



January 13, 2020

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The Honorable Rudy Salas, Chairman
Joint Legislative Audit Committee
1020 N Street, Room 107
Sacramento, California 95814

RE: Local Government High Risk Audit Program – City of San Gabriel

Dear Chairman Salas:

Government Code section 8546.10 permits the California State Auditor's Office (office) to develop a high-risk local government agency audit program for the purpose of identifying, auditing, and issuing reports on any local government agency, including a city, county, special district, or other publicly created entity, that the office identifies as being at high risk for the potential of waste, fraud, abuse, or mismanagement or that has major challenges associated with its economy, efficiency, or effectiveness. Pursuant to this provision, I am respectfully requesting the committee's approval of an audit of the City of San Gabriel.

Located approximately 10 miles northeast of the City of Los Angeles, San Gabriel has a population of more than 40,000. The city is governed by a city council comprised of five elected officials who appoint a city manager to carry out the council's initiatives and provide administrative direction to the city. The city manager is also responsible for keeping the city council fully informed of San Gabriel's financial condition and future financial challenges. City staff provide services including public safety, public works, recreational and cultural activities, planning, zoning, and general administrative services.

In October 2019, my office identified San Gabriel as the eighth most fiscally challenged city in California primarily because it had insufficient cash and financial reserves to pay its ongoing bills and it faces challenges in paying for employee retirement benefits. My office subsequently conducted an onsite assessment in December 2019 and determined that San Gabriel is potentially a high-risk entity as it still lacks available cash, has depleted its financial reserves, and has large unfunded retirement costs.

San Gabriel's fiscal challenges raise concerns about its ability to continue providing essential services to its residents. From fiscal years 2015–16 through 2017–18, San Gabriel's annual expenditures exceeded its revenues by amounts ranging from \$2.6 million to \$6.6 million, which caused its general fund balance to decline significantly. San Gabriel also entered into a loan in 2014 that required it to set aside millions of dollars of its general fund cash for 10 years as collateral for the loan—further inhibiting its ability to pay its bills. Because this cash is not currently available, San Gabriel borrows money from its other funds to support its operations, which can create challenges in stabilizing its finances. San Gabriel's audited financial statements for fiscal year 2018–19 raised concerns about the significant reductions in San Gabriel's general fund balance and the impact on its future operations.

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Other factors contribute to San Gabriel's financial challenges. For example, many of San Gabriel's key management positions turned over in the last five years, including the city manager and finance director. As of December 2019, San Gabriel had not hired a permanent finance director, an individual who would play a key role in developing a plan to address San Gabriel's fiscal challenges. Finally, San Gabriel appears to lack adequate controls over its contracting and hiring functions.

An audit of the city of San Gabriel will determine whether the city has effective controls in place to protect city funds, whether it uses its funds in the best interests of the city's residents, and whether it has a plan to address its financial challenges. The proposed audit will address the following questions:

- What is causing San Gabriel's financial challenges and does it have an adequate plan for addressing those challenges?
- Has San Gabriel management accurately and transparently characterized the city's financial condition and challenges to its city council and residents?
- Why did San Gabriel's city council approve the loan in 2014 that tied up millions of dollars of its cash?
- Are San Gabriel's financial challenges affecting its ability to pay its bills when due or impacting its ability to provide services to its residents?
- Does San Gabriel comply with prudent procurement policies and best practices for ensuring it receives the best value for the goods and services it purchases?
- What efforts is San Gabriel making to fill key management vacancies with qualified candidates and to maintain organizational and leadership continuity within city operations?

If you have any questions regarding this audit proposal, please contact me or Paul Navarro, Chief Deputy State Auditor, Operations, at (916) 445-0255.

Sincerely,



ELAINE M. HOWLE, CPA
California State Auditor