ENGEL & ENGEL LLP
FORENSIC ACCOUNTANTS

350 S. Grand Avenue, Suite 3160, Los Angeles, CA 90071 | (310) 277-2220 | www.engelandengel.com

ENGEL & ENGEL, LLP
FORENSIC REPORT

OCTOBER 9, 2026

PREPARED FOR
SUBDIVISION DEFERRED IMPROVEMENT FUND
ADVISORY COMMITTEE

RE: SUBDIVISION DEFERRED IMPROVEMENT FUND

Table of Contents

I. Retention and Assignment 4
II. Limitations of Engagement 4
III. Summary of Findings 5
IV. Background 10
1. Purpose of the SDI 10
2. Investment of SDI Funds 10
3. Record Maintenance 12
4. The City's Accounting and Investment Policies 12
5. Individuals Responsible for the SDI Fund's Investments 13
V. Documents Requested by E&E and Not Provided by the City 13
VI. The City Has Failed to Maintain Adequate and Accurate Accounting Records for the SDI Fund 17
1. The Ledger Maintained by the City for the SDI Fund is Incomplete, Inaccurate, Deficient, and Does Not Satisfy the Basic Function of a General Ledger, Posing a Major Risk to the SDI Fund. 17
2. The City's Monthly Financial Statements Issued to the Public are Materially Inaccurate 27
3. The Treasurer's Reports Issued to the Public Overstated the SDI Fund's Primary Investment Account in 16 of 121 Months 33
4. The City's Adopted Budget For the Fiscal Year 2026/27 Overstated the SDI Fund's FY2024 Investment Revenue by Approximately $12.1 Million 33

5. The City States That Quarterly Investment Reports Required by the SDI Ordinance and the City's Accounting and Investment Policies Do Not Exist for Periods Exceeding 10 Years 34

VII. The City's Unaccounted For, Unexplained, and Potentially Concealed Use of SDI's $1,354,346 Street Maintenance Reserve 35

1. Background: The SDI Fund's Street Maintenance Obligations and the City's Failure to Account or Produce Documents 35
2. The SDI Fund's $1,354,346 Reserve Account in the Street Maintenance Fund 41
3. The City's General Ledger Accounting of the SDI Fund's Street Maintenance Reserve Account 42
4. The Monthly Financial Statement Accounting of the SDI Fund's Street Maintenance Reserve Account 43
5. Potential Concealment of the City's Unexplained Write Off 46

VIII. Performance of SDI Fund Investments and Non-Compliance with Investment Goals and Policies 47

1. Background of SDI Fund Investments and Historical Performance 47
2. Sale of Bonds Prior to Maturity 51
3. Corporate Bonds Purchased for the SDI Fund Are Not Permitted Per the City's Municipal Code, and When Purchased, Caused a Loss for the SDI Fund Approximating $1.9 million 53
4. Foreign Bank Notes Held by the SDI Fund Are Not Permitted by the City's Municipal Code or the City's Accounting and Investment Policies, and Do Not Appear to Be Consistent with California Government Code 59
5. Approximately 17% of SDI Fund Bond Purchases Exceeded the Statutory and Policy Maturity Limit of 5 Years 61
6. SDI Purchased Six Bonds That Exceeded the City's and GASB's 5% Concentration of Credit Risk Threshold, Which Went Undisclosed 64
7. Municipal Bonds Issued Outside California, Approximating $73.4 Million, Are Not Permitted by the City's Municipal Code or Accounting and Investment Policies, and At Least $10.6 Million Also Do Not Appear to Be Permitted Under California Government Code 68
8. The SDI Fund's Money Market Fund Holdings Exceeded the 20% Limit in California Government Code and the City's Accounting and Investment Policies Prior to SSDW's Engagement 74
9. SDI's Idle Cash Was Automatically Held in a Money Market Fund Rather Than LAIF 75
10. Historical Performance of SDI Investments vs. Benchmark Indices 76
11. Ratio Analysis and the Excessive-Trading Standard 77
12. The Cost to the SDI Fund of SSDW's Change in Investment Composition 79

13. The City's Records Do Not Reflect the Treasurer or Finance Director Approving the SDI Fund's Bond Trades 80

IX. Broker Engagement, Disciplinary Actions, Compensation, and Documentation 81

1. Timeline of Broker Relationships 81
2. Requirements for Investment Intermediaries Under the City's Municipal Code Were Not Provided and May Not Have Been Followed 81
3. Absence of Documentation in Response to Document Requests 84
4. Ronald C. Gross's Disciplinary History 86
5. Broker Compensation and Commissions 87

X. The City Continues to Report a $20,684,224 Allowance Against Two RDA Loans Without Producing Evidence Supporting the Basis for That Determination 89

1. Background: The Two RDA Promissory Notes Funded by the SDI Fund 89
2. Recording of the Two Loans on the City's Audited Financial Statements 91
3. The City's 2018 Resolutions 92
4. The City Has Not Produced Evidence Supporting the Basis for the Allowance 93
5. GASB's Framework for Recognizing Assets and Loss Contingencies..... 95
6. Interest Calculated Through Current Date Under Alternative Methodologies..... 97

XI. E&E Recommendations 97

1. Supporting Documentation 98
2. General Ledger and Internal Accounting Controls 98
3. Public Financial Reporting 99
4. Street Maintenance Reserve 99
5. Investment Oversight and Broker Relationships 99
6. RDA Loans Receivable..... 100
7. Segregation of Duties..... 101

I. Retention and Assignment

Engel & Engel, LLP ("E&E") was retained by the SDI Advisory Committee to conduct a forensic accounting investigation of California City's accounting of the SDI Fund, the SDI Fund's financial position, and reported performance of the SDI Fund. On May 13, 2025, E&E's retention was formally approved by Resolution No. 25-3136 **(See Exhibit 1)**.

II. Limitations of Engagement

This engagement was performed in accordance with the AICPA's Statement on Standards for Forensic Services No. 1 ('SSFS 1') and does not constitute a financial statement audit, review, or attestation engagement under standards established by the American Institute of Certified Public Accountants ("AICPA") or any other professional body.

A financial statement audit is designed to provide reasonable assurance that financial statements are free of material misstatement and provides an opinion on whether an organization's financial statements are fairly presented. Conversely, this forensic investigation was specifically directed to investigate accounting errors, irregularities, potential misconduct, and quantify the financial impact of such transactions.

For purposes of this report and the procedures performed, the terms "forensic audit" and "forensic investigation" are used interchangeably to describe the forensic application of specialized accounting, data analysis, and investigative techniques to reconstruct financial events and identify potential accounting irregularities.

This report presents our findings and observations based on the information available to us as of the date of this report. Nothing in this report should be construed as a legal conclusion, including any determination as to whether fraud,

embezzlement, or any other unlawful conduct occurred. Where this report references statutes, ordinances, City policies, or other legal authorities, E&E has applied their plain language to the facts identified in its investigation; it has not offered an opinion on their legal interpretation, enforceability, or effect. Such determinations are outside the scope of this engagement and would require legal analysis beyond our role as forensic accountants. Our findings and opinions are subject to change should additional documents or information become available.

III. Summary of Findings

The SDI Fund is a Special Revenue Fund of California City ("the City"), established for the benefit of lot owners within the City, with assets exceeding $100 million as of June 2026. It is governed by three priorities, in order of importance: (1) safeguarding principal, (2) meeting liquidity needs, and (3) achieving a return on investment. Under the City's Municipal Code, responsibility for the custody, investment, and record-keeping of the SDI Fund rests with the City.

Overall, E&E found that the City's accounting system is inadequate to safeguard the SDI Fund's assets and has contributed to its economic losses. E&E identified four recurring issues in the City's handling of the SDI Fund: deficiencies in internal controls, inadequate recordkeeping, material misstatements in information reported to the public, and a lack of supporting documentation for unexplained transactions.

E&E identified the following economic losses suffered by the SDI Fund, reflecting those deficiencies whose financial effect could be quantified:

Summary of Economic Losses (See Schedule 1)

Description	Amount
Losses From Investment Strategy and Non-Compliance with the City's Municipal Code, Accounting and Investment Policies, and California Government Code	$ 10,296,155
Unaccounted For SDI Street Reserves	$ 1,354,346
Unaccounted For Negative Cash Balance	$ 113,643
Deferred RDA Loan Receivable and Compound Interest Through Current	$ 100,286,860
Total Economic Losses	**$ 112,051,003**

The deficiencies described throughout this report are not limited to the amounts identified above.

Article 5, Section 3-2.507 of the City's Municipal Code requires the City to pre-qualify any investment intermediary before engaging it, so the City can judge that person's integrity and competence and evaluate the intermediary's investment philosophy against the SDI Fund's goals. The City may only engage an intermediary after soliciting proposals and entering into a Council-approved written agreement. The City itself contends that no documentation exists showing any of this process was followed for either of the SDI Fund's broker relationships. Regardless, the City engaged and continued using an individual broker with a documented disciplinary history, including a prior regulatory suspension and outstanding federal tax liens, without ever executing a written contract for the relationship. The result was an investment mix riskier than at any point in the approximately eight preceding years of records reviewed, and non-permitted investments that caused millions of dollars in losses to the SDI Fund.

The following represents SDI Fund's investments that were not permitted under the City's Municipal Code, the City's Accounting and Investment Policies, or California Government Code Section 53601 **(See Schedule 4.8)**:

- Corporate bond purchases approximating $28 million not included in the City's Municipal Code's list of permitted investments

- Corporate bond purchases in three separate months that brought corporate holdings above the 30% limit in California Government Code Section

53601 and the City's Accounting and Investment Policies, with holdings remaining above 30% for approximately 24 months

- 64 bond purchases exceeding the five-year maturity limit in the City's Accounting and Investment Policies and California Government Code Section 53601, without the Council authorization required by the City's Municipal Code

- Single-issuer concentration exceeding the 5% limit in the City's Accounting and Investment Policies, at times more than tripling it, for four issuers

- Investments in two foreign bank notes not included in the lists of permitted investments in the City's Municipal Code or the City's Accounting and Investment Policies, and that do not appear to be consistent with California Government Code Section 53601, based on CDIAC guidance

- Municipal bond purchases approximating $73.4 million issued outside California, not included in the lists of permitted investments in the City's Municipal Code or the City's Accounting and Investment Policies, and at least $10.6 million of which also do not appear to be of a type permitted under California Government Code Section 53601

Separately, prior to SSDW's engagement, the SDI Fund's holdings in a money market fund exceeded the 20% limit in California Government Code Section 53601 and the City's Accounting and Investment Policies in 34 months, reaching as high as approximately 81% of the SDI Fund's investments.

