



**State of Arizona
Office
of the
Auditor General**

PERFORMANCE AUDIT

**PINAL COUNTY
TRANSPORTATION
EXCISE TAX**

**Report to the Arizona Legislature
By Douglas R. Norton
Auditor General
March 1998
Report Number 98-8**



DOUGLAS R. NORTON, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

DEBRA K. DAVENPORT, CPA
DEPUTY AUDITOR GENERAL

March 30, 1998

Members of the Arizona Legislature

The Honorable Jane Dee Hull, Governor

Transmitted herewith is a report of the Auditor General, A Performance Audit of the Pinal County Transportation Excise Tax. This report is in response to a May 27, 1997, resolution of the Joint Legislative Audit Committee and was conducted under the authority vested in the Auditor General by A.R.S. §41-1279.03

The report addresses the extent to which the transportation excise tax has helped solve Pinal County's transportation problems. Pinal County voters approved the tax in 1996 to "provide additional funding for the construction, reconstruction, maintenance, repair and roadside development of County, city and town roads, streets, and bridges." To date, the excise tax has had varying levels of impact in solving Pinal County's transportation problems. First, while the tax was estimated to generate between \$125 million to \$200 million before it expires in the year 2006, actual revenues have fallen short of projected revenue by at least \$1 million each year since 1988 and over \$2 million each year since 1993. Despite the shortfall in tax revenues we found that the Pinal County Department of Civil Works has effectively used its portion of transportation excise tax revenues expending 90 percent of these monies on new road construction and reconstruction projects. It is more difficult to assess the impact the excise tax has had on the ability of Pinal County's cities and towns to address their road needs. An analysis of road fund revenues and expenditures for these municipalities reveals that many are not using all the "additional monies" the excise tax was intended to provide. In fact, our analysis suggest that most of the cities and towns have spent 60 percent or less of their excise tax revenue.

Although Arizona statutes restrict use of these monies for highway, street and transportation purposes, our review also discovered that three municipalities have inappropriately loaned transportation excise tax and other road money to other funds. While one entity has since repaid the monies, the second municipality had an outstanding balance of \$419,150, and the third municipality had an outstanding balance of \$24,429.

Pinal County and the eight incorporated cities and towns were provided an opportunity to submit responses to this report. Only the City of Eloy, and the towns of Mammoth and Florence chose to do so. As outlined in their responses, these entities agree with the report recommendations.

My staff and I will be pleased to discuss or clarify items in the report.

This report will be released to the public on March 31, 1998.

Sincerely,

Douglas R. Norton
Auditor General

Enclosure

SUMMARY

The Office of the Auditor General has conducted a performance audit of the Pinal County Transportation Excise Tax. This audit was conducted under the authority vested in the Auditor General by Arizona Revised Statutes (A.R.S.) §41-1279.03 and pursuant to a May 27, 1997, resolution of the Joint Legislative Audit Committee.

In 1986, the residents of Pinal County voted to pass a half-cent sales tax to... *“provide additional funding for the construction, reconstruction, maintenance, repair and roadside development of County, city and town roads, streets and bridges.”* The excise tax became effective January 1, 1987, and is to remain in effect for a period of 20 years. In the first 10 years of the excise tax’s existence, it has generated nearly \$40 million in revenues for roads and highways in Pinal County. This revenue is shared between 8 incorporated cities and towns and the County, which is responsible for unincorporated roads. The tax is distributed to each entity according to a population-based formula. Currently, cities and towns receive 57 percent of the tax revenue while the County receives the remaining 43 percent.

Tax Has Provided Differing Levels of Impact **(See pages 5 through 10)**

The transportation excise tax has had varying levels of impact in solving Pinal County’s transportation problems. First, the tax has not generated as much additional revenue as anticipated. While the tax was estimated to generate between \$125 million to \$200 million before it expires in 2006, actual revenues have fallen short of projected revenue by at least \$1 million each year since 1988 and over \$2 million each year since 1993. Consequently, to date, the tax has yielded only 65 percent of original projections.

Despite the shortfall in tax revenues, the Pinal County Department of Civil Works has effectively used its portion of transportation excise tax revenues to build new roads and reconstruct existing roads. A review of road projects completed between fiscal years 1995 and 1997 confirmed that the County spent over \$10 million on road projects using excise tax monies, with 90 percent of these monies expended on new road construction and reconstruction projects. However, even with the excise tax revenues, the County’s estimated road needs are still expected to exceed revenues. According to a 1995 transportation needs assessment, County road needs total over \$98 million for fiscal years 1996 through 2000, yet the County can expect to receive only approximately \$51 million during that same time period in primary stable funding (i.e., road revenue that has been consistently received over fiscal years 1992-1996).

