



San Luis Obispo Flood Control and Water Conservation District

Proposition 84 Bond Program

Grant Agreements 4600009717, 4600010061,
4600010880, and 4600011487

Team Members

Jennifer Whitaker, Chief
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Final reports are available on our website at <http://www.dof.ca.gov>

You can contact our office at:

California Department of Finance
Office of State Audits and Evaluations
915 L Street, 6th Floor
Sacramento, CA 95814
(916) 322-2985



Transmitted via e-mail

May 4, 2018

Ms. Karla Nemeth, Director
California Department of Water Resources
P.O. Box 942836, Room 1115-1
Sacramento, CA 94236-0001

Dear Ms. Nemeth:

**Final Report—San Luis Obispo Flood Control and Water Conservation District,
Proposition 84 Grant Audit**

The California Department of Finance, Office of State Audits and Evaluations, has completed its audit of the San Luis Obispo Flood Control and Water Conservation District's (District) grants 4600009717, 4600010061, 4600010880, and 4600011487, issued by the California Department of Water Resources.

The enclosed report is for your information and use. The District's response to the report findings is incorporated into this final report. The District agreed with our findings. We appreciate their assistance and cooperation during the engagement, and their willingness to implement corrective actions. This report will be placed on our website.

If you have any questions regarding this report, please contact Diana Antony, Manager, or Vance Cable, Supervisor, at (916) 322-2985.

Sincerely,

Original Signed by

Jennifer Whitaker, Chief
Office of State Audits and Evaluations

Enclosure

cc: Ms. Cindy Messer, Chief Deputy Director, California Department of Water Resources
Ms. Katherine Kishaba, Deputy Director of Business Operations, California Department of Water Resources
Mr. Michael Tufts, Acting Deputy Assistant, Bond Accountability Office, California Department of Water Resources
Mr. David Whitsell, Chief Auditor, California Department of Water Resources
Mr. Bryan Cash, Assistant Secretary for Administration and Finance, California Natural Resources Agency
Ms. Julie Alvis, Deputy Assistant Secretary, California Natural Resources Agency
Mr. Wade Horton, County Administrative Officer, County of San Luis Obispo
Mr. John Peschong, Chair, Board of Supervisors, County of San Luis Obispo

BACKGROUND, SCOPE AND METHODOLOGY

BACKGROUND

California voters approved the Safe Drinking Water, Water Quality and Supply, Flood Control, River and Coastal Protection Bond Act of 2006 (Proposition 84). The \$5.4 billion of bond proceeds finance a variety of natural resource programs.

Established by the Legislature in 1945, the San Luis Obispo Flood Control and Water Conservation District (District) is tasked with identifying flooding problems, recommending solutions, and helping local areas in the County of San Luis Obispo (County) implement recommended solutions. Governed by the County Board of Supervisors, the District shares the same staff and the same geographic boundaries as the County.

The District received four grants from the California Department of Water Resources (DWR) as part of DWR's Integrated Regional Water Management Program (IRWM), designed to improve water supply reliability and to improve and protect water quality. Specifically:

- Grant 4600009717 – \$10.4 million to assist with four separately identified projects.
- Grant 4600010061 – \$1 million to update the San Luis Obispo County Region's IRWM Plan to meet standards established in the August 2010 IRWM Program Guidelines.
- Grant 4600010880 – \$6.3 million to assist with four separately identified projects.
- Grant 4600011487 – \$3.7 million to assist with four separately identified projects.

For each grant, the District is required to provide a minimum of 25 percent of the total project cost as match funding. The District is the lead agency for administering the grants and collaborates with several Local Project Sponsors (LPS) to oversee the completion of projects awarded under the grants. An LPS is a local public agency which provides project management, oversight, and compliance administration. The LPSs are responsible for completing the project deliverables and providing the support for reimbursable grant expenditures.

SCOPE

In accordance with the California Department of Finance's bond oversight responsibilities, we audited the following District Proposition 84 funded grants:

<u>Grant Agreement</u>	<u>Audit Period</u>
4600009717	August 16, 2011 through December 21, 2016 ¹
4600010061	September 30, 2008 through March 31, 2015
4600010880	January 1, 2010 through March 20, 2017 ²
4600011487	October 1, 2014 through September 26, 2016 ³

¹ An interim audit was conducted on grant 4600009717 as the grant period ends May 30, 2018.

² An interim audit was conducted on grant 4600010880 as the grant completion report had not been submitted at the time of our fieldwork in November 2017.

³ An interim audit was conducted on grant 4600011487 as the grant period ends June 30, 2019.

The audit objectives were to determine whether the District claimed grant expenditures in compliance with the grant requirements and to determine whether grant deliverables were completed as required. We did not assess the efficiency or effectiveness of program operations. Further, no assessment was performed on the reasonableness of the land acquisition costs or the conservation value of acquired land or projects completed.

The District's management is responsible for ensuring accurate financial reporting and compliance with applicable laws, regulations, and grant requirements. DWR and the California Natural Resources Agency are responsible for the state-level administration of the bond program.