When the City brought in SouthState|DuncanWilliams ("SSDW") as the SDI Fund's broker in December 2020, the SDI Fund's portfolio changed more sharply than at any other point in the decade of records reviewed. The City acquired $27.9 million in corporate bonds, and the SDI Fund's cash position fell from 46% of assets to just 8% within a single month.

The SDI Fund's value declined by approximately $8.5 million over the following 23 months. From December 2021 through the end of this period, the City's monthly financial statements overstated the SDI Fund's assets by as much as $8 million, obscuring the decline during its most severe months. E&E's analysis reflects that had SSDW never been hired and its investments were left untouched, the SDI Fund would hold approximately $10 million more as of August 31, 2025.

The City did not produce records reflecting what SSDW was paid. Using publicly available trade data, E&E identified more than $2.3 million in commissions on a limited subset of the SDI Fund's municipal bond transactions alone and was unable to determine the full extent of compensation SSDW received. This same lack of records also prevented E&E from calculating the SDI Fund's cost-to-equity ratio, one of two standard measures used to assess excessive trading in an account.

Inaccurate public reporting by the City recurs across multiple public-facing documents, spanning years, and represents an ongoing failure to inform the public accurately about the SDI Fund. For 14 consecutive months, from March 2025 through April 2026, the City reported the exact same investment balance, $84,901,921, while the SDI Fund's investments grew to approximately $94 million. The City's Treasurer's Reports separately overstated the balance in the SDI Fund's primary investment account in 16 of 121 months reviewed, by an average of $873,566 and as much as $1,233,764. Furthermore, the City's Fiscal Year 2026/27 Adopted Budget overstated the SDI Fund's 2024 revenues by approximately $12.1 million.

Beyond these inaccuracies, quarterly investment reports required by the SDI Ordinance and the City’s Accounting and Investment Policies were not produced for periods exceeding 10 years. In response to E&E's request for these records, the City stated that the documents do not exist.

In its audit of fiscal year 2019, the City's auditor found that the Finance Department "does not have adequate oversight over all aspects of the accounting functions." The 2021-2022 Kern County Grand Jury separately reported that, in 2020, the City's outside auditor had advised that the City's books were “unauditable”. E&E's own review of the general ledger reflects the same gap: approximately 46% of its entries in the SDI’s general ledger are adjustments made with no description of what they represent. A general ledger in this condition cannot distinguish a legitimate correction from an error, or from an adjustment made to conceal a misappropriation of the SDI Fund's principal.

A pattern runs through the City's accounting of the SDI Fund: transactions with real financial consequences were recorded with no documented basis, and the City did not explain them even when E&E requested the underlying records directly.

Since fiscal year 2021, the SDI Fund's cash account has carried a negative, unexplained balance of approximately $113,643. This balance stems from recurring charges the general ledger recorded against the SDI Fund's cash account, even though the SDI Fund’s own bank statements show no corresponding activity for those same periods. The City provided no documentation explaining these entries, despite specific requests for that information from E&E.

A separate reserve account of $1,354,346, set aside for SDI street maintenance, remained on the books of the Street Maintenance Fund for nearly seven years, until 2021, when the account was commingled with five other accounts and its balance became untraceable. The combined account later went negative, and the City has not explained what the reserve was spent on or why.

Most significantly, the SDI Fund has carried a $20 million receivable that the City has characterized as uncollectible for the past decade, unsupported by any documentation. In 2018, the City Council, the Successor Agency, and the Oversight Board adopted resolutions acknowledging the same loans and

authorizing their repayment, actions inconsistent with treating the loans as uncollectible, and the City's accounting has not been updated to reflect them. Calculated with compound interest at the rates stated in the original promissory notes, the loans and accrued interest would exceed $100 million.

E&E's ability to verify these findings was itself limited by the City's own response to this investigation. Of 152 items requested across three separate document requests, the City fully complied with only 9, or approximately 6%. The City claimed 43% of the requested records do not exist, though some of these same records were later obtained independently by E&E. The City did not respond at all to another 20% of the items requested by E&E.

The City controls the SDI Fund's custody, investment, and accounting. In addition to the economic losses already incurred by the SDI Fund, the City's deficient accounting system leaves the SDI Fund's more than $100 million in assets exposed on the first and most basic of its priorities: safeguarding its principal.

IV. Background

1. Purpose of the SDI

The Subdivision Deferred Improvement Fund ("SDI Fund") was created to benefit owners of lots in 29 designated SDI Tracts within California City. The City adopted Ordinance No. 98-552 ("the SDI Ordinance") amending the Municipal Code **(See Exhibit 2)** to govern, among other things, the investment, expenditure, maintenance, and administration of the SDI Fund.

2. Investment of SDI Funds

The SDI Ordinance assigns responsibility for investing SDI Fund money to the City Treasurer and Finance Director and requires that investments comply with the Municipal Code and California Government Code Section 53601. The SDI Ordinance sets three investment goals, in order of priority: (1)

safeguarding principal, (2) meeting liquidity needs, and (3) achieving return on investment. The SDI Ordinance also states the following:

a. "When the investments mature or when other monies are available for investment, the monies may be invested in the Local Agency Investment Fund ("LAIF") pending more permanent investment."

b. "The investments shall be held in the name of the City as trustee for the SDI Fund. Investment documents shall be held for safekeeping in the City vault or in a depository approved by the City Council. The City Council shall, from time to time, execute such documents as are necessary to provide evidence of trading authority as set forth herein."

c. "The Treasurer shall present quarterly reports on cash flow and the investments of the money in the SDI Fund to the SDI Advisory Committee, City Manager and the City Council. The report shall show: the type of investment; date of investment; how title is held; institution; date of maturity; par value; amount of each investment; current market value for all securities with a maturity of more than 12 months; rate of interest; confirmation that each investment is consistent with this investment policy; information showing expenditure requirements can be met in the following quarter; and specify which investments were made pursuant to Government Code Sections 53601(i), 53601.1 and 53635(i). For money managed by LAIF, a county investment pool, or placed in FDIC insured accounts, the Treasurer may use the statement from these institutions in lieu of a separate report."

d. "The City Manager, Finance Director and SDI Advisory Committee (hereinafter collectively "Investment Review Committee") shall review this investment policy annually on or about July 1st of each year and recommend changes as necessary to meet the above stated investment goals. The City Council shall consider any such

recommendations made by the Investment Review Committee at a public meeting."

3. Record Maintenance

Under the ordinance, the City is responsible for keeping, investing, and disbursing SDI Fund money. The ordinance assigns investment selection duties specifically to the City Treasurer and Finance Director, and assigns the duty to prepare quarterly reports on SDI Fund cash flow and investments specifically to the Treasurer. Investment documents are required to be held for safekeeping in the City vault or an approved depository. The City must provide the SDI Advisory Committee with reports and information as requested, along with access to a meeting place, and must provide environmental documents for SDI projects to the Committee.

4. The City's Accounting and Investment Policies

Separate from the SDI Ordinance and the City's Municipal Code, the City maintains two policy documents that govern the SDI Fund. The first is the City's Accounting Policies and Procedures Manual, which governs the City's accounting practices, including investment management, accounts payable, cash receipts, and fiscal year-end closing procedures (See Exhibit 12). The manual states that it was "approved as official policy of the City of California City by the City Council" and that "all Finance employees from the City of California City are bound by the policies herein, and any deviation from established policy is prohibited." The second is the City's Annual Investment Policy, which the City Council adopted by Resolution No. 03-15-2600 on March 17, 2015 **(See Exhibit 13)**. Section 7 of the Accounting Policies and Procedures Manual contains investment provisions almost identical to those in the Annual Investment Policy, under the same section numbers. In this report, E&E refers to the two documents together as the "City's Accounting and Investment Policies."

E&E requested the City's investment policy for the period July 1, 2014 to the present. In response, the City produced only the Annual Investment Policy dated March 2015 (Request No. 49). The City's Accounting and Investment Policies require the City Council to review the investment policy at the beginning of each fiscal year (Sec. 7.19). The City did not produce any later version.

5. Individuals Responsible for the SDI Fund's Investments

Keith Middleton has served as the City's Treasurer continuously since at least 2016 through August 2026, according to the most recent records available to E&E. The position of Finance Director has been considerably less stable. Between 2014 and 2021, the position turned over among four different individuals, two of whom held the role simultaneously with the separate position of Assistant City Manager. By June 2021, the Finance Director position was held only on a part-time basis. Beginning June 2022, E&E was unable to identify any individual holding the position of Finance Director, and this remained the case through the most recent records available to E&E, dated August 2026. As of that date, the City's own website listed the position as open. **Schedule 15.4** is a historical analysis of the individuals who served at various accounting positions for the City including the City Treasurer and Finance Director.

V. Documents Requested by E&E and Not Provided by the City

Our investigation was limited by the scope of documentation made available to us. E&E provided the City with three Document and Information Requests, including an original request in August 2025 and two separate follow-up requests in October 2025 and February 2026. As detailed in this report, significant and material requested records, including financial statements, bank records, general ledgers, and key brokerage and investment documents were not provided to us or were represented as unavailable. Upon review of each of the City's document

productions, our firm identified several continuing issues, including the following:

1. Numerous requested documents were not provided, responded to, or otherwise addressed, including documents originally requested in August 2025 that have never been acknowledged or responded to and remain outstanding after three separate document requests by E&E.

2. A significant number of City responses stated that records do not exist; however, we have determined that such documents do and should exist. In our document requests, we have provided detailed explanations for why such documents do and should exist. We also requested written explanations from the City for why certain documents do not exist, however we did not receive responses to such explanations.