Although the cities and towns, like the County, also have substantial road needs, it is more difficult to assess the impact the excise tax has had on their ability to address these needs. The cities and towns have used excise tax revenues for various road projects, including new road construction and reconstruction, pavement preservation, and maintenance. However, an analysis of road fund revenues and expenditures since the inception of the tax reveals that many of the cities and towns are not using all the “additional monies” the excise tax was intended to provide. Specifically, the cities and towns received nearly \$18 million in excise tax revenues from fiscal years 1987 through 1996 while during that same period increasing road fund balances of approximately \$7 million. The difference between total excise tax revenues received and the increase in fund balances for each municipality suggests that most have, in effect, spent 60 percent or less of their excise tax revenue. Despite the high fund balances, most of the cities and towns within Pinal County have road needs that exceed available revenue.

Specifically, cited road needs for Pinal County’s cities and towns total over \$79 million for fiscal years 1996 through 2000, yet primary stable road monies for that same time period are estimated to be only \$59.4 million. Although projected revenue will not likely address all transportation problems, some cities and towns appear to have large enough fund balances to address at least some existing road needs.

Some Municipalities Have Inappropriately Used Road Monies (See pages 11 through 13)

While Arizona statutes explicitly limit expenditure of road revenues for highway, street, and transportation purposes, three of Pinal County’s cities and towns have inappropriately borrowed transportation excise tax and other road money from their road funds and loaned it to other funds. Specifically, over the past several years, the municipalities of Eloy, Mammoth, and Florence have inappropriately loaned road monies to other funds primarily to pay for general and enterprise fund expenditures and expenses. For example, since at least 1987, the City of Eloy has loaned road monies primarily to its enterprise funds to cover an excess of expenses over revenues for its utility services and golf course enterprises. Until recently, the amount of road monies loaned had increased and as of June 30, 1997, the outstanding balance totaled approximately \$419,150.

The municipalities mentioned above should take two actions to comply with statutes governing the use of road monies.

- **First**—They should immediately cease using road monies for non-road purposes. While Florence ceased this practice and repaid its outstanding loan in 1995, Eloy and Mammoth are still inappropriately loaning road monies.

- **Second**—Eloy and Mammoth should promptly repay to their road funds all outstanding amounts of monies inappropriately borrowed. As of fiscal year 1997, Eloy still owed \$419,150 and Mammoth owed \$24,429.

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INTRODUCTION AND BACKGROUND

The Office of the Auditor General has conducted a performance audit of the Pinal County Transportation Excise Tax. This audit was conducted under the authority vested in the Auditor General by A.R.S §41.1279.03 and pursuant to a May 27, 1997, resolution of the Joint Legislative Audit Committee.

Background on the Excise Tax

In 1986, the residents of Pinal County voted to pass a half-cent sales tax to “*provide additional funding for the construction, reconstruction, maintenance, repair and roadside development of County, city and town roads, streets and bridges.*” As of fiscal year 1997, the tax generated a total of \$39,690,732 in revenues for roads and highways in Pinal County, which is one of only three counties to pass such a tax. The excise tax comprises approximately 29 percent of primary stable funding for roads in the cities and towns and 25 percent of primary stable road funding for the County.¹

Revenue from the transportation excise tax (excise tax) is shared between eight incorporated cities and towns and the County, which is responsible for unincorporated roads. While the monies are collected by the Department of Revenue and passed through the State Treasurer, the Pinal County Treasurer actually distributes excise tax revenue to the County, cities, and towns according to a population-based formula. Currently, cities and towns receive 57 percent of the tax revenue while the County receives the remaining 43 percent.

Road Funding in Pinal County

All eight cities and towns rely on revenue from the excise tax, the Highway User Revenue Fund (HURF), and the Local Transportation Assistance Fund (LTAF) as their primary, stable sources of road funding.² Although the municipalities may also receive road monies through federal and state sources, such as the Community Development Block Grant Program, Federal-Aid Highway Construction Program, and Economic Strengths Project Fund, these monies are typically competitive and, therefore, not reliable from year to year.

¹ Primary stable funding is defined as revenue, excluding grants, that has been consistently received. These revenues have comprised over 75 percent of total road funding over fiscal years 1992-1996.

² HURF monies are primarily generated through a gas tax while LTAF monies are lottery proceeds earmarked for transportation purposes.

The County relies on the excise tax and HURF for its primary stable road funding. In addition, a small percentage of road monies is generated through license fees, private contributions, map sales, etc. Finally, like the cities and towns, the County may also receive funding through state grants and federal assistance programs. Again, because such funding is competitive, it is not considered reliable from year to year.

