

SANTA CLARA VALLEY WATER DISTRICT

Audit Report

FLOOD CONTROL SUBVENTIONS PROGRAM

Upper Guadalupe River and
Upper Llagas Creek Watershed Projects

July 1, 2014, through December 31, 2019



BETTY T. YEE
California State Controller

August 2022



BETTY T. YEE
California State Controller

August 31, 2022

Eric Nichol, Assistant Division Chief
Division of Flood Management
Department of Water Resources
3310 El Camino Avenue, Suite 120
Sacramento, CA 95821

Dear Mr. Nichol:

The State Controller's Office audited Flood Control Subventions Program claims submitted by the Santa Clara Valley Water District to the Department of Water Resources (DWR). Our audit pertained to DWR Claim Numbers UGR 52 through 55 and ULCW 164 through 286, for the period of July 1, 2014, through December 31, 2019.

The district claimed \$47,335,299 for the Upper Guadalupe River and Upper Llagas Creek Watershed projects during the audit period. Our audit found that \$43,202,026 is allowable and \$4,133,273 is unallowable. The costs are unallowable because the district lacked required DWR preapproval or supporting documentation, or the costs were unrelated to the projects.

The State's share of allowable costs is \$35,062,825. DWR reimbursed the district \$33,296,010 during the audit period; therefore, the district is owed the remaining balance of \$1,766,815.

DWR retained \$3,699,557, which was to be released to the district pending the results of this audit. DWR should reduce the retention balance by \$1,932,742 to \$1,766,815, the amount still owed to the district, based on our audit.

If you have any questions, please contact Efren Loste, Chief, Local Government Audits Bureau, by telephone at (916) 324-7226.

Sincerely,

Original signed by

KIMBERLY TARVIN, CPA
Chief, Division of Audits

KT/as

cc: Sami Nall, Manager, Flood Control Subventions Program
Department of Water Resources
Rick Callender, Chief Executive Officer
Santa Clara Valley Water District
Darin Taylor, Chief Financial Officer
Santa Clara Valley Water District
John L. Varela, Chair Pro Tem
Santa Clara Valley Water District

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Audit Report

Summary

The State Controller's Office (SCO) audited Flood Control Subventions Program claims submitted by the Santa Clara Valley Water District to the Department of Water Resources (DWR). Our audit pertained to DWR Claim Numbers UGR 52 through 55 and ULCW 164 through 286, for the Upper Guadalupe River and Upper Llagas Creek Watershed projects, for the period of July 1, 2014, through December 31, 2019.

The district claimed \$47,335,299 for the Upper Guadalupe River and Upper Llagas Creek Watershed projects during the audit period. Our audit found that \$43,202,026 is allowable and \$4,133,273 is unallowable. The costs are unallowable because the district lacked required DWR preapproval or supporting documentation, or the costs were unrelated to the projects.

Pursuant to California Water Code section 12832, the DWR reimbursed the district 90% of eligible costs claimed, with the remaining 10% to be released subject to the completion of this audit.¹ Based on our audit, the State's share of allowable project costs is \$35,062,825. DWR reimbursed the district \$33,296,010 during the audit period; therefore, the district is owed the remaining balance of \$1,766,815.

Background

The State of California provides financial assistance to local agencies participating in the construction of federal flood control projects. Under the Flood Control Subventions Program (California Water Code, Division 6, Part 6, Chapters 1 through 4), the DWR pays a portion of the local agency's share of flood control project costs, including the costs of rights of way, relocation, and recreation and fish and wildlife enhancements. The DWR's *Guidelines for Reimbursement on Flood Control Projects (Guidelines)* describe the compliance requirements for local agencies seeking reimbursement for the State's share of federal flood control projects.

Audit Authority

We conducted this performance audit under the general authority of Government Code section 12410 and the specific authority of California Water Code section 12832, which requires the State Controller to perform audits of flood control projects.