3. Numerous responses included incorrect or incomplete document productions.

Attached hereto as **Exhibit 3** is a copy of our February 6, 2026 Document Request which contains a summary of the City's responses, identification of the outstanding records, and a detailed chronology of E&E's requests along with the City's productions and responses for each request. The chart below has been updated to reflect the City's responses and productions received after the February 6, 2026 Document Request. Overall, the responses received from the City in connection with our three document requests are categorized as follows:

Response Type	Document and Information Request Number	Total	% of Responses
No Response and No Documents Received	11, 23, 29, 31, 32, 35, 41, 53, 57, 66, 70a, 70b, 70c, 70d, 70e, 71, 72, 74, 77, 78, 79, 80, 81, 83, 84, 85, 87, 94, 26, 88, 37	31	20%
Incorrect Documents Received	25, 34, 40, 106, 114, 121, 21, 135, 136, 137, 138	11	7%
Documents Not Fully Received	8b, 12, 30, 38, 45, 96, 6, 7, 8a, 9a, 9b, 9c, 9d, 9e, 14, 36, 97, 98, 99, 100, 101, 102, 103, 104, 105	25	16%
Not Available Online	2, 3	2	1%
Partially Available Online	82, 92	2	1%
Per Response Does Not Exist	46, 17, 13, 18, 22, 33, 39, 42, 43, 44, 48, 50, 51, 54, 55, 56, 59a, 59c, 60, 61, 63, 64, 65, 68, 69, 75, 76, 86, 89, 93, 95, 107, 108, 109, 110, 111, 112, 113, 115, 116, 117, 118, 119, 120, 122, 123, 124, 125, 126, 127, 128, 129, 130, 131, 132, 133, 134, 90, 73, 67, 59e, 59d, 59b, 58, 52, 47	66	43%
Documents Fully Received	15, 16, 20, 24, 49, 62, 5, 27, 4	9	6%
No Follow-Up Request from E&E	1, 9f, 10, 19, 28, 91	6	4%
Total		**152**	**100%**

E&E provided approximately 152 document and information requests to the City. Overall, the City fully complied with approximately 9 requests or 6% of our total requests.

The City responded that approximately 43% of the documents requested by E&E do not exist. Such documents include but were not limited to quarterly investment reports, contracts and agreements with SDI's investment brokers, compensation paid to SDI's investment brokers, communications and reports provided by SDI's investment brokers, bank reconciliations for the SDI, invoices for the SDI's costs, supporting documents for pooled cash accounts, supporting documents for SDI funds invested in LAIF, information provided to the City's auditors, and audit findings issued to the City by its auditors. It is important to note that certain documents the City claimed do not exist, were provided to E&E by the SDI Advisory Committee. Accordingly, E&E found that certain of the documents did exist.

The City did not respond to or provide any documents with respect to approximately 20% of the documents requested by E&E. E&E requested many of the items three separate times, across the three separate requests, and did not receive any response. Such documents included but were not limited to

supporting invoices and documents for SDI fund expenses, internal approval procedures for SDI investment transactions, supporting documents for loans of the SDI fund, supporting documents for SDI fund payments designated to Public Works, a complete general ledger for the Street Maintenance Fund, communications with the City's auditors, and the City's internal communications regarding the SDI Fund.

For E&E's requests relating to SDI's financial statements, the City advised E&E to retrieve the City's monthly financial statements issued on the City's website, which include reporting for the SDI Fund. Between January 2015 and May 2026, there were 79 months of financial statements not reported on the City's website. The City does not report any monthly financial statements on its website from January 2015 through December 2020. In addition, the City did not report any monthly financial statements in the months July 2021 through October 2021 and January through February 2022. E&E was unable to obtain monthly financial statements for such periods despite the City's reference to the City website for such information.

Under the SDI Ordinance, responsibility for the custody, investment, and record-keeping of the SDI Fund rests with the City, which is required to maintain investment records and report on SDI Fund activity. The SDI Advisory Committee itself holds no independent recordkeeping ability or custody of SDI Fund records. In accordance with the ordinance, it is instead entitled to receive information from the City upon request in addition to investment reports on a quarterly basis. As a result, the completeness and reliability of the SDI Fund's financial history is dependent on the records the City maintains and produces, and the deficiencies identified in this section directly limited the scope of records available for our review.

VI. The City Has Failed to Maintain Adequate and Accurate Accounting Records for the SDI Fund

1. The Ledger Maintained by the City for the SDI Fund is Incomplete, Inaccurate, Deficient, and Does Not Satisfy the Basic Function of a General Ledger, Posing a Major Risk to the SDI Fund.

A general ledger exists to record, on an ongoing basis, the transactions underlying a fund's reported financial position. For a fund holding approximately $100 million in public trust, this function is fundamental. The general ledger maintained by the City for the SDI Fund **(See Exhibit 4)** does not perform this function in multiple significant respects.

Cash and investments are two of the SDI Fund's three main assets, and neither is maintained in the ledger on an ongoing basis. The SDI Fund's investment balance is updated only once a year. Its cash balance is recorded in bulk without any description, omits transactions that occurred, and includes a balance that has remained unexplained for years.

In addition, hundreds of entries throughout the ledger change account balances, some by tens of millions of dollars, without any description of what the entry represents. Some of these entries correct balances years after the underlying transactions were either recorded incorrectly or omitted entirely, with no description of what was being corrected or why. This pattern recurs throughout the general ledger and is not limited to the specific instances described in this report. For the years before a correcting adjustment was made, the general ledger did not reflect the SDI Fund's actual financial condition. For other adjustments, E&E cannot confirm whether the adjustment was warranted or accurate, because the general ledger includes no description of what it represents. This lack of explanation makes it difficult to reconcile what the general ledger actually reflects at any given time.

This absence of explanation across hundreds of adjusting entries is a serious control weakness. Without a description, there is no way to distinguish a

legitimate correction from an error, or an adjustment made to conceal a misappropriation of funds. A general ledger that allows account balances to be changed, by any amount, at any time, without explanation, cannot protect a fund from that risk.

a. The General Ledger Reflects the SDI Fund's Investment Balance Only Once a Year, at Fiscal Year End.

The City updates the general ledger's investment accounts only once a year. Each year from 2015 through 2024, the City records a single adjusting entry, dated June 30, that brought the ledger's investment balance in line with the SDI Fund's U.S. Bank custodian statement as of that date **(See Exhibit 4) (See Schedules 5.9, 5.10, 5.11, 5.12, and 5.13)**. No other investment activity, including monthly interest, dividends, purchases, sales, or changes in market value, was recorded in the general ledger at any other time during the year. As a result, the general ledger's investment balance, the SDI Fund's single largest asset, is accurate on only one day out of the year and provides no reliable record of the SDI Fund's investment position at any other time. A ledger that is updated once a year cannot be used to identify an error or improper transaction affecting the SDI Fund's investments until, at the earliest, the following year end.

b. The General Ledger Does Not Record the SDI Fund's Cash Transactions Individually or as They Occur.

The City's general ledger cash account does not record who was paid, or why, for the SDI Fund's cash disbursements. Checks and other disbursements are recorded in the cash account only under the generic label 'Total Checks & Other Charges,' rather than the payee's name or a description of the transaction **(See Schedule 5.4)**. As recorded, the cash account does not permit a reviewer to determine who was paid, for what purpose, or why, for any disbursement of the SDI Fund’s cash, without separately reconciling each entry to its corresponding

record elsewhere. While the offsetting entries to some of these disbursements recorded in the SDI Fund's expense accounts do identify a payee, that information can only be obtained through this same transaction-by-transaction reconciliation. The cash account reflects the SDI Fund's most basic financial activity, the movement of its cash, and is accordingly one of the most significant accounts to monitor. This documentation gap constitutes a control weakness: it leaves the account most directly reflecting the SDI Fund's cash activity without the information necessary to identify an error, verify the propriety of a disbursement, or detect an improper payment.

The general ledger also fails to record cash transactions individually as they occur. Bank of the Sierra deposited interest into the SDI Fund's account 24 separate times between July 2021 and June 2023, totaling $9,504.31. None of these 24 deposits were recorded in the general ledger as it occurred **(See Schedule 5.4)**. While the interest amounts are relatively immaterial to the SDI Fund's assets, they demonstrate the City's failure to record transactions at the time they occurred.

The City's Accounting Policies and Procedures Manual states the following:

> "On a monthly basis, the accountant, who does not prepare the initial cash receipts listing of bank deposit, shall reconcile the listings of receipts to bank deposits reflected on the monthly bank statement. Any discrepancies shall be immediately investigated and reported to the Finance Director, City Treasurer, and City Manager." (Sec. 10) **(See Exhibit 12).**

Based on the City's failure to record the 24 interest deposits described above for approximately two years, it appears that the SDI's general ledger was not being reconciled on a monthly basis as required by the City's Accounting Policies and Procedures Manual.

The general ledger's cash account also carried an unexplained negative balance of $113,643 since fiscal year 2021. This balance, and what E&E's investigation found regarding its origin, is discussed below.

c. The General Ledger's Cash Account Has Carried an Unexplained, Unsupported Negative Balance of $113,643 Since Fiscal Year 2021.

The SDI Fund's general ledger has reported a negative balance of $113,643 in its Cash-SDI account since fiscal year 2021. The City internally refers to this balance as “pooled cash” and has not produced any record explaining how this balance arose. E&E specifically requested the journal entries and supporting documentation underlying this balance and asked the City to explain how it was determined. The City responded that the documentation does not exist.

The City's Accounting Policies and Procedures Manual states, “During the year and also as part of the fiscal year-end process, finance will insure that all journal entries have appropriate back up to substantiate the entry(s).” (Sec. 11.03.12) (**See Exhibit 12**).

Based on the City’s contention that supporting documentation for this balance does not exist, the journal entries do not have appropriate back up to substantiate the entries as required by the City's Accounting Policies and Procedures Manual.

E&E investigated the negative balance and found that it did not result from a single transaction. E&E traced the balance through the general ledger's detailed transaction history and found that it accumulated gradually, from fiscal year 2017 through fiscal year 2021, through a combination of various accounts payable postings, a recurring charge described as a "US Bank Corporate Payment," and a separate "Due to General Fund" account.

A substantial part of the balance, $67,715.91, relates to the recurring "US Bank Corporate Payment" charge **(See Schedule 5.3.4)**. E&E reviewed the SDI Fund's Bank of the Sierra bank statements for the periods in which these charges were recorded in the general ledger and found no corresponding bank activity. For example, on August 23, 2018, the general ledger recorded a $6,291.21 charge against the SDI Fund's cash under this description, corresponding to a July 25, 2018 'US Bank Corporate Payment' entry in the SDI Fund's Contracts account **(See Schedule 5.3.5)**. E&E reviewed the SDI Fund's Bank of the Sierra bank statement for this same period and found no corresponding bank activity **(See Schedule 5.3.5)**. The general ledger's cash balance was reduced by the full $67,715.91, even though the bank's own records show no money left the account for any of them.

The remaining $45,926.74 of the balance relates to accounts payable postings that reduced the SDI Fund's cash between March 2017 and June 2018 **(See Schedule 5.3.4)**. Of this amount, $20,771.34 is described in the general ledger only as payments to "Jones & Mayer," recorded across fourteen separate entries. In addition, $18,903.60 is described as “US Bank” with no further description. A separate $6,251.80 entry, dated September 7, 2017, is described only as "California City Successor Agency" **(See Schedule 5.3.4)**. The SDI Fund’s general ledger cash balance was reduced by the full $45,926.74, even though the SDI Fund’s bank statements show no money left the account for any of them.