METHODOLOGY

To determine whether grant expenditures were in compliance with the grant requirements; and if the grant deliverables were completed, we performed the following procedures:

- Examined grant files, grant agreements, and applicable policies and procedures, to gain an understanding of the IRWM grant projects and program.
- Interviewed DWR, District, and LPS personnel responsible for overseeing reimbursable grant expenditures to obtain an understanding of how each party oversees various grant funded projects.
- Selected a sample of projects to determine if claimed expenditures, including match, were allowable (i.e. grant-related, incurred within the grant period), and supported by accounting records by reviewing District and LPS accounting records, vendor invoices, and bank statements or similar documentation. Projects were selected to achieve representation of the various LPS, project statuses, and project types.
- Evaluated whether a sample of grant compliance terms and deliverables were met by reviewing quarterly progress reports, project completion reports certified by a California Registered Civil Engineer, engineering and inspection reports, construction site photos, and conducting a site visit to verify existence.

In conducting our audit, we obtained an understanding of the District's internal controls, including any information systems controls that we considered significant within the context of our audit objectives. We assessed whether those controls were properly designed, implemented, and operating effectively. No deficiencies in internal control were identified during our audit or were determined to be significant within the context of our audit objectives.

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.

Except as noted below, the grant expenditures claimed, including match, complied with the grant agreements' requirements. Additionally, the grant deliverables available for review at the time of our audit fieldwork in November 2017, were completed as specified in the grant agreements. However, as detailed in Finding 2, one of the projects funded under agreement 4600010880 was non-operational as of our audit fieldwork in November 2017. The Schedules of Claimed and Questioned Amounts are presented below.

Schedule of Claimed and Questioned Amounts

Grant Agreement Number 4600009717		
Task	Claimed¹	Questioned
Direct Project Administration	\$ 55,556	\$ 0
Construction/Implementation	7,883,471	0
Total Grant Funds	\$ 7,939,027	\$ 0
Match Funds	47,361,486	0
Total Project Expenditures	\$ 55,300,513	\$ 0

Grant Agreement Number 4600010061		
Task	Claimed	Questioned
Personnel Services	\$ 400,000	\$ 113,603
Professional and Consultant Services	600,000	0
Total Grant Funds	\$ 1,000,000	\$ 113,603
Match Funds	434,660	0
Total Project Expenditures	\$ 1,434,660	\$ 113,603

Grant Agreement Number 4600010880		
Task	Claimed²	Questioned
Direct Project Administration	\$ 281,220	\$ 0
Land Purchase/Easements	13,821	0
Planning/Design/Engineering/Environmental Documentation	1,088,547	0
Construction/Implementation	4,939,402	0
Total Grant Funds	\$ 6,322,990	\$ 0
Match Funds	3,089,850	0
Total Project Expenditures	\$ 9,412,840	\$ 0

Grant Agreement Number 4600011487		
Task	Claimed³	Questioned
Planning/Design/Engineering/Environmental Documentation	11,970	\$ 0
Construction/Implementation	337,831	0
Total Grant Funds	\$ 349,801	\$ 0
Match Funds	86,259	0
Total Project Expenditures	\$ 436,060	\$ 0

¹ DWR awarded \$10,401,000; however, the District only claimed \$7,939,027 as of December 21, 2016.

² DWR awarded \$6,323,610; however, the District only claimed \$6,322,990 as of March 20, 2017.

³ DWR awarded \$3,702,762; however, the District only claimed \$349,801 as of September 26, 2016.

Finding 1: Expenditures Claimed Outside Allowable Period

The District claimed \$113,603 for work that was performed prior to the beginning of the allowable period of grant agreement 4600010061. Specifically, the allowable period for grant funds and match funding are distinct. Grant Agreement, section 11, states that work performed after the grant award date, November 29, 2012, shall be eligible for reimbursement. However, the District erroneously used section 6 of the Grant Agreement, which allows match funding to be claimed if performed after September 30, 2008. Consequently, the \$113,603 claimed represented expenditures for work performed prior to November 29, 2012.

Recommendations:

- A. Remit \$113,603 to DWR for the portion of project expenditures reimbursed for work performed prior to the beginning of the grant term.
- B. Ensure claimed expenditures are incurred within the appropriate grant term. The grant agreement provisions should be used as a guide to develop any desk procedures for preparing reimbursement claims.

Finding 2: Non-Operational Project

Although the Cambria Community Services District (Cambria), a local project sponsor, completed an Advanced Water Treatment Plant (Plant) in accordance with grant agreement 4600010880, the Plant is currently non-operational. Specifically, Cambria received over \$4.3 million in grant funds from DWR to construct a Plant that would provide approximately 240 to 250 acre-feet of water during a six-month dry period. Cambria reported in its June 2016 project completion report that it had completed construction of the Plant and had determined through intermittent testing that the Plant could produce the requisite amount of water. However, due to subsequent events, the Plant became non-operational.

