



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 West Covina**

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 West Covina.

Located approximately 19 miles east of Los Angeles, West Covina has a population of more than 110,000. 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. City staff provide services including law enforcement, fire protection, street construction and maintenance, recreational and cultural activities, public improvements, planning, and general administrative services.

In October 2019, my office identified West Covina as the 17<sup>th</sup> most fiscally challenged city in California primarily because it had insufficient financial reserves and a compromised ability to pay for employee retirement benefits. My office subsequently conducted an onsite assessment in early January 2020 and determined that West Covina is potentially a high-risk entity as its financial reserves have continued to steadily decline, potentially straining the city’s ability to pay its bills in the event of declining revenues or increasing costs. The city’s audited financial statements report general fund revenue of \$67.2 million for fiscal year 2017–18. However, over the past several fiscal years, the city’s expenditures have at times exceeded its revenues. Likely because of this, the city’s general fund reserves declined from \$20.5 million in fiscal year 2014–15 to \$12.3 million at the end of fiscal year 2017–18, a 40 percent decrease. In addition, although the city has not yet released its audited financial statements for fiscal year 2018–19, city management anticipates that general fund expenditures once again exceeded its revenues, likely resulting in a further reduction in its financial reserves.

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Furthermore, West Covina's unfunded pension liability of \$185 million is very high compared to its annual revenues, and it has only set aside a portion of the funding it will need to pay for the pension benefits already earned by its employees. Its growing pension costs will also put additional pressure on its finances. Specifically, the city's required contribution to its pension plan was \$12.9 million in fiscal year 2016–17, and the California Public Employees' Retirement System projects that the city's annual required contribution will increase 77 percent to \$22.8 million by fiscal year 2024–25. Similarly, West Covina has an unfunded liability for retiree health and other postemployment benefits of \$59.9 million and has not set aside any funds to pay for these benefits.

In spite of its declining financial reserves and increasing costs, the city has not produced a budget beyond the current year that forecasts its projected revenues and expenditures in future years. In 2015, the State Controller's Office (SCO) also reported serious and pervasive weaknesses in West Covina's administrative and internal accounting controls, concluding that such controls, were in effect, non-existent. Finally, the city has experienced turnover in its key management positions, including city manager, finance director, human resources director, and fire and police chiefs.

An audit of the City of West Covina will help address the following questions:

- What is causing West Covina's financial challenges and does it have an adequate plan for addressing those challenges?
- Are West Covina's financial challenges affecting its ability to pay its bills when due or impacting its ability to provide services to its residents?
- Do West Covina's budgeting processes, including its procedures for projecting future revenues and expenditures, comply with best practices and result in accurate budgets?
- Has West Covina addressed the deficiencies the SCO identified in its 2015 report?
- What effort is West Covina making to ensure that key management and staff positions are filled with qualified candidates?

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