For the $45,926.74 in accounts payable postings, the City's Accounting Policies and Procedures Manual specifies exactly what this backup should include as follows:

> "All requests for payment to be submitted to finance shall include an A/P package. Each A/P package shall contain the following documents:
>
> a. Original invoice
> b. Packing Slip (where appropriate)
> c. Purchase Order…
> f. Any other supporting documentation deemed appropriate.
>
> All A/P packages must be approved by the department director. (Sec. 4.02) **(See Exhibit 12)**."

A separate $34,951.90 of the pooled cash was later reversed and relates to an account titled "Due to General Fund" **(See Schedule 5.3.4)**. This amount was first recorded on March 31, 2018 at $30,859.81, and grew to $34,951.90 by fiscal year 2019 through two further adjustments **(See Schedule 5.3.5)**. Both the creation and the later reversal of this balance were recorded through internal journal entries between the SDI Fund's own accounts, and E&E has not been able to confirm, with the documents available, that either event corresponded to an actual transfer of cash between the SDI Fund and the General Fund. None of the entries comprising this account's activity, including its initial recording, its later adjustments, its reversal, and its reopening, includes any description explaining why the entry was made. The City reversed this account to zero on June 30, 2019 **(See Schedule 5.3.5)**, then reopened it at the same $34,951.90 balance on July 1, 2019 **(See Schedule 5.3.6)**. The account was carried forward at this same balance into fiscal year 2020. It was not until April 22, 2021, nearly two years after the account was reopened, that the City retroactively adjusted both the fiscal year 2019 and fiscal year 2020 opening balances in the Due to General Fund account back to zero, again with no description explaining the

adjustment **(See Schedule 5.3.6)**. The general ledger shows no further activity in this account since that adjustment.

The total $113,643 negative cash balance is not recorded as a liability of the SDI Fund in either the City's monthly financial statements or its audited financial statements. It instead appears as a negative asset in the SDI Fund's own Cash-SDI account, unchanged since fiscal year 2021, with no supporting explanation or explanation from the City.

d. The SDI General Ledger is Not Being Maintained on a Monthly Basis, Despite the City Producing Monthly Financial Statements to the Public.

With the exception of a small number of routine operating expense accounts and the cash account, almost every account in the SDI Fund's general ledger reflecting its investments and reserves, including its two largest assets, is updated approximately once or only a few times per fiscal year. This is not because no activity occurred during the intervening months but because the transactions were not being recorded. For example, the general ledger's US Bank Investments account, the SDI Fund's single largest asset, is updated only once or twice a year, through opening balance entries set at the start of each fiscal year, rather than reflecting the account's actual activity as it occurs. Similarly, the general ledger's Interest Receivable and Market Value Adjustments accounts are each updated only twice a year, despite the fact that interest accrues continuously and the market value of the SDI Fund's investments changes daily. As a result, the ledger's recorded values can diverge substantially from the SDI Fund's actual financial position for months at a time. A general ledger updated once a year cannot support financial statements represented to the public as current on a monthly basis.

e. Approximately 46% of the General Ledger Entries are Adjustments to Account Balances Without Any Description

Of the approximately 964 individual entries in the SDI Fund's general ledger for fiscal years 2015 - 2025, approximately 447 entries inexplicably adjust the account balances with no description of what the entry represents or why it was made **(See Schedule 12)**. Each of these entries is labeled only "Opening balance created" or "Opening balance modified," and they appear across nearly every account in the ledger, spanning every fiscal year from 2016 through 2025 **(See Schedule 12)**. Adjustments have been as high as $86,473,356, an amount as large as the SDI Fund's entire reported assets in some years, with no description beyond the date and time the change was made **(See Schedule 12)**. A general ledger in which hundreds of balance changes are made without any description of what caused them, or why they were necessary, does not provide a reliable record of the SDI Fund's financial activity and poses a high risk for misstatement.

Furthermore, the general ledger contains an account titled 'Prior Period Adjustments' (**See Exhibit 4**). In February 2017, this account was modified nine separate times within a two-week span, recording total debits of $4,085,255 and total credits of $4,261,597, without any description of what was being corrected or why **(See Schedule 12.1)**. An account created for the express purpose of explaining prior errors or adjustments does not itself explain the changes recorded within it, leaving no way to verify what was corrected, why, or whether the correction was appropriate.

The City's Accounting Policies and Procedures Manual states the following:

> "During the year and also as part of the fiscal year-end process, finance will insure that all journal entries have appropriate back up to substantiate the entry(s)." (Sec. 11.03.12) **(See Exhibit 12)**.

E&E specifically requested supporting documentation for the 'Prior Period' adjustments and for the journal entries. In response, the City did not provide support for the journal entries; it resubmitted documents already produced, which E&E had already determined do not contain the requested support. This is inconsistent with the City's policy requiring that such backup exist.

Adjustments of this size, made without explanation, create a significant risk of undetected misstatement or fraud. Unsupported journal entries are one of the most common methods used to conceal errors or the misappropriation of assets. Without a description, there is no way to distinguish a legitimate correction from an error or deliberate concealment. Hundreds of undescribed entries, some in the tens of millions of dollars, in a fund holding nearly $90 million in public trust, is a serious control failure that would allow a material misstatement to go undetected indefinitely.

f. <u>Two Independent Sources Informed the City That its General Ledger Was Inadequate, and it Remains So Today.</u>

The deficiencies identified above in the SDI Fund's general ledger are consistent with the City's own outside auditor and the Kern County Grand Jury, regarding the City's accounting practices.

The City's independent auditor, Bryant L. Jolley, CPA, found the following in its Management Report and Auditor's Communication Letter for the fiscal year ended June 30, 2019 **(See Exhibit 5)**:

i. "The Finance Department does not have adequate oversight over all aspects of the accounting functions, including cash management, recording of year end accruals and the development of internal controls."

ii. "The Finance Department does not have adequate controls in place over the general accounting procedures including timely reconciliation of accounts and recording of year-end accruals."

iii. "Inadequate Finance Department oversight over all aspects of the City's accounting, including the collection of cash and the development of internal controls, could result in a misappropriation of assets, material accounting errors, reporting delays, and/or noncompliance with grant agreements."

Separately, Bryant L. Jolley, CPA found the following in the City's audited financial statements for the fiscal year ended June 30, 2020:

iv. "The City has determined that certain transactions were recorded incorrectly in the prior year," resulting in restatements of cash and investments, accounts receivable, interest receivable, intergovernmental receivables, and accounts payable across multiple funds **(Page 45)**.

Separately, the 2021-2022 Kern County Grand Jury reported the following **(See Exhibit 6)**:

v. "In 2020, the Certified Public Accountant (CPA) firm retained by Cal City to conduct the annual audit, advised that Cal City's books were unauditable."

vi. The Grand Jury's own finding: "To describe Cal City's general ledger and financial position as unauditable is shocking. Cal City must move on from past mismanagement and solve this dilemma."

vii. The Grand Jury's recommendation: "Under the direction of a qualified Finance Director, the City Council should assure Cal City's General Ledger is organized (per Generally Accepted Accounting Practices), so an independent financial audit can be completed by the end of every fiscal year."

The Grand Jury's recommendation above presumed a Finance Director would be in place to direct this effort. As discussed in Section IV Subsection 5, E&E was unable to identify any individual in the position of Finance Director since at least June 2022 **(See Schedule 15.4)**.

E&E's findings regarding the SDI Fund's general ledger, made independently of the City's own auditor, Bryant L. Jolley, CPA (fiscal years 2019 and 2020), and the Kern County Grand Jury (2021-2022), confirm that the same deficiencies persist today.

2. The City's Monthly Financial Statements Issued to the Public are Materially Inaccurate

a. Recurring Material Overstatements and Understatements of the SDI Fund's Investments

The City publishes monthly financial statements on its website, including a reported balance for the SDI Fund's investments. Every single monthly financial statement issued by the City and available on the City website has been inaccurate with respect to the SDI Fund's investments **(See Schedule 2)**. From March 2022 through December 2022, the City overstated the value of the SDI Fund's investments by an average of

approximately $6.3 million during that 10-month period, and as high as $8 million **(See Schedule 2)**. In the year 2026, the value of the SDI Fund's investments has been understated by approximately $10 million **(See Schedule 2)**.

The following is a sample of the City's understatement and overstatement of the SDI Fund's investments in its monthly financial statements:

Comparison of SDI Fund's Actual Investment Value To The City's Published Monthly Financial Statements

	Per Brokerage Statements	Per Monthly Financial Statements				
Period	Balance	Balance	Market Value Adjustment	Adjusted Balance	Difference	Overstatement/ Understatement
1/31/2021	88,300,630	90,730,230	(3,982,108)	86,748,123	1,552,507	Understatement
6/30/2021	87,800,526	90,730,230	(3,982,108)	86,748,123	1,052,403	Understatement
12/31/2021	87,119,557	92,650,610	(3,817,311)	88,833,299	(1,713,742)	Overstatement
3/31/2022	83,708,753	92,650,610	(3,817,311)	88,833,299	(5,124,545)	Overstatement
4/30/2022	82,882,397	94,570,990	(3,652,515)	90,918,475	(8,036,078)	Overstatement
5/31/2022	83,222,999	92,650,610	(3,817,311)	88,833,299	(5,610,300)	Overstatement
6/30/2022	82,548,002	92,650,610	(3,817,311)	88,833,299	(6,285,297)	Overstatement
7/31/2022	83,484,982	89,639,661	(1,839,135)	87,800,526	(4,315,543)	Overstatement
8/31/2022	82,207,868	89,639,661	(1,839,135)	87,800,526	(5,592,657)	Overstatement
9/30/2022	80,517,362	89,639,661	(1,839,135)	87,800,526	(7,283,164)	Overstatement
10/31/2022	80,349,785	89,639,661	(1,839,135)	87,800,526	(7,450,741)	Overstatement
11/30/2022	81,446,849	89,639,661	(1,839,135)	87,800,526	(6,353,677)	Overstatement
12/31/2022	81,268,550	89,639,661	(1,839,135)	87,800,526	(6,531,976)	Overstatement
1/31/2023	82,086,640	91,414,155	(8,866,153)	82,548,002	(461,362)	Overstatement
2/28/2023	80,920,934	91,414,155	(8,866,153)	82,548,002	(1,627,068)	Overstatement
3/31/2023	82,234,667	91,414,155	(8,866,153)	82,548,002	(313,335)	Overstatement
4/30/2023	82,692,319	91,414,155	(8,866,153)	82,548,002	144,318	Understatement
5/31/2023	82,524,230	91,414,155	(8,866,153)	82,548,002	(23,772)	Overstatement
6/30/2023	81,900,229	91,414,155	(8,866,153)	82,548,002	(647,773)	Overstatement
7/31/2023	82,116,665	91,414,155	(8,866,153)	82,548,002	(431,337)	Overstatement