Objective, Scope, and Methodology

Our audit objective was to determine whether the costs claimed, as presented in the Schedule were allowable and in compliance with the DWR *Guidelines*, and adequately supported and documented.

Our audit pertained to DWR Claim Numbers UGR 52 through 55 and ULCW 164 through 286 for the Upper Guadalupe River and Upper Llagas Creek Watershed projects, for the period of July 1, 2014, through December 31, 2019.

¹ California Water Code stipulates the percentage of state funding by project cost category.

To achieve our objective, we performed the following procedures:

- We gained an understanding of the district's internal controls that are significant to the audit objective by interviewing key personnel, completing an internal control questionnaire, and reviewing the district's organization chart.
- We evaluated and assessed control activities over the claim preparation process by inspecting documents and records, and by inquiring with key personnel.
- We assessed the reliability of computer-processed data by reviewing existing information about the data and the system that produced it; by interviewing district officials knowledgeable about the data; and by tracing data to source documents, based on auditor judgment and non-statistical sampling. We determined that the data was sufficiently reliable for the purposes of achieving our audit objective.
- We conducted a risk assessment to determine the nature, timing, and extent of substantive testing.
- We reviewed the district's prior SCO and single audits.
- We reviewed the DWR's engineering reports and/or claim evaluations pertaining to the district's claims.
- We determined whether the district received revenues that should have been offset against the flood program expenditures.
- We reviewed the district's claim detail for any condemnation interest, and inquired of the district whether it had received interest on condemnation deposits.
- We determined whether the district received from DWR advances on its flood control project expenditures.
- We verified through sampling that the costs claimed were supported by proper documentation and eligible in accordance with the applicable criteria. Based on our risk assessment, we tested all items that were equal to or greater than the significant item amount (calculated based on materiality threshold). We also tested additional items that were valued less than the individual significant item amount, based on auditor judgment and non-statistical sampling. Based on errors identified in the selected sample, we expanded our testing.

We tested the following expenditures:

- Land – We tested all \$39,390,921 in total land, easement, and right-of-way acquisition costs claimed.
- Relocation – We tested \$242,257 of \$300,257 in total relocation costs claimed.
- Labor – We tested \$67,965 of \$4,519,305 in total labor costs.
- Services and supplies – We tested \$939,046 of \$3,124,816 in total services and supplies costs claimed.

For the selected sample, errors found were not projected to the intended (total) population.

We did not audit the district's financial statements. We limited our audit scope to planning and performing audit procedures necessary to obtain reasonable assurance that costs claimed are allowable for reimbursement.

We conducted the 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Conclusion

The district claimed \$47,335,299 in project costs for the period of July 1, 2014, through December 31, 2019.

Our audit found instances of noncompliance with the requirements described in the Objective, Scope, and Methodology section. These instances are quantified in the Schedule and described in the Findings and Recommendations section.

Based on our audit, the State's share of allowable project costs is \$35,062,825. DWR reimbursed the district \$33,296,010 during the audit period; therefore, the district is owed the remaining balance of \$1,766,815.

Follow-up on Prior Audit Findings

The finding noted in our prior audit report, issued on June 29, 2020, has been satisfactorily resolved by the district.

Views of Responsible Officials

We issued a draft audit report on June 24, 2022. The district's representative responded by letter dated July 5, 2022 agreeing with the audit results. This final audit report includes the district's response as an attachment.

Restricted Use

This audit report is solely for the information and use of the Santa Clara Valley Water District, the DWR, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record, and is available on the SCO website at www.sco.ca.gov.

