TUOLUMNE COUNTY ECONOMIC DEVELOPMENT AUTHORITY

EVALUATION OF SELECT CONTROL ELEMENTS OF THE TUOLUMNE COUNTY ECONOMIC DEVELOPMENT AUTHORITY

FINAL REPORT

April 11, 2019

Certified Public Accountants

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MGO Certified Public Accountants

Evaluation Report on Select Control Elements of TCEDA

Clerk and Auditor Controller
County of Tuolumne

Macias Gini & O'Connell LLP (MGO) presents its report concerning our evaluation of select control elements of the Tuolumne County Economic Development Authority (TCEDA) for the calendar year 2017 as follows:

Background

The Tuolumne County Economic Development Authority (TCEDA) was created in 2008 by the County of Tuolumne and the City of Sonora as a Joint Powers Authority vested with the power to implement, coordinate, and administer general economic development programs within Tuolumne County, including the City of Sonora. The TCEDA is one of a number of local economic development entities that have been created in recent decades as tools to help drive economic growth, job creation, and business assistance within their communities.

The TCEDA is administered by a Governing Board of seven members, comprised of two members each from the Tuolumne County Board of Supervisors and the Sonora City Council, as well as three at-large members who are appointed by the four City and County members of the Board. The Treasurer-Tax Collector of the County, the Clerk/Auditor-Controller of the County, and the County Counsel are designated as the Treasurer, Auditor-Controller, and Legal Advisor of the TCEDA, respectively.

The Economic Development Director (Director) of TCEDA was hired in 2009 and continued to work in that capacity until the dissolution of TCEDA began in 2019. Although administrative staff was also hired on occasion, the Director was at times the sole employee of the TCEDA conducting activities related to business retention, expansion, and attraction within the City and County.

In 2018, the Tuolumne County Grand Jury issued a report which identified weaknesses in TCEDA's management oversight and with the TCEDA's strategy and direction. Subsequently, the TCEDA Governing Board contracted with MGO to conduct an evaluation of specific internal control elements based on the Grand Jury's findings.

Objectives and Scope

The objectives of this engagement was to evaluate select control elements of TCEDA identified by the Grand Jury report. Specifically, we were to:

(a) Identify recommendations for improved internal controls over travel and entertainment authorization and approval to travel, and approvals of actual expenditures based on best practices;
(b) Identify recommendations for minimum disclosure requirements for business travel and business entertainment, which shall meet the Accountable Plan rules;
(c) Compare TCEDA performance metrics and management reporting to no more than three comparable agencies;
(d) Identify specific independent review and approval policy and processes for exceptions to established policies;
(e) Compare TCEDA disclosures regarding interactions with private businesses to County and City standards/guidelines for interactions with private businesses;
(f) Identify recommendations for policy elements addressing subsistence meals, lodging, business entertainment, and alcohol to meet the requirements of 2 CFR200 for federal allowable costs; and the minimum requirements shall meet the Accountable Plan rules; and
(g) Identify instances where the TCEDA Director's reported time was inconsistent with the employment agreement and compensation documents based on a non-statistical sample of 12 months.

Methodology

To meet the objectives of our engagement, we performed the following procedures: conducted on-site interviews with management/oversight staff; reviewed current travel and entertainment policy; reviewed travel and entertainment practices of three selected comparable agencies; reviewed the IRS accountable plan rules; reviewed TCEDA performance metrics and management reporting; reviewed metrics used by three comparable agencies; reviewed the current travel and entertainment policy of TCEDA; reviewed TCEDA disclosures; reviewed County and City standards; reviewed the employment agreement of the Director of the TCEDA; reviewed Executive/Confidential MOU during review period (2017); reviewed email correspondence and developed a timeline between emails, calendar, and time report; and identified gaps in the timeline. We were also tasked with reviewing 2 CFR 200 relating to meals, lodging, business entertainment, and alcohol. After review, however, we determined that the IRS accountable plan rules provided more applicable criteria.

Our evaluation was conducted in accordance with the Statements on Standards for Consulting Services issued by the American Institute of Certified Public Accountants (AICPA) and the terms of the agreement between MGO and the TCEDA. The work performed is only for the use and benefit of the County, the City, and the TCEDA Board of Directors.