8/31/2023	82,247,726	91,414,155	(8,866,153)	82,548,002	(300,276)	Overstatement
9/30/2023	82,186,564	91,414,155	(8,866,153)	82,548,002	(361,438)	Overstatement
10/31/2023	82,103,951	91,414,155	(8,866,153)	82,548,002	(444,051)	Overstatement
11/30/2023	83,346,153	91,414,155	(8,866,153)	82,548,002	798,151	Understatement
12/31/2023	84,630,872	91,414,155	(8,866,153)	82,548,002	2,082,870	Understatement
3/31/2024	84,982,521	91,414,155	(8,866,153)	82,548,002	2,434,519	Understatement
6/30/2024	84,901,921	91,414,155	(8,866,153)	82,548,002	2,353,919	Understatement
9/30/2024	88,421,116	91,414,155	(8,866,153)	82,548,002	5,873,114	Understatement
12/31/2024	87,519,835	91,414,155	(8,866,153)	82,548,002	4,971,833	Understatement
3/31/2025	89,426,580	85,453,094	(551,173)	84,901,921	4,524,659	Understatement
6/30/2025	90,747,955	85,453,094	(551,173)	84,901,921	5,846,034	Understatement
9/30/2025	90,025,891	85,453,094	(551,173)	84,901,921	5,123,970	Understatement
12/31/2025	93,292,986	85,453,094	(551,173)	84,901,921	8,391,065	Understatement
3/31/2026	93,960,973	85,453,094	(551,173)	84,901,921	9,059,052	Understatement
6/30/2026	93,492,204	84,453,094	(551,173)	83,901,921	9,590,283	Understatement
7/31/2026	93,634,638	84,453,094	(551,173)	83,901,921	9,732,717	Understatement

It is important to note that despite the City obtaining audited financial statements, which do state the accurate balances, the City continues to issue inaccurate financial information for the SDI Fund's investments. The investment balance published by the City remained identical each month, at exactly $84,901,921, from March 2025 through April 2026, despite the SDI Fund's actual investment balance reaching approximately $94.2 million as of April 2026, a difference of approximately $9.3 million **(See Schedule 2)**.

b. City Management's Failure to Ensure Reporting Accuracy in the City's Monthly Financial Statements

The Government Finance Officers Association ("GFOA") recommends that governments maintain an ongoing process of monthly, quarterly, and annual reviews to catch inaccurate or incomplete financial data[1]:

- "A government should undertake a process of monthly, quarterly, and annual reviews to ensure the ongoing completeness and accuracy of the data it collects. This process should include appropriate reconciliations to identify adjustments, as well as financial analysis of interim management reports to identify anomalous or incomplete data to be corrected."

- "The need for timeliness has to be balanced against the need for reliability, which also was identified as one of the characteristics of information in financial reporting identified in GASB Concepts Statement No. 1."

If the City had a monthly reconciliation process in place, it would have caught this discrepancy before it reached as much as $9.7 million **(See Schedule 2)**. The fact that it persisted, undetected, for years is a material control failure.

Governmental Accounting Standards Board Statement No. 72, Fair Value Measurement and Application[2] explains the importance of reporting investments at fair value:

- "Investments should be measured at fair value."

[1] Government Finance Officers Association, Timely Financial Reporting (best practice, approved September 25, 2020). Available at: https://www.gfoa.org/materials/timely-financial-reporting
[2] GASB, Statement No. 72 of the Governmental Accounting Standards Board, Fair Value Measurement and Application. Available at: https://www.gasb.org/page/ShowPdf?path=GASBS72.pdf&title=GASB%20STATEMENT%20NO.%2072,%20FAIR%20VALUE%20MEASUREMENT%20AND%20APPLICATION

- "Changes in the fair value of investments during the reporting period should be recognized."

- "In addition, investments reported in governmental fund financial statements, prepared using the current financial resources measurement focus and modified accrual basis of accounting, should be measured at fair value."

GASB adopted this requirement for the following reasons:

- "Fair value provides the best measure of a government's financial resources available to finance operations."

- "The changes in fair value are a faithful reflection of the increase or decrease in the financial resources available to the government to fund its activities."

- "The overall objective of financial reporting by state and local governments is to provide information to assist users (the citizenry, legislative and oversight bodies, and investors and creditors) in assessing the accountability of governments and in making economic, social, and political decisions."

As shown above, the balance the City has published for the SDI Fund's investments has never matched the investments' actual fair value in any month for which a comparison was possible in the last five years (2021 – 2026), with differences reaching as high as $9.7 million. The figures the City has issued to the public do not reflect the SDI Fund's actual financial resources, leaving the public without accurate information about the SDI Fund's true financial condition.

c. The Fair Market Value of the SDI Fund's Investments Was Readily Available to the City Each Month

The fair market value of the SDI Fund's investments is stated directly on the U.S. Bank custodian statements the City receives each month. The City needed only to transcribe a figure on the statements in its possession. The City's failure to adequately report the SDI's financial condition to the public each month cannot be attributed to the difficulty, cost, or complexity of determining the investment's fair market value.

d. The City's Monthly Financial Statements Do Not Disclose That They Are Unaudited or Should Not Be Relied Upon

Financial statements that have not been audited, reviewed, or otherwise verified should be clearly labeled as such. This convention is well established in the accounting profession, especially when issuing financial statements to the public. The AICPA's standards for accountants engaged to prepare financial statements require the following: a statement, on each page of the financial statements, disclosing that the financial statements "were not subjected to an audit, review, or compilation engagement" and that, accordingly, "no opinion, conclusion, or assurance" is provided on them.

The City's monthly financial statements include no such statement, or any other indication that the reported figures have not been verified or should not be relied upon. Without a disclosure statement regarding the reliability of the financial statements, a member of the public reviewing the City's monthly financial statements may reasonably rely on the financial statements as accurate financial information for making economic and political decisions.

Similarly, when the City's monthly financial statements do change from one month to the next, nothing in the statements indicates whether the change reflects actual transactions, or the correction of a previously reported error. A member of the public reviewing these statements has no way to distinguish the two.

As discussed above, the SDI Fund's investment balance published in the City's monthly financial statements differed from the actual balance by as much as $9.7 million, with no disclosure anywhere in those statements alerting the public that the figures might be inaccurate **(See Schedule 2)**.

3. The Treasurer's Reports Issued to the Public Overstated the SDI Fund's Primary Investment Account in 16 of 121 Months

The City separately publishes Treasurer's Reports, presented to the City Council, which include reporting for the SDI Fund's cash and investment balances by account. E&E compared the balances reported in the City's Treasurer's Reports to the corresponding brokerage, bank, and CD statements for each of the SDI Fund's cash and investment accounts, for the period June 2015 through June 2025.

Of the 121 months reviewed for the SDI Fund's US Bank Investments account, its largest holding, the majority were accurately stated. 16 months, however, overstated the account's balance, by an average of $873,566 and as much as $1,233,764, in August 2017 **(See Schedule 5.17)**

The Treasurer's Reports for the SDI Fund's cash and CD accounts were largely accurate with only immaterial discrepancies **(See Schedules 5.18 and 5.19)**.

4. The City’s Adopted Budget For the Fiscal Year 2026/27 Overstated the SDI Fund's FY2024 Investment Revenue by Approximately $12.1 Million

The City separately publishes an adopted budget. The City's Fiscal Year 2026/27 Final Budget was adopted on August 25, 2026, by Resolution No. 2026-3270, and includes a summary of the SDI Fund's revenues and expenditures. E&E compared the SDI Fund revenues reported in the City's Fiscal Year 2026/27 Adopted Budget to the corresponding audited financial

statements, the City's general ledger, and the underlying US Bank brokerage statements, for fiscal year 2024.

The Adopted Budget reports the SDI Fund's total FY2024 revenue as $15,170,704, consisting of $6,066,406 in "Investment Earnings" and $9,104,298 in "Net change in investments' FMV" **(See Schedule 5.16)**. The City's audited financial statements, general ledger, and US Bank brokerage statements each independently report the SDI Fund's actual FY2024 investment revenue as approximately $3.04 million, an overstatement in the Adopted Budget of approximately $12.1 million **(See Schedule 5.16)**.

Overstatement of SDI's 2024 Revenues

Source Document	Total Revenues
Per Adopted Budget	$ 15,170,704
Per Audited Financial Statements	$ 3,037,892
Per Detail Ledger	$ 3,037,892
Per US Bank Brokerage Statements	$ 3,025,351

5. <u>The City States That Quarterly Investment Reports Required by the SDI Ordinance and the City's Accounting and Investment Policies Do Not Exist for Periods Exceeding 10 Years</u>

As set forth in Section IV above, the SDI Ordinance states the following:

> "The Treasurer shall present quarterly reports on cash flow and the investments of the money in the SDI Fund to the SDI Advisory Committee, City Manager and the City Council. The report shall show: the type of investment; date of investment; how title is held; institution; date of maturity; par value; amount of each investment; current market value for all securities with a maturity of more than 12 months; rate of interest; confirmation that each investment is consistent with this investment policy; information showing expenditure requirements can be met in the following quarter; and specify which investments were made pursuant to Government Code Sections 53601(i), 53601.1 and 53635(i).

For money managed by LAIF, a county investment pool, or placed in FDIC insured accounts, the Treasurer may use the statement from these institutions in lieu of a separate report." **(See Exhibit 2)**

A substantially similar requirement is separately set forth in the City's Accounting and Investment Policies (Sec. 7.18) **(See Exhibits 12 and 13).**

E&E specifically requested the City's monthly, quarterly, and annual investment portfolio reports for the period July 1, 2014 through the present. In response, the City produced three quarterly reports, covering September 2024, December 2024, and March 2025, each prepared by the SDI Fund's broker rather than the City Treasurer or Finance Director as the SDI Ordinance and the City's Accounting and Investment Policies require. The City explicitly stated that "Documents beyond the three provided does not exist.'"