Specifically, on July 13, 2017, the Regional Board adopted Cease and Desist Order No. R3-2016-007 (Order), which required Cambria to immediately cease use of the evaporation pond, a key component of the Plant. According to the Regional Board, an inundation of surface water in January and February 2017 caused several regulatory violations that threatened water quality and the environment, resulting in the issuance of the Order. As a result, Cambria worked with the Regional Board to develop a plan to remediate the issues, which in December 2017 the Regional Board voted to accept. Cambria's plan involves ultimately abandoning the evaporation pond and modifying the Plant's water treatment process with a targeted completion date of August 2018. However, Cambria has not tested whether its modified Plant will be able to produce the requisite amount of water. As part of the grant agreement, Cambria must submit to DWR an annual Post-Performance Report that summarizes, among other things, the actual performance of the Plant compared to its expected performance and any additional information relevant to its continued operation.

Recommendations:

- A. Monitor Cambria's efforts in complying with the Regional Board's cease and desist order and modification of the Plant.
- B. After Plant modifications, require Cambria to test whether the new Plant can produce the requisite 240 to 250 acre-feet of water over a six-month dry period and report the results of its testing to the District and DWR.



COUNTY OF SAN LUIS OBISPO
Department of Public Works
John Diodati, Interim Director

April 13, 2018

TRANSMITTED VIA EMAIL ONLY

Ms. Jennifer Whitaker, Chief
Office of State Audits and Evaluations
Department of Finance
915 L Street
Sacramento, CA 95814-3706

Subject: Response to Draft Report-San Luis Obispo Flood Control and Water Conservation
District, Proposition 84 Grant Audit

Dear Ms. Whitaker:

We are in receipt of your draft audit report dated March 30, 2018 and have prepared the attached responses.

The District appreciates the opportunity to respond to your recommendations and findings, and hope for mutual resolution. If you have any questions regarding the responses, please contact Mladen Bandov, Water Resources Engineer, or Straith Smith Zanartu, Finance Division Manager, at (805) 781-5252.

Sincerely,

"Original signed by"

JOHN DIODATI
Interim Director

Enclosure

c: Wade Horton, County of San Luis Obispo Administrative Officer
Mark Hutchinson, Deputy Director, Department of Public Works
Straith Smith Zanartu, Finance Division Manager, Department of Public Works
Wendy Hall, Division Manager Administration, Department of Public Works
Courtney Howard, Division Manager Water Resources, Department of Public Works
Kerry Bailey, Audit Chief, Auditor Controller Treasurer Tax Collector
Mark Maier, Auditor, Auditor Controller Treasurer Tax Collector

File: CF 900.48.01.01

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**San Luis Obispo Flood Control and Water Conservation District
Department of Public Works, County of San Luis Obispo
Proposition 84 Grant Audit
Responses to Findings**

Response to Finding #1: Expenditures Claimed Outside Allowable Period

Regarding Grant Agreement 4600010061, at the time the initial billing was done, the Project Manager at Department of Water Resources indicated that the budget could be reallocated via a formal budget adjustment between categories to align with the actual costs incurred for the program. This budget was adjusted on Amendment #1 to the grant agreement, which was executed on February 9, 2015. Shortly after executing the Amendment, Invoice #1 was submitted to Department of Water Resources by the District as originally prepared. Unfortunately, when the budget was reallocated within the three budget categories (Personnel, Operating Expenses, and Professional Services), the amounts and categories were incorrectly reapportioned. Since the budget adjustment was completed after the billing was prepared, the District did not discern this error as this was the District's first and only billing. It was the intent of both parties to mirror the invoice and the budget to reconcile the grant.

Due to the fact that the budget adjustment was not completed in alignment with the billing, the District is proposing two alternatives instead of returning \$113,603. The first alternative would be for the District to work with the Department of Water Resources and request a budget amendment to realign the budgeted line items with actual expenditures, which was the intent of the budget amendment originally. The second alternative would be that since the District has sufficient expenditures in other budget line items that do fit within the grant timeline criteria and program scope, the District would resubmit these expenditures to the Department of Water Resources for their approval, and ultimately back to the Department of Finance for their audit.

The District takes grant program compliance very seriously, values the ongoing partnerships and continued collaboration with the Department of Water Resources, who have been an integral partner in many of District's programs. The District also understands the Department of Finance's role in safeguarding grant funding to ensure resources are spent in accordance with the grant's scope of work.

As recommended, the District will develop a grant agreement procedure manual. In addition, a supplementary review process will be implemented regarding follow up on budget adjustments to ensure that the Grantor and Grantee are both in agreement with any budget revisions.

Response to Finding #2: Non-Operational Project

The District agrees that the Cambria Community Services District (CSD) emergency water supply project is currently non-operational and they are working to modify the facility so that it is operational for future drought conditions. Although the CSD submits annual post-performance reports that summarize the actual performance of the facility, the District will request additional monthly reports from the CSD to monitor its compliance with the Regional Water Board's cease and desist order. The District is committed to taking all actions necessary to satisfy its obligations under the grant agreement, including those set forth in Paragraph 20 related to operation and maintenance of the project. Upon modification of the facility and pursuant to the grant agreement and the District's related funding agreement with the CSD, the District will direct the CSD to test and report to the District and DWR that the facility can achieve the benefits stated in the grant agreement.