Road operations in each of the nine entities (County and eight municipalities) receiving the tax vary significantly depending on the number of road miles maintained, as well as the amount of road revenue received each year. For example, as illustrated in Table 1, the County, which maintains 1,851 miles of unincorporated roads, received approximately \$9.8 million in primary stable road funding in fiscal year 1997. In contrast, the most populated city in Pinal County, Casa Grande, maintains 175 miles of road and received \$2.7 million in primary stable road funding in fiscal year 1997. Likewise, Mammoth, the smallest of the municipalities, maintains 11 miles of road and received \$257,321 in primary stable road monies in fiscal year 1997.

Table 1

**Pinal County Transportation Excise Tax Recipients
Year Ended June 30, 1997
(Unaudited)**

Excise Tax Recipient	1990 Population	Miles Maintained	Excise Tax Distribution	Primary Stable Road Funding¹
Pinal County (unincorporated)	50,143	1,851	\$2,150,674	\$ 9,788,807
Casa Grande	19,082	175	818,734	2,710,783
Apache Junction	17,931	167	769,310	2,545,268
Florence	7,510	40	322,002	1,355,619
Eloy	7,211	311	309,521	1,118,042
Coolidge	6,927	32	297,041	936,527
Superior	3,468	20	148,770	464,950
Kearny	2,262	14	96,850	318,941
Mammoth	<u>1,845</u>	<u>11</u>	<u>79,377</u>	<u>257,321</u>
Total	<u>116,379</u>	<u>2,621</u>	<u>\$4,992,279</u>	<u>\$19,496,258</u>

¹ Primary stable road funding consists of excise tax, HURF, and LTAF monies for the cities and towns, and excise tax and HURF monies for the County.

Source: Population figures from the Pinal County Elections Department; road miles from the Arizona Department of Transportation and each entity; and revenue amounts derived by Auditor General staff analysis of County and State Treasurer data.

Audit Scope and Methodology

This audit was conducted in response to A.R.S §41-1279.03, which requires a performance audit in the tenth year and every third year thereafter in counties where a transportation excise tax is in effect. Specifically, the statute requires a review of past and future planned expenditures and road projects to determine their impact on solving transportation problems.

The law also requires a review of HURF distributions to ensure compliance with A.R.S. §28-1598. Because this information was included in the July 1997 Maricopa County Regional Freeway System performance audit report, it was not addressed in this audit.

This review of the excise tax was limited due to the practice of most cities and towns to commingle their excise tax revenue with other road monies, such as the HURF and LTAF. Because all three revenue sources are restricted in their use to road purposes only, most cities and towns combine them into one fund to finance road projects. As such, isolating excise tax expenditures and road projects from the other funding sources was not possible. As a result, this report deals with primary stable “road monies,” which include the excise tax, HURF and LTAF for the cities and towns, and the excise tax and HURF for the County.

In addition, some of the nine entities were unable to provide detailed expenditure and project information since the inception of the tax. Consequently, auditors’ analysis of detailed expenditures was limited primarily to fiscal years 1994 through 1997, the time period for which data was obtained for all of the entities. Similarly, this analysis of project data was limited to fiscal years 1995 through 1997 since some of the cities, towns, and the County could not provide this information prior to fiscal year 1995.

Several methods were used in this analysis of past and future planned expenditures and road projects, including:

- Reviewing general purpose financial statements and reports on compliance and the internal control structure from fiscal years 1987 through 1996 to determine if road monies were used appropriately (for road purposes);
- Reviewing project data, city council, and county board of supervisor meeting minutes from 1995 through 1997 and interviewing public works personnel and city management officials to determine the types of road projects completed by the nine entities;
- Accompanying personnel from the County and three municipalities to observe road projects financed by road monies and to view existing road needs; and

- Examining planning, capital improvement, and budget documents to identify road needs and the efforts made to address such needs.

This report presents findings and recommendations in two areas:

- The impact of road monies on the County's, cities', and towns' ability to address transportation problems; and
- The need for some cities and towns to discontinue the practice of inappropriately loaning road monies to other funds for non-road purposes.

This audit was conducted in accordance with government auditing standards.

The Auditor General and his staff express appreciation to the Director and staff of the Pinal County Department of Civil Works; and the management and staff of the following municipalities: Apache Junction, Casa Grande, Coolidge, Eloy, Florence, Kearny, Mammoth, and Superior for their cooperation and assistance throughout the audit.

FINDING I

TAX HAS PROVIDED DIFFERING LEVELS OF IMPACT

The transportation excise tax has had varying levels of impact in solving Pinal County's transportation problems. Although the tax has not generated as much additional revenue as anticipated, the County has effectively used excise tax revenues to build new roads and reconstruct existing roads. However, the impact of the excise tax on the eight cities and towns is less clear, with many of them spending only a portion of their primary stable road funding over the last ten years.