Original signed by

KIMBERLY TARVIN, CPA
Chief, Division of Audits

August 31, 2022

Schedule— Summary of Project Costs July 1, 2014, through December 31, 2019

Project / Claim #	Costs Claimed	Audit Adjustments to Claimed Costs ¹	Allowable per Audit	State Share of Eligibility Percentage ²	State Share of Claimed Costs	Adjustments to State Share	State Share of Allowable Costs	Reimbursement Received by the District ³	Reimbursement Due to District Pending Audit
Upper Guadalupe River Project									
UGR 2018-01(52)	\$ 20,275,000	\$ -	\$ 20,275,000	70%	\$ 14,192,500	\$ -	\$ 14,192,500	\$ 12,773,250	\$ 1,419,250
UGR 2019-01(53)	283,848	-	283,848	70%	198,694	-	198,694	178,824	19,870
UGR 2019-01(54)	646,822	-	646,822	70%	452,775	-	452,775	407,498	45,277
UGR 2019-02 (55)	825,000	-	825,000	70%	577,500	-	577,500	519,750	57,750
	\$ 22,030,670	\$ -	\$ 22,030,670		\$ 15,421,469	\$ -	\$ 15,421,469	\$ 13,879,322	\$ 1,542,147
Upper Llagas Creek Watershed Project									
ULCW 2015-01(164, 165)	\$ 919,750	\$ (44,450)	\$ 875,300	100%	\$ 919,750	\$ (44,450)	\$ 875,300	\$ 827,775	\$ 47,525
ULCW 2015-02 (166)	64,600	-	64,600	100%	64,600	-	64,600	58,140	6,460
ULCW 2015-02 (167)	408,369	-	408,369	100%	408,369	-	408,369	367,532	40,837
ULCW 2015-03 (168)	42,817	(37,500)	5,317	100%	42,817	(37,500)	5,317	38,535	(33,218)
ULCW 2015-03 (169)	24,428	-	24,428	100%	24,428	-	24,428	21,985	2,443
ULCW 2015-03 (170, 171 Revised)	868,169	-	868,169	100%	868,169	-	868,169	1,178,481	(310,312)
ULCW 2016-01(174, 177 Revised)	925,269	-	925,269	100%	925,269	-	925,269	1,332,988	(407,719)
ULCW 2016-02 (172, 175)	982,313	(4,605)	977,708	100%	982,313	(4,605)	977,708	879,937	97,771
ULCW 2016-03 (173, 176)	187,093	(2,754)	184,339	100%	187,093	(2,754)	184,339	165,905	18,434
ULCW 2017-01(178- 192)	1,653,650	(218,800)	1,434,850	100%	1,653,650	(218,800)	1,434,850	1,488,285	(53,435)
ULCW 2017-02 (193-208)	1,452,375	(239,561)	1,212,814	100%	1,452,375	(239,561)	1,212,814	1,302,792	(89,978)
ULCW 2017-03 (209-226)	1,794,800	(366,575)	1,428,225	100%	1,794,800	(366,575)	1,428,225	1,615,320	(187,095)
ULCW 2018-01(229, 232, 235 Revised)	1,081,016	-	1,081,016	100%	1,081,016	-	1,081,016	972,914	108,102
ULCW 2018-02 (227, 230, 233)	900,282	(36)	900,246	100%	900,282	(36)	900,246	810,222	90,024
ULCW 2018-03 (228, 231, 234 Revised)	513,458	-	513,458	100%	513,458	-	513,458	462,112	51,346
ULCW 2018-03 (231 Partial)	1,000,000	-	1,000,000	55%	550,000	-	550,000	495,000	55,000
ULCW 2019-01(237, 241, 242, 244)	433,400	-	433,400	100%	433,400	-	433,400	390,060	43,340
ULCW 2019-02 (236)	44,000	(16,800)	27,200	100%	44,000	(16,800)	27,200	24,480	2,720
ULCW 2019-03 (238)	80,100	(31,200)	48,900	100%	80,100	(31,200)	48,900	44,010	4,890
ULCW 2019-04 (239)	116,900	(17,400)	99,500	100%	116,900	(17,400)	99,500	105,210	(5,710)
ULCW 2019-05 (240)	169,000	(5,200)	163,800	100%	169,000	(5,200)	163,800	152,100	11,700
ULCW 2019-06 (243)	202,800	(51,700)	151,100	100%	202,800	(51,700)	151,100	135,990	15,110
ULCW 2019-07 (245)	90,000	(9,326)	80,674	100%	90,000	(9,326)	80,674	72,607	8,067
ULCW 2019-08 (246)	83,900	(11,200)	72,700	100%	83,900	(11,200)	72,700	65,430	7,270