Because the scope of work listed above does not constitute an examination or audit in accordance with generally accepted government auditing standards, we did not express an opinion on the results of our work, but instead have provided this report with our findings and recommendations. We had no obligation to perform any procedures beyond those listed in the objectives. If, however, as a result of the procedures or through other means, matters had come to our attention, we would have disclosed those matters to the TCEDA. Such disclosures, if any, may not include all matters which might have come to our attention had we performed additional procedures or an examination.

Results

Internal Controls over Travel and Entertainment, including Authorization and Approvals, Require Strengthening

A sound structure for internal controls can identify and address major performance and management challenges and areas at greatest risk of fraud, waste, abuse, and mismanagement. Internal controls comprise the governance structure, plans, methods, and policies and procedures used to accomplish the TCEDA's mission, goals, and objectives. Control activities are the policies and procedures that help ensure that management directives are carried out, and one key control activity - segregation of duties - is to ensure that no single person performs all the tasks related to any single transaction cycle. The creation, approval, review, and payment of any expenditure at a public agency should be performed by separate individuals. For some small local governments, segregation of duties may be a challenge. Review and approval by an appropriate second person may be the most important control activity. That second person may be a member of the governing body in a review or approval role.

During the timeframe of our review of TCEDA's Travel and Business Expense policy, there was no proper segregation of duties over the travel and expense reimbursement and approval processes within the policy; and, therefore, we could not conduct testing of authorizations or approvals over expenditures; the TCEDA Director prepared and approved his own expense reimbursements and travel arrangements. TCEDA's Travel and Business Expense policy did not include the needed mitigating controls, given that TCEDA employed a single staff member and no second person was identified for authorizations of expenses.

In addition to the lack of mitigating controls for segregation of duties within the TCEDA Travel and Business Expense policy, many sections of the policy directly provided the Director exemptions to the rules and also listed the Director as the approver of any exceptions. This allowed the Director to approve his own expenses that exceeded the policy limitations, or that were a variance from Travel policy provisions in the following areas; expenses exceeding $500, booking higher cost airfare, approval of rental car, higher lodging rates, and meal costs and tips.

To address these weaknesses in the policy, and strengthen internal controls surrounding the Travel and Business Expense process, the Governing Board should update the TCEDA Travel Policy in areas related to authorization and approvals for travel to establish appropriate segregation of duties, specifically where the Director has sole approval or is exempt from the rules. The next Director should be required to submit his/her travel plans, and independent reviews and approvals of expenditures and reimbursements should be performed, as well as monitoring conducted by the Auditor-Controller's office. Additionally, there should be a clear alignment of travel plans with the TCEDA's annual goals/plans, to establish a business connection and show justification of expenses incurred. Linking the travel expense to a goal of the TCEDA would bring the policy in better alignment with the Accountable Plan. Lastly, the policy update should include the requirement of an approval by the Board on expenses outside of the TCEDA's annual Workplan.

Specific Recommendations for Travel and Business Expense Policy Updates:

The Governing Board should:

- Update the current Travel and Business Expense Policy to comply with the Accountable Plan requirement of establishing a business connection to the expenses incurred for TCEDA programs/plans. Consider developing a Travel Authorization Form, which would require a statement with the purpose and benefit, and approval prior to travel being incurred. Additionally, a Travel Summary Form should be submitted within 30-45 days of travel, which includes both actual and estimated costs along with an explanation for any significant differences. Only through approval of the Travel Summary Form will additional expenses not included in the original Travel Authorization Form be approved.

- At a minimum, require the Director to document reasons for granting exceptions or justification for an exemption from policy; and requests should be subject to approval by the Governing Board. Alternatively, a more risk-based approach may be taken by addressing each identified exception individually and perform a gap analysis between current policy and exceptions identified as high risk. Policies and procedures would be adjusted according to the level of assessed risk of each exception.

