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## **Audit: City lacked fiscal oversight But Desert Hot Springs says it is already on the mend**

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DESERT HOT SPRINGS - The city of Desert Hot Springs can't find deeds to its property, had inadequate reserves in accounts and failed to produce a report outlining its significant development fees.

That's according to a firm that put forth five potentially damaging "reportable conditions" in the city's latest audit and accompanying report on financial internal controls obtained by The Desert Sun on Thursday through an open records request.

The January report on the city's internal financial controls pointed out several problems with the way city money and property are accounted for and transferred.

Some city leaders Thursday said the problems have been fixed and the city's financial house is in order.

But experts experienced with in-depth audits and analyses of city budgets said the report could indicate Desert Hot Springs' finances were not receiving the proper level of oversight.

"It's troublesome," said Steve Levin, a political reform project manager at the Center for Governmental Studies, a nonprofit, nonpartisan research organization in Los Angeles.

"Newer cities are less established and have less formal procedures," Levin said, after hearing a synopsis of the public documents from the city that was incorporated in 1963. "But that's no excuse."

"It sounds unorganized, and an audit like that does not instill confidence in the citizens that their government is doing everything it should be doing," he explained.

Desert Hot Springs emerged from a three-year bankruptcy in October 2004, shortly after the completion of the audit. The city issued \$12.7 million in bonds at that time to pay off nearly

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\$11 million in debt to a private housing developer who sued the city for discrimination.

The report pointed out these problems:

the city had inadequate reserve balances in capital project funds for two assessment districts;

the city couldn't find deeds to four properties it owned. Other deeds were not properly in the name of Desert Hot Springs;

the city had no accounting policies and procedures manual;

the city didn't produce a timely report to record development fees, such as for fire protection, general services, park land and storm drainage; and

the city had no administrative policy to deal with basic budget amendments and line item transfers.

That led to situations in which expenditures exceeded the City Council-approved budget.

Mayor Matt Weyuker, Vice Mayor Mary Stephens, Public Information Officer Theresa Thompson, Councilman Hank Hohenstein, Finance Director Linda Kelly and City Attorney Corky Larson did not return calls and e-mails requesting comment. City Manager Jerry Hanson could not be reached for comment.

But Councilmembers Will Pieper and Gary Bosworth say the audit is an improvement over previous years, both in internal controls and in the bottom line for the city that is emerging from bankruptcy and on the edge of a development boom.

## What it means

A reportable condition is a matter coming to an auditor's attention relating to "significant deficiencies" in the design or operation of the entity's internal control that could adversely affect an entity's ability to fulfill future obligations with customers and/or the satisfaction of financial liabilities.

In Desert Hot Springs' case, that meant:

stale, dated checks remained outstanding on the books;

nonexistent journal entry and accounting policies;

a Senior Services account that languished, with no deposits or withdrawals, over years; and

missing deeds for city-owned property.

The report was submitted as part of the 2003-04 financial audit of the city by Vavrinek, Trine, Day & Co., of Rancho Cucamonga.

The firm, which specializes in school district and municipality audits, noted in its Jan. 13, 2005, supplementary report to Weyuker and the City Council that five "reportable" findings as of fiscal year ended June 30, 2004, could "adversely affect" Desert Hot Springs' ability to record, process, summarize and report financial data.

Lew Piper, a certified public accountant and partner in the financial planning firm of Boseant Piper & Associates of Indian Wells, said the findings seem to reflect a view that the reportable conditions are not what is known as the more serious accounting term of a "material weakness" in the city's finance department.

"It's serious, but not so serious it would have material impact on the preparation of the financial statement," Piper said. "What it says is that the city finance office is not running with a proper level of oversight or continuity, and their auditors have provided them with several areas of compliance they need to get in place."

## What could happen

Failure to correct the situations could be costly to taxpayers, he said.

Carrying an inadequate reserve balance on capital project funds could lead to a situation where the city is forced to refinance its debt, Piper said, and failure to report development fee collections could have an impact on computed costs for future developers.

"If you let them develop at \$2,000 a parcel, and in 2010 you find it costs \$5,000, the city may find itself in position where it is underfunded," Piper said. If city property is improperly recorded, and Desert Hot Springs has no basis to prove its ownership, he added, there could be repercussions of a legal nature that could cost the city in the long run.

Oftentimes, Levin said, it takes an audit like this to promote change, to get the wheels turning.

Hopefully, he added, it will open people's eyes to push for change because failure to mandate that either condones or opens the door for fraudulent behavior.

"Anytime you don't have formal budget procedures in place, that enables people to stray from the norm," he said. "It opens the door to all kinds of wrong-doing and mishandling of funds. Again, those aren't the things you want or expect from your public officials."

## Other cities

Palm Springs City Manager David Ready, who was been with the city since 2000, said during his tenure in Palm Springs, the fourth-largest city in the Coachella Valley has not

received such findings on internal controls audits.

Cathedral City City Manager Don Bradley said in the five years he's been with the city the municipality has received recommendations for improvement in management letters, but its most recent audit had none.

Bradley said he did not recall if these recommendations involved so-called "reportable" conditions.

## **Positive steps, fixing holes**

Despite the findings on internal controls, Desert Hot Springs council members said the overall audit for fiscal year ended June 30, 2004, was positive and showed the city's finances were on the mend.

"It looks like we have these terrible negative balances," said Councilman Will Pieper, "But we are paying off the bankruptcy in full now."

Since then, Desert Hot Springs has exploded and city officials say they've tightened controls.

A few city officials called the audit a significant success.

"I was thrilled with it," Pieper said. "I think it's very clear and concise and it shows the city moving forward."

Pieper said the city had already addressed most, if not all, of the concerns raised in the audit.

City staff had already created a formal policy for handling outstanding checks older than six months, he said, and had begun a study outlining procedures for check-writing and updating the senior services account.

"Once they brought it up, we fixed it," Pieper said.

Others outside of Desert Hot Springs, however, described the reportable findings as problematic.

## **Improvement over past**

Desert Hot Springs Councilman Gary Bosworth said the audit earmarked a positive turn in the city, as it was released at the same time steps were being taken to improve its financial affairs.

Pieper's corrective actions - establishing processing for tracking checks, instituting accounting procedures, addressing neglected fund balances - were noted in the Jan. 13,

2005, report to the city by the auditing firm.

That report said that beyond the city's admission it would draft financial policies and procedures, Desert Hot Springs officials intended to deal with the depleted debt reserves, hire a consultant to work with staff to develop ways to document accounting policies and complete its required annual report on development impact fees in a timely fashion.

It says the city's third amended plan involving bankruptcy-related debt became effective Oct. 27, 2004, and noted that the city intends to work with Riverside County to correct the names on titles of properties.

Comparing the 2003-04 audit with those of previous years, Bosworth, the senior person on council, said the documents show Desert Hot Springs is on its way up.

Bosworth said just years ago the city's audit contained a finding labeled "growing concern," meaning auditors wondered if Desert Hot Springs had the financial fortitude to survive as a city. He said the findings of the most current audit are not minimal concerns, but miniscule when compared to what the council has dealt with in the past.

"In every aspect of it there was improvement from what I saw last year," Bosworth said.

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