Schedule (continued)

Project / Claim #	Costs Claimed	Audit Adjustments to Claimed Costs ¹	Allowable per Audit	State Share of Eligibility Percentage ²	State Share of Claimed Costs	Adjustments to State Share	State Share of Allowable Costs	Reimbursement Received by the District ³	Reimbursement Due to District Pending Audit
Upper Llagas Creek Watershed Project (continued)									
ULCW 2019-09 (247, 248, 250, 253)	596,200	(11,000)	585,200	100%	596,200	(11,000)	585,200	536,580	48,620
ULCW 2019-10 (254, 255, 256, 257)	118,900	-	118,900	100%	118,900	-	118,900	107,010	11,890
ULCW 2019-11 (249)	150,800	(76,438)	74,362	100%	150,800	(76,438)	74,362	66,926	7,436
ULCW 2019-12 (251)	161,800	(54,200)	107,600	100%	161,800	(54,200)	107,600	96,840	10,760
ULCW 2019-13 (252)	60,500	(12,244)	48,256	100%	60,500	(12,244)	48,256	43,431	4,825
ULCW 2020-01 (258-268)	530,575	-	530,575	100%	530,575	-	530,575	477,518	53,057
ULCW 2020-02 (269)	5,313,439	(2,913,439)	2,400,000	55%	2,922,391	(1,602,391)	1,320,000	1,188,000	132,000
ULCW 2020-03 (278, 281, 284)	84,772	(8,845)	75,927	100%	84,772	(8,845)	75,927	68,334	7,593
ULCW 2020-03 (279, 282, 285)	219,245	-	219,245	100%	219,245	-	219,245	197,321	21,924
ULCW 2020-03 (280, 283, 286)	998,029	-	998,029	100%	998,029	-	998,029	898,226	99,803
ULCW 2020-04 (270-272)	1,136,000	-	1,136,000	100%	1,136,000	-	1,136,000	1,022,400	113,600
ULCW 2020-05 (273-277)	1,895,880	-	1,895,880	100%	1,895,880	-	1,895,880	1,706,292	189,588
	\$ 25,304,629	\$ (4,133,273)	\$ 21,171,356		\$ 22,463,581	\$ (2,822,225)	\$ 19,641,356	\$ 19,416,688	\$ 224,668
	\$ 47,335,299	\$ (4,133,273)	\$ 43,202,026		\$ 37,885,050	\$ (2,822,225)	\$ 35,062,825	\$ 33,296,010	\$ 1,766,815

¹ See the Findings and Recommendations section. The audit adjustment of \$4,133,273 is comprised of \$3,197,615 (Finding 1); and \$935,658 (Finding 2).

² The State's share of allowable project costs represents the percentage of state funding, as stipulated in the California Water Code, for each project cost category.

³ See the Findings and Recommendations section. The district submitted revised claims for ULCW Claim Numbers 170, 171, 174, and 177 subsequent to receiving reimbursement from DWR (Finding 3).

Findings and Recommendations

FINDING 1— DWR adjustments

The district claimed \$47,335,299 for costs related to the Upper Guadalupe River Project and Upper Llagas Creek Watershed Project. During its review of the claims, the DWR identified \$3,197,615 as ineligible for reimbursement.

The DWR reimburses the district for 70% of eligible costs for the Upper Guadalupe River Project and 100% of eligible costs for the Upper Llagas Creek Watershed Project, except for the Nature Quality property. For this property acquisition, the DWR and the district mutually agreed on a 55% reimbursement rate for eligible costs.

At the time of DWR review and approval, the State's share of the reimbursable claimed costs was \$36,995,567. The DWR reimbursed the district \$33,296,010 (90% of eligible project costs) and withheld \$3,699,557 (10% of eligible project costs) as a retention balance pending our audit.