- To strengthen segregation of duties overall and to address exceptions, the policy should be updated to require the Auditor Controller's Office to conduct independent oversight of the TCEDA Director's expenses by: (a) ensuring expenses are properly reviewed and authorized, (b) actual expenditures are supported by accurate and required documentation, and (c) expenses incurred are paid according to TCEDA policies, through the use of the Travel Authorization and Travel Summary forms. When the actual cost of a trip significantly exceeds the cost authorized prior to travel, the Auditor Controller should review and authorize or deny the additional expense based on the documentation provided.

- Require any expense, travel or otherwise, with a purpose outside of the TCEDA goals and Workplan to be reviewed and approved by the Governing Board.

Minimum Disclosure Requirements for Business Travel and Business Entertainment Should Meet the Accountable Plan Rules

The Accountable Plan requires that an organization's payment or reimbursement arrangement include the following three criteria: (1) a requirement of a business connection to the expense, (2) timely accounting of the expense, and (3) the timely return of excess reimbursements. We observed gaps between the Accountable Plan requirements and the TCEDA policy in two of the three areas. First, the Accountable Plan requires a business connection to claim expense reimbursement. The TCEDA Travel and Business Expense Policy does not require this. Additionally, the Accountable

Plan requirement of a timely return of excess reimbursements is not included in TCEDA's Travel and Business Expense Policy. The third Accountable Plan requirement of timely accounting of expenses was present within the TCEDA Policy. To align its policies with the Accountable Plan and the IRS Fringe Benefit Guide, the Governing Board should update the travel policy to include requirements of a business connection to the claimed expense and the timely return of any excess reimbursements. Updates should also be included to require that any travel expense incurred and claimed for reimbursement involve temporary travel on business away from the employee's tax home. Additionally, while there are no specifics on dollar limits and alcohol in the IRS Fringe Benefit Guide, there should be an update to the current policy to include language regarding the fair market value of meals may only be nontaxable if they meet the purpose and timeliness restrictions. Additionally, the Governing Board may consider budgeting and accounting for local meal expenses separately from travel expenses and monitor the reasonableness of the Director and staff's local meal expenses on a monthly basis. Documentation of meal expenses should provide a detailed description of business purpose, identifying participants by name, business or type of business, if confidential, and include itemized receipts for every meal event.

TCEDA Disclosures and Interactions with Private Businesses Are Managed by County Counsel

Companies negotiating or working with economic development authorities such as TCEDA may ask for confidentiality for specific legal reasons during negotiations. For example, businesses may share strategic plans or proprietary information that they may not want disclosed to the public, or premature release of information could possibly terminate the project. Funding and/or incentives could be lost, a neighboring EDO could offer a better package, or a land owner may increase the price of their property if the location plan is leaked. While confidentiality may be imperative during the early stages of negotiations, the tracking and reporting of business contacts are important for both performance metric reporting and transparency. With the understanding that TCEDA may wish to keep some business contact information private, at least early on in the process, Tuolumne County Counsel explained that the County handles its disclosures of information considered confidential and proprietary on a case-by-case basis and relies heavily on the California Public Records Act, which states that governmental records shall be disclosed to the public, upon request, unless there is a specific reason not to do so. Consistent application of this exception requires standards or guidelines to ensure disclosures are appropriate and applied across the organization.[1]

TCEDA Tracked and Reported Fewer Performance Metrics than Peers

We reviewed the performance metrics and management reporting provided by the Madera County Economic Development Commission (MCEDC), and Siskiyou Economic Development Council (SEDC), and compared them to TCEDA. We were unable to locate performance metrics or management reporting provided by a third entity, the Economic Development Corporation of Mariposa County.

Our review of the two comparable agencies found a wide variety of performance metrics. While there was minimal overlap, TCEDA fell short in comparison. Tracking the number of businesses contacted was a common element for each economic development organization (EDO) reviewed; MCEDC, SEDC, and TCEDA each track performance metrics related to the number of businesses assisted by the EDO. The TCEDA did not, however, collect other metrics used by peer entities, such as the number of site requests made by businesses, the industrial vacancy rate, the amount of

[1] We were originally tasked to review and compare TCEDA's disclosure practices with Tuolumne County and the City of Sonora. However, neither entity had written standards/guidelines on disclosures regarding interactions with private businesses.

funds invested in the economy, and finally, TCEDA does not calculate return on investment (ROI) based on the EDO's funding and the resulting public/private investment ratio.