VII. The City's Unaccounted For, Unexplained, and Potentially Concealed Use of SDI's $1,354,346 Street Maintenance Reserve

1. Background: The SDI Fund's Street Maintenance Obligations and the City's Failure to Account or Produce Documents

a. Ordinance No. 98-552 and the SDI Fund's Obligation to Pay for Street Maintenance

City of California City Municipal Code Section 9-6.303, part of Ordinance No. 98-552 adopted by the City Council in January 1998, allows the City to transfer money out of the SDI Fund each year to pay for maintaining SDI-related street improvements and administrative expenses. The ordinance limits the transfers as follows:

> "Money shall annually be transferred from the SDI Fund to the City's General Fund for such purpose and shall not exceed the lesser of:

(1) $290,000.00 per fiscal year, which total may be an average of such expenditures over a four-year period.
(2) The amount of money in the SDI Fund attributable to investment earnings (as opposed to principal).
(3) The amount of money in the SDI Fund which the City Engineer and the Finance Director jointly certify to exceed the anticipated cost of constructing outstanding SDI Improvements for SDI Tracts.(k)
(4) The cost of maintaining SDI Improvements."

In simple terms, the City would be required to transfer the lower of the four amounts above, with $290,000 being the maximum.

b. The City's Audited Financial Statements Confirm It Has Not Accounted For SDI Street Maintenance Reserves, for Nine Consecutive Years

The ordinance names the General Fund as the recipient of SDI's payments for street improvements in accordance with Ordinance No. 98-552. The City's independently audited financial statements, however, state that the Street Maintenance Fund is also entitled to this money. The notes to the audited financial statements contain the same disclosure in every audit for the fiscal years ended June 30, 2016 through June 30, 2024, nine consecutive years. The most recent version, from the audit for the fiscal year ended June 30, 2024, reads as follows:

"On January 8, 1998, the City Council adopted Ordinance No. 98-552, authorizing annual transfers of up to $290,000 from the Subdivision Deferred Improvement (SDI) Fund for the maintenance of SDI improvements and related administrative expenses as provided under the ordinance.

During fiscal year 2015-2016, management reviewed current and prior year financial records and determined that the General Fund and

> Street Maintenance Fund incurred eligible expenditures as permitted by Article 3, Section 9-6303 (1)-(4), but the corresponding allowable transfers were not made. Management intends to perform an assessment in future years to determine the retroactive and cumulative maximum allowable transfers, which could result in a material transfer from the SDI Fund to the General Fund and/or Street Maintenance Fund.
>
> As of June 30, 2024, no determination has been made regarding the accumulation of allowable prior-year expenditures."

In plain terms, the audited financial statements state that at some point during the 2015-2016 fiscal year, the City reviewed its own financial records and determined that the General Fund and the Street Maintenance Fund had already incurred costs that should be applied to SDI's funds under the ordinance described above, but had not done an accounting of what was incurred.

c. <u>The City Has Not Provided an Accounting of What Was Spent, or What Remains of SDI's Street Maintenance Reserves</u>

The City's audited financial statements for fiscal years 2016 through 2024, the same nine consecutive years discussed in Section VII (1)(b) above, state that the General Fund and Street Maintenance Fund "incurred eligible expenditures as permitted by Article 3, Section 9-6303 (1)-(4)," the same provision quoted in Section VII (1)(a) above.

The City has not provided any accounting or verification of the eligible expenditures it says the General Fund and Street Maintenance Fund incurred, how much was spent, what it was spent on, or when it was spent. Without that information, there is no way to independently confirm the expenditures the City says occurred or reconcile them against what the SDI Fund has already contributed.

Robbie Cordes of the SDI Advisory Committee submitted approximately six public records requests (**See Exhibit 7**) which included a request for the following:

> "Information from 2016 – current related to City account 27-03140 Street Fund Reserve for SDI Streets specific to where money was spent/transferred and why account was removed from balance sheet (last known balance in account 1,354,316.00)"

As detailed in Section VII(1)(d) below, when E&E requested the specific accounting and banking records that would confirm the existence and amount of the City's alleged expenditures, the City represented that these records do not exist, or did not respond at all to E&E.

d. <u>The City Claims No Bank Records or Internal Accounting Records Exist and Fails to Respond or Produce General Ledgers: The Exact Documents It Needs to Perform the Accounting It Has Said It Intends to Do for Nine Years</u>

The SDI Advisory Committee claims that the City has not provided the SDI with any information detailing how much of the SDI's $1.3 million have been used, what the funds were used for, and if there were any funds left. In nine consecutive audited financial statements, the City has stated that it "intends to perform an assessment in future years to determine the retroactive and cumulative maximum allowable transfers." E&E requested the following documents from the City to investigate the use of SDI's funds for street maintenance. The City claims critical documents such as bank records and internal accounting records do not exist, and failed to respond to other basic requests as follows:

E&E Requests to the City Regarding SDI Reserves For Street Maintenance

Req. #	Section	Item Requested (Verbatim)	Response Category
86	VIII	"Banking records including but not limited to account opening documents, account closing documents, bank statements, cancelled checks, certificates of deposit, wire transfers, withdrawal slips, and deposit slips for all SDI funds held in Street Maintenance Fund Account 27-03140 for the years 7/1/2014 – Current. If the City maintains that that no documents exist, please explain how SDI funds are transferred to Street Maintenance Fund Account 27-03140 and whether such funds are deposited into a separate bank account for Street Maintenance Fund Account 27-03140."	Per Response Does Not Exist
87	VIII	"Investment account statements, investment account opening documents, and investment account closing documents for the years 7/1/2014 – Current."	No Response and No Documents Received
88	VIII	"General ledgers or detailed ledgers for the Street Maintenance Fund for the years 7/1/2014 – Current."	No Response and No Documents Received
89	VIII	"Any and all internal accounting records, ledgers, transaction registers, journal entries, and supporting documentation reflecting activity in Account 27-03140, including but not limited to records showing transfers, reimbursable costs, or allocations between the SDI Fund and Account 27-03140 SDI Street Reserves for the years 7/1/2014 - Current. All records sufficient to identify, calculate, and record transfers from the SDI Fund to the Street Maintenance Fund or track reimbursable expenses. If the City maintains that no records reflecting reimbursable costs to Street Maintenance Fund Account 27-03140 exist, please provide a written explanation as to how the City identifies and tracks such reimbursements."	Per Response Does Not Exist
92	VIII	Detail accounting of transactions and account balances for the Street Maintenance Fund Account #27-03140 for the years 7/1/2014 - Current. City internal financials including the Street Maintenance Fund Account #27-03140 for the years 7/1/2014 - 12/31/2020; 3/1/2021 - Current. Explanation of why the Street Maintenance Fund Account #27-03140 no longer appears in the City's internal financials after 2/28/2021.	Partially Available Online
93	VIII	"Bank reconciliations and investment account reconciliations relating to any bank account and investment account that holds funds relating to the Street Maintenance Fund Account 27-03140 (SDI Street Reserves) for the years 7/1/2014 – Current."	Per Response Does Not Exist
94	VIII	"Loan documentation for all loans active, outstanding, or in effect at any time during the period 7/1/2014 – Current, including loan agreements, promissory notes, escrow statements, board meeting minutes, legal documents, court rulings, correspondence, internal reports, internal calculations, and any other supporting documentation."	No Response and No Documents Received
95	VIII	"All audit-related records, communications, findings, workpapers, and supporting documentation prepared, maintained, reviewed, or relied upon in connection with the accounting, reporting, and audit of Street Maintenance Fund Account 27-03140 (SDI Street Reserves) for fiscal years 2014 through the present. Responsive records are not limited to documents titled 'audit finding' or 'management letter,' but include any materials reflecting auditor review, testing, analysis, or reporting relating to Fund 27-03140, regardless of how such records are labeled or stored. If the City contends that no audit-related records exist concerning Account 27-03140, please confirm in writing whether the City's auditors performed no audit procedures, issued no communications, and relied upon no supporting documentation regarding this account during the relevant period."	Per Response Does Not Exist

Bank statements and complete general ledgers are basic records that any city is expected to maintain for its own funds. The City has stated outright that banking records, internal accounting records, and reconciliations for the Street Maintenance Fund's Account 27-03140 do not exist. When E&E requested annual general ledgers for the Street Maintenance Fund, the City produced detail for one account only **(See Exhibit 8)**, not the

complete general ledgers requested, and did not respond when E&E followed up. For other requests, including investment account statements and loan documentation, the City did not respond at all, neither producing the records nor denying their existence.

The City's Accounting Policies and Procedures Manual states, “During the year and also as part of the fiscal year-end process, finance will insure that all journal entries have appropriate back up to substantiate the entry(s).” (Sec. 11.03.12) **(See Exhibit 12)**. To the extent the 'eligible expenditures' reflect payments to vendors for goods or services, the City's Accounting Policies and Procedures Manual would separately require these payments to be supported by an A/P package as follows:

> “The vendor invoices should be reviewed and approved by a department director prior to being processed for payment. All requests for payment to be submitted to finance shall include an A/P package. Each A/P package shall contain the following documents:
>
> a. Original invoice
> b. Packing Slip (where appropriate)
> c. Purchase Order…
> f. Any other supporting documentation deemed appropriate.
>
> All A/P packages must be approved by the department director.” (Sec. 4.02) **(See Exhibit 12).**

The City's representation that these records do not exist is inconsistent with its accounting policy requiring that such documentation be created and maintained for every journal entry and, to the extent these expenditures were vendor payments, for every disbursement.

It is not apparent how the City could perform the assessment it has told its auditors in nine consecutive years that it intends to perform, let alone

perform any accounting, conduct any transactions, or do anything at all with the funds in this account, without complete general ledgers, bank records, or reconciliations.

2. The SDI Fund's $1,354,346 Reserve Account in the Street Maintenance Fund

   a. The City's Books Confirm that $1,354,346 Was Held in the Street Maintenance Fund as SDI Reserves

   The City's accounting records identify a specific account within the Street Maintenance Fund, labeled "Reserve for SDI Streets" (Account 27-03140), designated for maintaining SDI street improvements. This account appears in two of the City's accounting records: the Street Maintenance Fund's general ledger and the City's monthly financial statements issued on its website.

   As of February 2021, the last month the City reported this account separately in its monthly financial statements, the balance was $1,354,346 **(See Schedule 3)**. The Street Maintenance Fund's general ledger for this account shows the same balance, $1,354,346, as its opening balance as of July 1, 2014, the earliest date reflected in that ledger.

   Both records, independently of each other, confirm the same amount, held in the same specifically designated account, held for SDI's benefit.

   It is important to note that E&E was not provided with sufficient records to independently verify the accuracy or existence of SDI's disbursements to the Street Maintenance Fund. However, based on the 2013 and 2014 audited financial statements, the SDI Fund transferred $290,000 in fiscal year 2013 and $137,492 in fiscal year 2014, both prior to the July 1, 2014 opening balance of the Reserve for SDI Streets Account in the general ledger. These two confirmed transfers total $427,492. E&E has not been able to confirm the source of the remaining $926,854 of the $1,354,346 balance.