After corresponding with the DWR, the district submitted revised claims for ULCW Claim Numbers 170, 171, 174, and 177, reducing claimed costs by \$997,084 to \$47,335,299. The State's share of reimbursable claimed costs thus decreased to \$35,998,483.

Of the \$3,197,615 in ineligible costs identified by the DWR, \$3,181,375 was for negotiated settlements to acquire land, rights-of-way, and easements. The negotiated settlements exceeded the appraised fair market value, and the district did not request the necessary preapproval from the DWR.

The remaining \$16,240 of ineligible costs was for associated land costs (services and supplies). Of this amount, \$13,450 was related to the Nature Quality property, and \$2,790 was for items that lacked supporting documentation.

The following table shows the DWR's adjustment to the district's claimed costs:

DWR Audit Adjustments	Adjustment Amount
Negotiated settlements	\$ (3,181,375)
Nature Quality property	(13,450)
Services and supplies costs	(2,790)
Total DWR adjustments	<u>\$ (3,197,615)</u>

Paragraph 1 of Section IV.D, "Settlements," of the DWR *Guidelines* states:

Negotiated settlements and stipulated judgments may not exceed the local agency's high appraised value unless the advance approval of the Department [of Water Resources] has been obtained. . . .

Section VI.D., “State Review,” (page 39) of the DWR *Guidelines* states,

. . . The Department [of Water Resources] will deduct “without prejudice” any item which cannot be verified. The local agency will have 90 days from the date of notification of the deductions to submit additional supporting information. If such information is not received within 90 days, the Department will presume that the local agency accepted the deduction.

The district was unaware that the DWR *Guidelines* require local agencies to obtain advance approval from the DWR for negotiated settlements and stipulated court judgements that exceed the district’s high appraised value. The DWR informed the district, via email, of this requirement during its review process, and the district has since implemented a DWR preapproval process.

Recommendation

We recommend that the district follow applicable policies and procedures to ensure that all costs claimed for reimbursement are allowable.

FINDING 2— Unallowable land costs

The district claimed \$39,390,921 for land costs related to the Upper Guadalupe River Project and Upper Llagas Creek Watershed Project. We tested \$36,787,894 of these claimed costs, and identified \$683,250 in unallowable costs. We tested the remaining \$2,603,027 in land costs to determine whether additional claimed costs were unallowable. We identified an additional \$252,408 in unallowable costs, for a total of \$935,658 in unallowable land costs.

Of the \$935,658 in unallowable land costs, \$898,158 was for negotiated settlements to acquire land, rights-of-way, and easements; and \$37,500 was for costs that were unrelated to the flood control subvention projects. The \$898,158 was unallowable because the negotiated settlements exceeded the appraised fair market value, and the district did not request the necessary preapproval from the DWR. The \$37,500 was unallowable because the costs were for preventive maintenance work performed on bridges within the flood control project areas; however, the work was not for right-of-way or relocation costs. Therefore, the costs were unrelated to the Flood Control Subventions Program.

As a result, the State’s share of allowable costs should be reduced by \$935,658, as shown in the following table:

SCO Audit Adjustments	Adjustment Amount	State Share	Reduction in Reimbursement Due to District
Negotiated settlements	\$ 898,158	100%	\$ 898,158
Unrelated costs	37,500	100%	37,500
SCO Audit Adjustments	<u>\$ 935,658</u>		<u>\$ 935,658</u>

Paragraph 1 of Section IV.D, “Settlements,” of the *DWR Guidelines* states, in part:

Negotiated settlements and stipulated judgments may not exceed the local agency’s high appraised value unless the advance approval of the Department [of Water Resources] has been obtained. . . .

The Introduction of the *DWR Guidelines* states:

State assistance is limited to reimbursement of all or a portion of the costs of rights-of-way and relocations which are necessary for construction of the flood control features. . . .