While TCEDA metrics and management reporting are not far out of line with comparable agencies, such metrics and reporting used do not conform to contemporary best practices for EDOs. The performance of an EDO can be difficult to measure due to the wide number of other inputs to economic development that are not directly within its control, and because results of its activities may not be apparent for years after EDO efforts are made.

However, there are a wide variety of potential metrics that can be used to measure performance by an EDO. We reviewed data on EDO performance metrics provided by the California Association for Local Economic Development (CALED), the International Economic Development Council (IEDC), and SRI International, in partnership with the Economic Development Administration (EDA). Each entity provided a menu of options within a variety of categories. Relevant categories and options provided include economic measures (commercial investment, amount/percentage of tax collected by industry, dollars spent in locally-owned businesses, tourism/bed tax revenues), labor and workforce measures (net job growth, average salaries, employment by sector), and business measures (new businesses started, manufacturing productivity, growth in number of clusters identified in comparison to previous year, or compared to state growth of same cluster). The metrics used by TCEDA were clustered within the business measures category and did not include metrics from the economic measures or labor and workforce categories. The metrics used by TCEDA are also clustered around the engagement of TCEDA with businesses (contacts or visits with existing businesses, out-of-county businesses, and new businesses) rather than external, objective measures.

Recommendation

The Governing Board should update its work plan for the TCEDA to provide a select set of performance metrics that encompass a variety of different measurements, and use CALED resources as a guide. These metrics should be selected based upon the goals set for TCEDA by the Board and should include clear, discrete, and measurable goals that can be tracked over time. The results of these performance metrics should be provided in regular updates to the Board through TCEDA reporting. The Board should review and discuss results regularly, including an evaluation of the success of the selected metrics in measuring performance.

Personal Leave Accrual and Cash Out Rules Were Not Followed

The County's Executive/Confidential Compensation Plan is the governing document and contains conditions of employment which contain rules over time-keeping and personal leave accrual cash out rules applicable to the TCEDA Director. Our review of the Director's time report, calendar, and email correspondence noted deviations from the employment agreement and from the Executive/Confidential Compensation Plan.

While the County's Executive/Confidential Compensation Plan requires the use of 80 hours of leave time within the fiscal year prior to approval of a request for personal leave accrual cash out, we found that a payout to the Director was made without the required formal request and use of leave time. In addition, the County's Executive/Confidential Compensation Plan requires that the request shall be in the form of a memorandum to the Auditor-Controller's office. Our review found that the TCEDA Director was paid for personal leave cash out before using 80 hours of leave within the fiscal year. We also found no evidence of a memorandum submitted by the Director to the Auditor-Controller's office to request the payout as required. Discussion with the Auditor-Controller noted that the customary practice within the County to request personal leave cash out is done primarily by email; however, there was no record of such an email request submitted by the former Director.

Multiple Inconsistencies between the TCEDA Director's Reported Time and Outlook Calendar were identified

Although the Compensation Plan does not require the Director to maintain an Outlook calendar that mirrors what is entered into the time keeping system, it is reasonable to suppose that there should be some consistency among time-keeping reports and activities reflected in the Director's calendar during the same time period. Upon our review of calendar year 2017, we noted inconsistencies between the TCEDA Director's time report and his calendar activities for at least 16 days. For example, on September 18-21, 2017, the Director's calendar showed "comp time, England," while the time reported was eight regular working hours for each day. Another example occurred on October 6, 2017. The time reflected on the calendar was "remote working, England," while the time report showed eight hours of vacation time. As part of the agreement with TCEDA upon the Director's separation, the cash value of 80 hours of PTO was returned.

A copy of this report has been provided to the TCEDA Board of Directors and to Tuolumne County Auditor-Controller.

This report is intended solely for the information and use of the County, the City, and the TCEDA Board of Directors, and is not intended to be and should not be used by anyone other than these specified parties.

Macias Gini & O'Connell LLP

Sacramento, California
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