Based on the information available, E&E has assumed that the Reserve for SDI Streets Account relates to monies transferred by the SDI Fund to the Street Maintenance Fund in connection with Ordinance No. 98-552.

3. The City's General Ledger Accounting of the SDI Fund's Street Maintenance Reserve Account

   a. The City's General Ledger Recording: The SDI Reserve Account Was Written Off in 2019, Restored in 2019/2020, and Then Retroactively Eliminated in 2021, All Without Any Explanation

   The Street Maintenance Fund's general ledger for Account 27-03140, "Reserve for Sdi Streets," shows the account balance at $1,354,346 from its earliest recorded date, July 1, 2014, through 2019 **(See Exhibit 8)**.

   On June 30, 2019, the City recorded Journal Entry #20, referenced "PPC-039 Reserve for Sdi Streets," effectively writing off the account to a zero balance. **(See Exhibit 8).**

   The following month, on July 1, 2019, the City restored the balance to its original amount of $1,354,346, and that balance remained through 2021 **(See Exhibit 8)**.

   Finally, on April 22, 2021, the general ledger was modified to eliminate the balances in the account beginning July 2019 and forward, to be zero **(See Exhibit 8)**. Effectively, the modifying entry is stating that the SDI Fund's reserves were completely used up by the City and there were no reserves remaining, since the balance in the account was modified to zero. The zero balance remained in the general ledger account through 7/31/2025, the last date the general ledger account was maintained by the City, based on the records provided **(See Exhibit 8)**.

The City's monthly financial statements for this same period, which were never amended or restated, continued to show the account at $1,354,346 through February 2021 **(See Schedule 3)**.

With the exception of the single journal entry recorded on June 30, 2019, every entry in the general ledger for this account, from 2014 through 2025, is either an opening balance entry or a modification to an opening balance **(See Exhibit 8)**. None of these entries include any description or explanation for why it was made. The one exception, Journal Entry #20, includes only the notation "PPC-039," which E&E has not been able to interpret.

It is important to note that during the same time that the general ledger account was eliminated to a zero balance in 2021, the City's audited financial statements continued to state that the City had not performed an accounting of how much of SDI's reserves were used (see Section VII (1)(b) above). Accordingly, the City's elimination of the SDI's reserve account in its general ledger is inconsistent with what the City reported to the public in its audited financial statements. The City cannot have genuinely never performed the assessment it told its auditors was still pending, while its own books show it had already eliminated the account that assessment would apply to.

4. The Monthly Financial Statement Accounting of the SDI Fund's Street Maintenance Reserve Account

   a. The City's Monthly Financial Statements: The SDI Street Reserve Account is Consolidated with Other Accounts, Rendering it Untraceable

   As of February 2021, the City's monthly financial statements for the Street Maintenance Fund were reported on an itemized basis with each account reported separately **(See Schedule 3)**. With this method of presentation, any reviewer of the City's monthly statements can see the balances in each of six accounts including the account "Reserve for SDI Streets."

Inexplicably, in March 2021 it appears that all of the accounts were consolidated into a single combined total in the account titled, "Retained Earnings" **(See Schedule 3)**. Under this new method of presentation, there is no reporting on the balances of each of the six specific accounts, including the account "Reserve for SDI Streets."

The following chart reflects the change in presentation of the monthly financial statements and the lack of transparency as to the account "Reserve for SDI Streets":

Account (City Ledger Code)	February 2021 (and prior)	March - June 2021
Retained Earnings (27-03110)	$ (620,913.91)	$ 1,096,055.25
Residual Equity Transf In/Out (27-03112)	133,814.07	-
Reserve for Prepaid Exp (27-03117)	13,438.12	-
Reserve for Parsac (27-03120)	100,000.00	-
Reserve for Street Improvement (27-03131)	200,000.00	-
Reserve for SDI Streets (27-03140)	1,354,346.00	-
Prior Period Adjustment (27-03199)	-	60,539.77
Total	**$ 1,180,684.28**	**$ 1,156,595.02**

Before March 2021, anyone reading the City's books could see that $1,354,346 was being held in a specific account for SDI street reserves. After March 2021, that same information is no longer available, as six accounts are consolidated into a single number. As the total consolidated balance changes, it is impossible to know which of the six accounts caused that change.

b. <u>The City's Monthly Financial Statements: A Negative Balance in the Consolidated Account Indicates the SDI Street Reserve Was Fully Depleted</u>

Before March 2021, the $1,354,346 reserve was held in its own separately designated account. Regardless of what changed in the Street

Maintenance Fund's finances, the amount designated for SDI streets remained separately identified at $1,354,346.

The March 2021 consolidation removed that separation. Once the reserve was consolidated with Retained Earnings and the fund's other accounts into a single balance, there was no longer any boundary keeping the SDI-designated money separate from the fund's ordinary operating results. From that point forward, any loss the Street Maintenance Fund experienced reduced the same consolidated balance that included the SDI reserve.

After the consolidation occurred in March 2021, the six consolidated accounts dropped to a negative balance for several consecutive months, from August 2023 through June 2024, reaching as low as $(45,104.25) **(See Schedule 3)**. The following chart reflects the decline in the consolidated account:

Date	Balance	Notes
March 2021	$ 1,096,055.25	Includes the $1,354,346 SDI Streets Reserve
December 2021	761,145.08	
December 2022	322,168.35	
August 2023	(44,944.25)	First negative balance
September 2023	(44,944.25)	
October 2023	(44,944.25)	
November 2023	(44,944.25)	
December 2023	(44,944.25)	
January - March 2024	No Statement Issued	Three-month reporting gap
April 2024	(45,104.25)	Lowest point reached
May 2024	(45,104.25)	
June 2024	(45,104.25)	
July 2024	244,937.52	Return to a positive balance
March 2025	743,775.07	
March 2026	4,950,392.42	

For the consolidated balance to go negative, the entire amount attributable to the $1,354,346 SDI Streets Reserve must have been used, along with everything else in the consolidated account. A negative combined balance

means the Street Maintenance Fund had no remaining resources available to cover the $1,354,346 reserve. Based on our findings, the SDI Fund's Reserve in the Street Maintenance Fund, to be used for SDI purposes, was instead depleted and may have been used for other purposes unrelated to the SDI Fund.

5. Potential Concealment of the City's Unexplained Write Off

   a. The SDI Reserve Disappeared from Public Reporting and Was Retroactively Written Off from the General Ledger Shortly After

   As discussed in Section VII(4) above, beginning with the monthly financial statement covering March 2021, the SDI Street Reserve Account no longer appeared as its own line in the City's monthly financial statements. From that point forward, there was no way to see the account's balance, or any activity in it, anywhere in the City's public reporting.

   A few weeks later, as discussed in Section VII(3) above, the City's general ledger for the SDI Street Reserve Account was retroactively modified on April 22, 2021, to show a zero balance for fiscal years 2019-2021 **(See Exhibit 8)**. It is important to note that the balance in the account was modified to prior years where the monthly financial statements were already issued. During this period of time, no audits were completed for several calendar years. Accordingly, the public's only source of information on this account, the monthly financial statements showing a balance of $1,354,346, was materially different from what the City's modified general ledger reflects for that same period.

   The account's disappearance from public reporting and the retroactive elimination of its balance in the general ledger occurred within a very short time of each other. Neither action includes any explanation. Furthermore, the City continued to report on its audited financial statements that it did not perform an accounting of how much of the SDI Reserves were used or owed.

Accordingly, E&E was not able to determine whether the timing of the SDI Street Reserve Account's disappearance from public reporting and its inexplicable write-off in the general ledger were meant to conceal the use of the SDI Reserves. However, the timing and lack of transparency is a red flag, especially considering the write-off itself is inconsistent with the City's audited financial statement disclosures.

VIII. Performance of SDI Fund Investments and Non-Compliance with Investment Goals and Policies

1. Background of SDI Fund Investments and Historical Performance

The SDI Fund's investments are by far its largest asset, every year from 2015 to the present, approximating $94 million as of July 31, 2026 **(See Schedule 2.5)**. Substantially all of the investments are held in a single U.S. Bank brokerage account. The figures presented in this section are drawn from U.S. Bank custodian account statements covering 12 years **(See Schedule 2.5)**.

Under §3-2.502(c) of the City's Municipal Code **(See Exhibit 9)**, the Finance Director and Treasurer are required to select the SDI Fund's investment mix in accordance with three stated goals, in order of priority:

a) Safeguarding principal;
b) Meeting liquidity needs; and
c) Achieving return on investment.

This order of priority reflects the standard recommended nationally for public investment policies by the GFOA.[3]

[3] GFOA Best Practice, Creating an Investment Policy (2010), stating: "The most prudent primary objectives for drafting a sound investment policy should be: safety, liquidity, and yield, in that order."

The following chart reflects the fair market value of the investments from 2015 to 2025 **(See Schedule 2.2)**:

Fair Market Value of Investments, 2015 - 2025

Date	Fair Market Value	% Change
December 31, 2015	$ 82,978,582.15	
December 31, 2016	83,334,486.40	+0.43%
December 31, 2017	84,498,911.72	+1.40%
December 31, 2018	85,520,244.51	+1.21%
December 31, 2019	88,142,355.38	+3.07%
December 31, 2020	89,191,112.74	+1.19%
December 31, 2021	87,642,678.63	-1.74%
December 31, 2022	81,855,635.83	-6.60%
December 31, 2023	85,458,264.65	+4.40%
December 31, 2024	88,308,938.94	+3.34%
December 31, 2025	94,071,552.79	+6.53%

From at least January 2013 through October 2016, brokerage services for the SDI Fund's investments were provided through Stifel, Nicolaus & Company, Incorporated ("Stifel"), with Ronald C. Gross acting as a broker. The last SDI Fund transaction identified during this period is dated October 17, 2016, the same date FINRA records reflect the end of Mr. Gross's registration with Stifel.

From October 2016 through December 2020, a period of approximately four years, no brokerage activity occurred on the SDI Fund's investment account. During this approximately four-year period, there were no purchases or sales, and the investments in the account remained virtually untouched. The investments in the account matured according to their scheduled terms and were automatically deposited into the account's default money market fund. The SDI Fund's custodian-reported value continued to grow modestly from interest and maturities during this four-year period of no brokerage activity, beginning at $84.6 million in October 2016 and reaching approximately $89.3 million by November 30, 2020, an increase of approximately $4.7 million **(See Schedule 2.5)**.