The district was unaware that the *DWR Guidelines* require local agencies to obtain advance approval from the DWR for negotiated settlements and stipulated court judgements that exceed the district’s high appraised value. The DWR informed the district, via email, of this requirement during its review process, and the district has since implemented a DWR preapproval process.

Recommendation

We recommend that the DWR reduce the retention balance for reimbursement due the district by \$935,658. We also recommend that the district ensure that all costs claimed for reimbursement are allowable.

FINDING 3— Reimbursement in excess of revised claimed costs

The district claimed a total of \$47,335,299 for costs related to the Upper Guadalupe River Project and Upper Llagas Creek Watershed Project. During its review of the district’s claims, the DWR identified ineligible overhead costs in claims with ULCW Claim Numbers 229, 232, and 235.

After corresponding with the DWR, the district submitted revised claims for ULCW Claim Numbers 229, 232, and 235, removing the ineligible overhead costs from the claims. The district also submitted revised claims to remove \$997,084 in overhead costs for ULCW Claim Numbers 170, 171, 174, and 177. The DWR, however, had already reimbursed the district, based on the initial claim submission, resulting in excess reimbursements of \$718,031, for these claim numbers.

Recommendation

We recommend that the DWR reduce its retention balance for ULCW Claim Numbers 170, 171, 174, and 177 to zero, and reduce the reimbursements due the district by \$718,031.

**Attachment—
Santa Clara Valley Water District's
Response to Draft Audit Report**



Clean Water • Healthy Environment • Flood Protection

July 5, 2022

Ms. Kimberly Tarvin
State Controller's Office
Chief, Division of Audits
901 Corporate Center Drive, Suite 200
Monterey Park, CA 91754

Subject: Upper Guadalupe River and Upper Llagas Creek Subvention Claims Audit

Dear Ms. Tarvin:

The Santa Clara Valley Water District (Valley Water) is responding to the draft report dated June 24, 2022.

Valley Water would like to thank you and the auditor for the thorough and thoughtful work in reviewing the subvention program claims. As discussed at the telephone exit conference on April 28, 2022, Valley Water agrees with the three findings from the Upper Guadalupe River and Upper Llagas Creek Watershed projects from July 1, 2014, through December 31, 2019. We are taking immediate actions to ensure these recommendations are implemented going forward.

We have some observations we would like to share with you, and below are the three findings Valley Water is acknowledging.

Finding 1- DWR identified \$3,197,615 of costs as ineligible for reimbursement.

Finding 2- DWR identified \$935,658 of land costs as unallowable.

Finding 3- After DWR informed Valley Water that overhead costs were unallowable, Valley Water took immediate action to remove the overhead costs and submitted revised claims. However, DWR had already reimbursed the district based on the initial claims which resulted in excess reimbursements of \$718,031 for these claims.

In your letter on page four or page eight of the PDF file, there is one line item on the summary of project costs that needs to be corrected. The audit adjustment of \$37,500.00 of unrelated costs should be applied to Upper Llagas Creek Claim #168 as opposed to claim #167. This was acknowledged by the auditor on the email dated May 2, 2022.

The costs mentioned above are unallowable due to the lack of required DWR preapproval or supporting documentation. Prior to March 2020, Department of Water Resources (DWR) was processing reimbursements without pre-approval which resulted in overpayments.

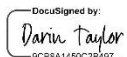
After being informed by DWR via email regarding this requirement, the district has since implemented the DWR preapproval process and will follow applicable policies and procedures to ensure that all future costs claimed for reimbursements are allowable. Valley Water's mutual goal is to prevent findings and we welcome your feedback.



According to the letter, Valley Water is owed the remaining balance of \$1,766,815 in retention.

Please contact Simon Lo, Senior Management Analyst at (408) 857-7036 or Mike Hagerty, Grants Administrator at (408) 599-9523 if you have any questions.

Regards,

DocuSigned by:


9C58A1450C2B407
Darin Taylor

Chief Financial Officer

Office of the Chief Executive Officer

**State Controller's Office
Division of Audits
Post Office Box 942850
Sacramento, CA 94250**

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