Excise Tax Revenues Fall Short of Projections

Although the publicity pamphlet prepared for Pinal County voters in 1986 described the road tax as "*additional funding for the construction, reconstruction, maintenance, repair and roadside development of County and town roads, streets and bridges,*" the tax has not generated as much "additional" funding as originally anticipated. While the excise tax was estimated to generate between \$125 to \$200 million before it expires in 2006, actual revenues have fallen short of projected revenue by at least \$1 million each year since 1988, and over \$2 million each year since 1993. Consequently, excise tax revenue, which was projected to yield a total of \$61 million from fiscal year 1987 to fiscal year 1997 to assist the County, cities, and towns with their road needs, has reached only \$40 million, or about 65 percent of projections.

For the County, the excise tax has provided even less "additional funding" because it essentially replaced a primary source of road funding soon after it was implemented. Prior to the inception of the excise tax, the County's Department of Civil Works relied primarily on Highway User Revenue Fund (HURF) allotments and property taxes earmarked for roads as its main funding sources. However, one year after the excise tax was implemented, County supervisors began reducing property taxes dedicated for roads. By 1989, the property tax as a source of road funding was eliminated altogether, leaving only HURF and the excise tax as the County's primary stable revenue sources for roads. The portion of property taxes earmarked for roads would have yielded an additional \$12.7 million from fiscal years 1988 to 1997 for the County had it not been eliminated.¹

¹ This figure is based on a property tax rate of 25 cents per \$100 valuation, which was in existence prior to the reduction and eventual elimination of the tax.

County Uses Excise Tax for New Road Construction and Reconstruction

Despite the shortfall in tax revenues, the Pinal County Department of Civil Works has effectively used its portion of transportation excise tax revenues to build new roads and reconstruct existing ones. Although the County has used 90 percent of its primary stable road monies to address transportation problems, road needs continue to exceed available revenue.

Excise tax helps County build new roads and reconstruct existing ones—The excise tax, which comprises approximately 25 percent of the County’s primary stable road funding, has helped the County address transportation problems by funding the construction of new roads and the reconstruction of existing ones. The County earmarked these monies primarily for new road construction and reconstruction soon after the tax was passed, leaving the HURF monies to pay for maintenance and most pavement preservation projects. In 1989, the Department of Civil Works created a Transportation Advisory Committee (TAC) for each of the County’s three districts to oversee excise tax expenditures as well as to increase citizen participation. These committees, composed of seven public members, are responsible for assisting the Department of Civil Works in prioritizing road projects, with the County Board of Supervisors giving final approval.

A review of road projects completed between fiscal years 1995 and 1997 confirmed that the County did, in fact, spend most of its excise tax monies during this period on new road construction and reconstruction projects.¹ Overall, the County spent \$10,088,604 on road projects financed with excise tax monies with 90 percent of these monies being expended on new road construction and reconstruction projects.² Table 2 (see page 7) provides examples of projects completed with the excise tax monies during this time period.

In addition to financing new road construction and reconstruction for the County, the excise tax has also enabled the Department of Civil Works to generate additional revenue from external sources for road projects. For example, the County was able to provide almost \$3.5 million of improvements to the Maricopa-Casa Grande Highway with only \$450,000 of County money because of external support from the Federal Highway Administration, the City of Casa Grande, and private business. According to the director of the Pinal County Department of Civil Works, the availability of the excise tax was critical to securing these external monies.

¹ The County was unable to provide road project records prior to fiscal year 1995.

² This figure includes jointly funded projects.

Table 2

**Examples of Pinal County Road Projects
Funded with Excise Tax Monies
Years Ended June 30, 1995 through 1997
(Unaudited)**

Location	Length in Miles	Problem	Solution	Cost of Project
Russell Road	0.8	Deteriorated surface	Reconstruct paved surface	\$138,036
McCartney Road Phase 1 and 2	2.0	Access road to Casa Grande's new high school	Construct new road	\$305,103
Val Vista Road Apache Junction	0.9	Poor access and drainage	Pave dirt road and install box culverts	\$265,240

Source: Pinal County Department of Civil Works' project records.

Excise tax will not likely help the County address all transportation problems—While the County has effectively used its road monies to address transportation problems, its estimated road needs are still expected to exceed available revenues. The Arizona Department of Transportation (ADOT) sends out a survey to all counties, cities, towns, tribes, and certain federal agencies in the State every five years to determine their road needs for the upcoming decade. This survey serves as a method of identifying road needs and future planned road projects. According to the 1995 transportation needs assessment, the County cited road needs totaling \$98,535,670 for fiscal years 1996 through 2000, many of which are to correct deteriorated surfaces on existing roads. However, revenue projections indicate the County can expect to receive only \$50,890,370, or 52 percent of what is needed in primary stable funding during that same period to address these needs.

