that the City has made up the FY 2021-22 MOE as well as delivered its current year MOE. Staff is recommending an amendment to the settlement agreement to reduce the term to deliver the FY 2021-22 shortfall to one year and remove the audit requirement for FY 2023-24, reinstate City eligibility upon execution of the amended settlement agreement, and direct staff to reinstate payments to the City that were held during the period of ineligibility (less FY 2022-23 audit costs) within ten days of execution of the amended settlement agreement. If approved by the Board, these actions would conclude the City's period of M2 ineligibility and place the City back on an eligibility cycle consistent with other eligible local agencies.

**Attachment**

- A. City of Cypress Measure M2 Maintenance of Effort Independent Accountant's Report on Applying Agreed-Upon Procedures for the Year Ended June 30, 2023

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