Impact of Tax Revenues on Cities and Towns Less Clear

Although the cities and towns, like the County, also have substantial road needs, it is more difficult to assess the impact the excise tax has had on their ability to address these needs. The cities and towns have used road monies for multiple purposes; however, a review of road revenues and expenditures revealed that many have not used all of their available road monies, instead accumulating large fund balances. These fund balances exist in spite of significant existing road needs.

Cities and towns use smaller portion of road monies—While the cities and towns within Pinal County have used road monies to some degree to address road needs, many are not using all the “additional monies” the excise tax was intended to provide. As illustrated in Table 3, the cities and towns have used their road monies for a variety of purposes.

Table 3

**Pinal County Municipalities
Major Use of Primary Stable Road Monies
Years Ended June 30, 1995 through 1997¹
(Unaudited)**

Municipality	Major Use ²
Casa Grande	New construction and reconstruction
Apache Junction	New construction and pavement preservation
Florence	Drainage and reconstruction
Eloy	Road maintenance
Coolidge	Reconstruction and pavement preservation
Superior	Pavement preservation
Kearny	Road maintenance
Mammoth	Road maintenance

¹ Excludes operating expenditures.

² Road project definitions obtained from the *Manual of Highway Improvement and Maintenance Costs*, Arizona Department of Transportation, December 1993.

Source: Auditor General staff analysis of Pinal County city and town road project records, audited financial reports, unaudited financial statement worksheets, and city and town council minutes.

However, an analysis of road fund revenues and expenditures since the inception of the tax reveals that the cities and towns received \$17,944,135 in excise tax revenues from fiscal years 1987 through 1996 while at the same time increasing fund balances by \$7,045,309 for the same time period.¹ As illustrated in Table 4 (see page 9), the difference between total excise tax revenues received and the increase in fund balances from fiscal years 1987-1996 for each municipality suggests that most have, in effect, spent 60 percent or less of their excise tax revenue. For example, the Town of Florence received \$2,207,569 in excise tax revenue from fiscal years 1987 through 1996. However, during the same time period, its fund balance increased

¹ Fund balances are made up of unexpended revenues from HURF, LTAF, and excise tax. The revenues received and fund balance amounts are based on only six of the eight cities and towns since auditors were unable to obtain a full ten-year fund balance history for the Towns of Kearny and Superior.

by \$1,270,097, suggesting it expended only 43 percent of the “additional monies” the excise tax provided.

Table 4

**Pinal County Municipalities
Percentage of Additional Monies Expended
Years Ended June 30, 1987 through 1996
(Unaudited)**

Municipality	Excise Tax Revenue Received	Percentage Expended
Apache Junction	\$5,216,219	81%
Casa Grande	\$5,633,395	60
Mammoth	\$579,647	57
Coolidge	\$2,192,831	56
Florence	\$2,207,569	43
Eloy	\$2,114,474	38

Source: Auditor General staff analysis of municipalities’ audited annual financial reports and Pinal County Treasurer’s excise tax distribution data.

Reasons for not spending more of the road monies vary from city to city. Some city and town managers indicated that they save the road monies in order to pay for large projects in the future. While auditors’ analysis of fund balances confirms this pattern to some degree, fund balances are still significant even after high spending years. Other city managers indicated they save the monies for emergencies, while others could provide no clear explanation as to why they have not spent more of their available revenue.

Cities and towns also faced with numerous road needs—Despite the high fund balances maintained by some of the cities and towns, most have road needs that exceed available revenue. The 1995 ADOT transportation needs assessment cited road needs for Pinal County’s cities and towns totaling \$79,334,345 for fiscal years 1996 through 2000. Yet primary stable road monies for that same time period are estimated to be only \$59,402,223, or 75 percent of anticipated needs.¹

Although projected revenue will not likely address all transportation problems, some cities and towns appear to have large enough fund balances to address at least some existing road needs. For example, results from a 1995 citizen survey conducted in Mammoth by the

¹ This figure also includes fund balances for seven of the eight municipalities as of June 30, 1995. The Town of Kearny’s 1995 ending fund balance was unavailable.

Central Arizona Association of Governments (CAAG) cited street improvements as the Town's most important need. Likewise, a 1996 Economic Development Program report produced by CAAG listed Mammoth's transportation needs as urgent, requiring \$900,000 in street improvements throughout the Town. With the Town's fiscal year 1996 ending fund balance of \$317,083, one-third of its urgent needs could have been met. In addition, of the projects cited in ADOT's 1995 transportation needs assessment, five of the eight cities and towns had at least three "backlogs" or projects that have been needed but not completed since the last survey in 1990. One city with a fund balance of over \$1 million in fiscal year 1996 had 45 backlogged projects, with many individually costing under \$200,000. Another city had 21 backlogged projects and a fund balance in fiscal year 1996 of \$2.2 million.¹

Recommendation

This chapter provides information only. Therefore, no recommendations are presented.

¹ The County also has backlogged projects listed on the 1995 transportation needs assessment. However, because it has expended 90 percent of its primary stable road funding over the last three years to address its road needs, large, unused balances do not appear to be a problem.

FINDING II

SOME MUNICIPALITIES HAVE INAPPROPRIATELY USED ROAD MONIES

Three of Pinal County's cities and towns inappropriately loaned transportation excise tax and additional road monies to other funds. Specifically, the municipalities established interfund loans to funds with non-road purposes despite statutory restrictions on the use of these monies. To ensure compliance with the law, the municipalities should restrict the use of road monies to statutorily allowed purposes and also repay their road funds any outstanding amounts they had loaned to other funds for non-road purposes.

Statutes Restrict Use of Road Monies

As noted earlier, the eight incorporated cities and towns within Pinal County have three primary stable sources of road revenue: the excise tax, the Arizona Highway User Revenue Fund (HURF) allotment, and the Local Area Transportation Assistance Fund (LTAf) allotment. Arizona statutes explicitly limit expenditure of these monies for highway, street, and transportation purposes. Specifically, A.R.S. §28-6392 states that the excise tax monies may only be used for *“street and highway purposes or for transportation projects included in the regional transportation plan of the county...”* Similarly, A.R.S. §28-8102 restricts LTAf monies for transportation purposes.¹ Finally, A.R.S. §28-6533 stipulates that HURF monies may only be expended for highway and street purposes as prescribed in Article IX, §14 of the Constitution of Arizona, which include *“costs of rights-of-way acquisitions and expenses related thereto, construction, reconstruction, maintenance, repair, roadside development, of county, city, and town roads, streets, and bridges and payment of principal and interest on highway and street bonds.”*

As these revenue sources are restricted for similar purposes, several of the cities and towns commingle them into one fund to pay for road projects. Consequently, road expenses paid for out of the fund may be financed by more than one revenue source. Thus, it is not possible to determine the extent to which the excise tax, specifically, was inappropriately used. Regardless, all three sources of road monies are still similarly restricted for highway, street, and transportation purposes.

¹ A.R.S. §28-8103 allows a city or town to authorize by resolution the use of up to 10 percent of its LTAf monies in any one fiscal year for cultural, educational, historical, recreational, or scientific facilities or programs for nonresidential outpatient programs or services for developmentally disabled persons if the monies are matched equally by nonpublic monies received by the city or town and expended for the same purposes.

Municipalities Using Road Revenue for Non-road Purposes

Over the past several years, the following three municipalities have inappropriately loaned road monies to other funds, primarily to pay for general and enterprise fund expenditures and expenses:

- **Eloy**—Since at least 1987, the City of Eloy has loaned road monies primarily to its enterprise funds to cover an excess of expenses over revenues. Specifically, the City loaned road monies to the utility services and golf course enterprises. The revenues for these two enterprises failed to meet operating expenses and the annual payment on a \$3.8 million bond for the golf course. Until recently, the amount of road monies loaned to these funds had increased and reached a peak of \$741,350 in fiscal year 1996. However, as of June 30, 1997, the outstanding balance had been reduced to \$419,150. The City raised utility rates in 1996 and is currently exploring options for selling the golf course in an attempt to alleviate this problem. However, over the last four fiscal years, the utility services and golf course enterprise funds have lacked the resources to repay the loans and have ended each fiscal year with deficit retained earnings.
- **Mammoth**—Since 1991, the Town of Mammoth has loaned road monies primarily to its general fund to cover an excess of expenditures over revenues. In 1994, the Town instituted a 2 percent sales tax in an effort to alleviate this shortfall. Until recently, the amount of road monies loaned to the general fund had typically increased each year, reaching a peak of approximately \$300,000 in fiscal year 1996. However, as of June 30, 1997, the outstanding balance of road monies loaned for non-road purposes was reduced to \$24,429.
- **Florence**—Although the Town of Florence has since repaid the monies borrowed from its road fund, between 1987 and 1994 it also loaned road monies, primarily to its general fund. Loans were made even though the general fund had the assets to cover annual expenditures for every year except one. End-of-fiscal year balances for these loans ranged from approximately \$121,000 to \$797,000. Current Town personnel could not provide a specific reason for the loans, but indicated that the practice ended in 1995 with a change in Town personnel.

Municipalities Should Comply with Statutory Restrictions Governing Road Monies

The municipalities should take two actions to comply with statutes governing the use of road monies.

- **First**, they should immediately cease using road monies for non-road purposes. While Florence ceased this practice and repaid its outstanding loan in 1995, Eloy and Mammoth are still inappropriately loaning their road monies for non-road purposes.
- **Second**, Eloy and Mammoth should promptly repay to their road funds all outstanding amounts of monies they have inappropriately borrowed. As of fiscal year 1997, Eloy still owed \$419,150 and Mammoth owed \$24,429. If monies are not available to immediately and completely repay the road monies, the municipalities should develop and implement a repayment schedule.

Recommendation

To comply with statutory requirements, Eloy and Mammoth should promptly:

- Discontinue the practice of using road monies for non-road purposes; and
- Repay inappropriately borrowed road monies. If resources are not currently available to completely repay loans, a repayment schedule should be developed and implemented.

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Agency Response



City of Casa Grande

March 23, 1998

Mr. Douglas R. Norton
Auditor General
2910 North 44th Street
Suite 410
Phoenix, AZ 85018

Dear Mr. Norton:

The City of Casa Grande is in receipt of the preliminary report of the Pinal County Transportation Excise Tax Report. This report is based on the compliance audit conducted under the authority vested in the Auditor General by Arizona Revised Statutes to review cent excise tax monies. The City of Casa Grande does not agree with the findings of the Auditor General, and there were no recommendations to be implemented.

The City of Casa Grande receives HURF, LTAF, and excise tax funds which are accounted for in a special revenue fund. Because of the purpose of the funds, all monies are accounted for in one fund. The special revenue fund, however, is segregated to account for the revenues and expenditures separately because of the specific purpose for each type of revenue source. The City uses HURF funds to maintain the existing 175 miles of streets. LTAF is used in either maintenance or reconstruction with ten percent going to cultural arts. Excise tax funds are used for new construction and reconstruction only.

Road construction and reconstruction vary in cost ranging from hundred thousands to millions of dollars. The City of Casa Grande has received an increasing amount of excise tax funds ranging from \$200,000 to \$800,000 per year. The City's most recent project was over \$1.8 million in which took over two years to accumulate enough funds for the project. Depending on what point in time you look at the City's fund balance, you may find an accumulation of funds. This practice is necessary due to the expense of the projects.

The preliminary report suggests the scope of the audit to be through the recent fiscal year 1997 yet Table 4 "Pinal County Municipalities Percentage of Additional Monies Expended" is only through 1996. Most of the numerical statements or statistics are also only through 1996. If taken through 1997, you would find the City of Casa Grande spending over \$1.8 million on construction and reconstruction, thereby depleting any excess excise tax funds. The report incorrectly infers the total increase in fund balance to belong to excise tax thereby obtaining a percentage of

unspent excise tax. Reiterating, the fund balance belongs to all revenue sources HURF, LTAF and excise tax. The funds are for specific purposes and are segregated. HURF's portion of the fund balance needs to maintain the City's 175 miles of streets. The report implies that all of the fund balance is available for construction/reconstruction. Another erroneous assumption in the report is that the City has backlogged projects costing \$100,000 - \$1,000,000 and that the fund balance should be used on the less costly projects first. City staff and Council may have deemed a multi-million dollar project more urgent and a more efficient use of resources.

I have attached a schedule for excise tax funds since 1986 showing excise tax revenues, interest earnings and excise tax expenditures. Assuming we spend interest earnings first, the schedule shows at the end of fiscal year 1997 that the City of Casa Grande had 2.94 percent of excise tax monies available. Concluding the City has used over 97 percent of our allocated excise tax funds. The preliminary report states the City of Casa Grande has spent 60 percent of allocated excise tax funds.

The preliminary report is misleading in that part of the report covers through 1997 and yet some of the numerical values or statistics are only through 1996. Some assumptions are not consistent with how the excise tax is accounted for in that 1) the City can not segregate expenditures, 2) all of fund balance is available for construction/reconstruction, and 3) lower cost projects should be completed first. Your review of the preliminary report along with the attached spreadsheet and financial statements would be greatly appreciated.

Sincerely,

Marilyn Mays
Supervising Accountant

Enclosure

xc: Ken Buchanan, City Manager
Frank N. Brown, Finance Director
Bob Jackson, Public Works Director

March 3, 1998

Mr. Douglas R. Norton
Auditor General
State of Arizona
2910 North 44th Street, Suite 410
Phoenix, Arizona 85018

Dear Mr. Norton:

The City of Eloy has received the preliminary report draft of the performance audit conducted by the Office of the Auditor General. As requested, included herein is the City's preliminary written response to each recommendation contained in the performance audit.

Finding II: The City of Eloy has inappropriately loaned transportation excise tax and additional road monies to other funds to cover an excess of expenses over revenues.

Recommendation #1: Discontinue the practice of using road monies for non-road purposes.

Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

Recommendation #2: Repay inappropriately borrowed road monies. If resources are not currently available to completely repay loans, a repayment schedule should be developed and implemented.

Response: The finding of the Auditor General is agreed to and the audit recommendation will be implemented.

I would also like to add that the City was aware of these inappropriate practices and has been addressing the problem. The utility and golf course funds were the primary funds that were being loaned these road monies. In 1996 the City increased utility rates, and are now performing annual reviews of the utility funds with its Utilities Advisory Board. The function of this board is to review the funds and make recommendations to the City Council that would allow these funds to be self-supporting.

Also, the City is currently negotiating a sale of its golf course. The sale of the course would help tremendously toward discontinuing these inappropriate practices.

Because of measures already taken by the City in addressing this issue, the balance owed to the road fund decreased from \$741,350 as of June 30, 1996, to \$419,150 as of June 30, 1997. The City is moving in the right direction.

I would like to thank you and your staff for their assistance, and the opportunity to respond to the report.

Sincerely,

Robert Camareno
Finance Director

cc: Mark A. Higgins, City Attorney/Interim City Manager

March 12, 1998

Douglas R. Norton, Auditor General
State of Arizona
2910 N. 44th Street, Suite 410
Phoenix, Arizona 85018

SUBJECT: Response to Report - Pinal County Transportation Excise Tax

Dear Mr. Norton:

I am writing to acknowledge receipt of the report on the County Transportation Excise Tax and would like to take this opportunity to offer a few observations.

First, with regard to the recommendations or findings contained in the report, it was noted that some communities, including Florence in the past, have improperly used road monies by making loans to other funds. It is of course noted that Florence has discontinued this practice and has paid back all such monies loaned. I simply want to re-affirm our comments to your staff, that the Town administration will not allow this to happen in the future.

Secondly, I would like to offer some observations about the conclusions drawn or inferred relative to cities and towns not spending all of their road fund revenues received and instead allowing their fund balances to build up.

As noted in the report, in most instances, the revenues from the excise tax, LTAF and HURF were commingled and then utilized. As a result of this, it is difficult if not impossible to determine whether the monies used for XYZ street project were in fact excise tax revenues, HURF or LTAF funds. Likewise, in looking at "increasing fund balances", it is difficult to determine what revenue source was not spent on road projects and was kept in fund balance for future emergencies or large projects.

In looking at the three sources of road revenues, I would submit that the excise tax revenues are the most stable of the three sources in that they came about as a result of a vote of the people of Pinal County. We are also well aware of the fact that the other two revenue sources are eyed annually by the State Legislature as a potential source of funds that could be tapped. Because of this, both the HURF and LTAF funds are viewed as the less stable sources of the three and therefore would be the most likely funds to be carried forward for future emergencies. This excise, taxes, however, would be those first spent, because the cities and towns are more certain they will be receiving them again the following year. In summary, I do not think one can draw conclusion that because not all of the commingled funds were spent, that the excise tax revenues went into increasing fund balances.

I appreciate the opportunity to review and comment on the report and as I indicated to your staff, I do not feel it necessary to have a meeting to discuss it further.

Should you have any questions regarding any of the above, please feel free to contact me at your convenience.

Sincerely,

John C.F. Geib,
Town Manager

**TOWN OF MAMMOTH
P.O. BOX 30
MAMMOTH, AZ 85618
(520) 487-2331 / FAX (520) 487-2152**

March 5, 1998

Mr. Douglas Norton
Auditor General
2910 N. 44th Street, Suite 410
Phoenix, AZ 85018

Dear Mr. Norton:

The Town of Mammoth has received the report of the performance audit conducted by the Office of the Auditor General. As a new staff member who began on December 17, 1998, I am grateful for the identification of the areas in which the Town needs to improve. Following are the Town's responses to the recommendations in the audit:

Finding I: The Town of Mammoth agrees that it has an urgent need to do street improvements and will make efforts in the future to pursue this. The Town agrees it must replace road funds and will set up a special line items in the General Ledger whereby the funds can be identified and used.

Finding II: The Town of Mammoth agrees that it would be beneficial to set up separate areas for excise, LTAF, and HURF tax monies to assure the proper use of such. The Town will immediately cease using road monies for non-road purposes. The Town will review it's resources to begin implementing a repayment schedule. It should be noted the passing of the May 19, 1998 Home Rule election would assist this effort.

Thank you for the opportunity to respond to the report. If there is any other information you require, please do not hesitate to contact me.

Sincerely,

T. Rae Zapata
Town Clerk / Finance Director

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