Around December 2020, Mr. Gross again served as a broker on the account, this time through SSDW. No engagement agreement, contract, or Council-approved intermediary agreement governing either Stifel, Nicolaus & Company's relationship or SSDW's relationship with the City was produced by the City. FINRA records reflect that Mr. Gross's registration with SSDW ended in July 2025.

Within weeks of SSDW's commencement as the broker in December 2020, the composition of the SDI Fund's investments changed substantially. Corporate bonds, which had not appeared in the portfolio at any point since at least 2013, were purchased in an aggregate face amount of approximately $27.9 million between the one-month period of November 30, 2020 and December 31, 2020, immediately after SSDW's commencement as the broker **(See Schedule 2.5)**. Municipal bonds, also absent from the portfolio in prior years, grew to approximately $53.9 million by fiscal year-end 2020-21 **(See Schedule 2.5)**. The following chart reflects the mix of the SDI Fund's investments as of November 30, 2020, the last month-end before SSDW commenced as the broker, and as of December 31, 2022 **(See Schedule 2.3)**:

Mix of Investments: November 30, 2020 vs. December 31, 2022

Asset Type	November 30, 2020	% of Total	December 31, 2022	% of Total
Cash Equivalents	$ 41,141,456	46.1%	$ 12,159,906	14.9%
US Government Issues	47,624,923	53.3%	-	0.0%
Corporate Issues	-	0.0%	23,129,345	28.3%
Foreign Issues	-	0.0%	-	0.0%
Municipal Issues	-	0.0%	45,979,298	56.2%
Global Corporate Obligations	-	0.0%	-	0.0%
Accrued Income	533,869	0.6%	587,086	0.7%
Total	**$ 89,300,248**	**100.0%**	**$ 81,855,636**	**100.0%**

As reflected above, the SDI Fund's cash position declined from 46.1% to 14.9% over this period, indicating that a substantial portion of previously idle cash, in addition to the SDI Fund's U.S. government issue holdings, was

deployed into corporate and municipal bonds. This decline was immediate rather than gradual, as reflected in the following chart **(See Schedule 2.4)**:

Cash Equivalent Balance: November 2020 - December 2022

Month-End	Cash Equivalents	% of Total Investments
November 30, 2020	$ 41,141,456.35	46.07%
December 31, 2020	$ 7,165,807.63	8.03%
June 30, 2022	$ 6,204.22	0.01%
October 31, 2022	$ 320,272.79	0.40%
December 31, 2022	$ 12,159,906.26	14.86%

The SDI Fund's cash position dropped from $41.1 million to $7.2 million within a single month of SSDW's commencement as the broker and remained low over the following two years, at one point falling to just $6,204, before recovering to $12.2 million by December 31, 2022.

Following SSDW's commencement as the broker, the SDI Fund's total investment balance declined from approximately $88.8 million in November 2020, immediately prior to SSDW's commencement as the broker, and reached a low of approximately $80.3 million as of October 31, 2022, a decrease of approximately $8.5 million or 9.5% **(See Schedule 2)**.

The City's monthly financial statements did not reflect this decline of approximately $8.5 million. Instead, the reported investment balance either overstated or understated the SDI Fund's actual value in every month for which a comparison could be made during this period, growing from an understatement of approximately $1.5 million in January 2021 to an overstatement of approximately $7.5 million by October 2022. A member of the public relying on the City's monthly financial statements during this period would not have known that the SDI Fund had lost millions of dollars in value.

From December 31, 2023, to December 31, 2025, the SDI Fund's investments then grew from approximately $85.5 million to approximately $94.1 million, an increase of approximately $8.6 million or 10%, **(See Schedule 2.5)**.

2. Sale of Bonds Prior to Maturity

a. Approximately 93% of SDI Fund's Bonds Disposed of Were Sold Prior to Maturity

E&E reviewed the SDI Fund's complete transaction history in its U.S. Bank brokerage account for the years 2013 through 2025. The SDI Fund's bond dispositions consisted of the following **(See Schedule 4)**:

Disposition Type	U.S. Government Issues	Municipal Issues	U.S. Corporate Issues	Total
Sale	177	53	26	256
Matured	10	1	0	11
Called by Issuer	0	6	1	7
Total	**187**	**60**	**27**	**274**

Accordingly, 256 bonds or approximately 93% of the bonds disposed of by the SDI Fund, were bonds sold prior to their maturity dates **(See Schedule 4)**. Selling a bond before its stated maturity date carries the following risks:

- The seller forgoes any interest payments the bond would otherwise have paid between the sale date and its original maturity date;

- The seller receives the price the bond can command in the market on the sale date rather than the bond's full stated principal value.

The price of the bond moves in the opposite direction of prevailing interest rates. If rates have risen since the bond was purchased, its market value will typically have fallen, and a sale at that point realizes a loss. If rates

have fallen, its market value will typically have risen, and a sale at that point realizes a gain. Holding a bond to maturity generally avoids this exposure altogether, returning the bond's full stated principal value regardless of how interest rates moved in the interim.

Approximately 120 or 47% of the SDI Fund's bond sales were sold prior to maturity during times when interest rates were higher than when the bonds were originally purchased **(See Schedule 4.2)**. In approximately 114 of these instances, the SDI Fund sold the bonds for losses and also missed out on future interest payments it would have been entitled to **(See Schedule 4.2)**.

Given that safeguarding the principal of the SDI Fund is the primary investment goal under §3-2.502(c) of the City's Municipal Code, the fact that approximately 47% of SDI Fund's bond sales occurred when interest rates were higher than when the bonds were purchased (resulting in losses) rather than held to maturity, is directly relevant to whether that primary goal was met.

b. GFOA Confirms Selling Prior to Maturity Poses Market Risk

The GFOA's "Managing Market Risk in Investment Portfolios" best practice states:

> "Many government investors employ a buy-and-hold approach, so that changes in a security's market value are never realized and the full-face value of the security is received upon maturity... Circumstances may arise in which an entity is forced to sell a security before its maturity. In such instances, a government entity may have to accept a loss on a security that it had never planned to sell. Market risk is a critical risk for a government investor. Therefore, it is necessary to understand fully the maturity structure of securities before investing."

3. Corporate Bonds Purchased for the SDI Fund Are Not Permitted Per the City's Municipal Code, and When Purchased, Caused a Loss for the SDI Fund Approximating $1.9 million

   a. The City's Municipal Code Does Not Permit Investment in Corporate Bonds

   Beginning immediately after SSDW's commencement as the broker, the City invested significant resources in corporate bonds for the SDI Fund. In this regard, the City's Municipal Code **(See Exhibit 9)** contains a list of permitted investments of which corporate bonds are not included.

   The City's Municipal Code also makes reference to the following:

   > "In making investments of money in the SDI Fund, the City shall comply with the limitations contained in the Government Code, including Section 53601, and this Chapter. If there is a conflict between State law and this Chapter, the most conservative investment rule shall prevail if the rule is permitted by State law." (§3-2.502(b))

   The City's Accounting and Investment Policies authorize investment in medium-term notes, a category that includes corporate notes, subject to the following limits: no more than 30% of the portfolio, a maximum maturity of five years, and a minimum credit rating of "A" (Sec. 7.08) **(See Exhibits 12 and 13)**.

   E&E has reviewed California Government Code §53601(k)[4] which states as follows:

[4] California Government Code § 53601. Available at: https://leginfo.legislature.ca.gov/faces/codes_displaySection.xhtml?sectionNum=53601.&nodeTreePath=6.2.1.11.1&lawCode=GOV

- "'Medium-term notes' are defined in Section 53601 as 'all corporate and depository institution debt securities with a maximum remaining maturity of five years or less, issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States.'"

- "Notes eligible for investment under this subdivision shall be rated in a rating category of 'A' or its equivalent or better by an NRSRO. Purchases of medium-term notes shall not include other instruments authorized by this section and shall not exceed 30 percent of the agency's moneys that may be invested pursuant to this section."

In summary, corporate bonds are not included in the City's Municipal Code's list of permitted investments. The City's Accounting and Investment Policies and California Government Code §53601(k) authorize medium-term notes, including corporate notes, only within the limits described above. As described below, the SDI Fund's corporate bond holdings exceeded the 30% limit for approximately 24 months, and the SDI Fund purchased a corporate bond with a maturity exceeding five years.

b. Corporate Bond Losses

The SDI Fund's total losses on corporate bond sales were $1,852,565 between the years 2013 and 2025. This represented 31.44% of the SDI Fund's total realized investment losses **(See Schedule 13)**. Approximately 25.6 million units of corporate bonds were sold prior to their maturity dates.

E&E compared the SDI Fund's corporate bond holdings, held from fiscal year 2021-22 through fiscal year 2024-25, to the Bloomberg US Corporate 1-5 A or Higher Index, a benchmark comprising similarly-rated corporate holdings of comparable maturity. Over this period, the SDI Fund's corporate bond holdings underperformed this benchmark in 3 of 4 fiscal years, by an average underperformance of 4.92% per fiscal year **(See Schedule 6)**.

These losses were incurred on an asset class not permitted under the City's Municipal Code, suffered by the SDI Fund whose primary stated goal is to safeguard principal.

c. Corporate Bonds Exceeded the 30% Limit in California Government Code and the City's Accounting and Investment Policies

As stated above, California Government Code §53601(k) provides that "purchases of medium-term notes...shall not exceed 30 percent of the agency's moneys that may be invested pursuant to this section."

The City's Accounting and Investment Policies set the same 30% limit (Sec. 7.08) **(See Exhibits 12 and 13).**

E&E identified 24 months in which corporate bonds exceeded 30% of the SDI Fund's investments, in apparent excess of these limits **(See Schedule 2.4)**

From December 2020 through July 2023, SDI's corporate bonds averaged 30.07% of the SDI Fund's total assets available for investment **(See Schedule 2.4)**. Within this period, two stretches averaged above 31%: December 2020 through June 2021, averaging 31.05%, and February 2023 through May 2023, averaging 31.30% **(See Schedule 2.4)**.

Considering the number one goal of the SDI Fund is to safeguard its investments, it is relevant that corporate bonds exceeded the maximum allowable percentage under California Government Code and the City's Accounting and Investment Policies over these extended periods of time. For a fund with a goal of safeguarding its investments, corporate bond holdings are inherently riskier than government bonds, and you would expect them to remain well below the 30% maximum, not consistently at or above it.

d. Long Term Corporate Bond Purchased That Exceeded the Five-Year Maturity Limit in California Government Code and the City's Accounting and Investment Policies

On May 29, 2024, the SDI Fund purchased a corporate bond issued by Metropolitan Detroit Area Hospital (CUSIP 591863AA3), maturing December 1, 2029. This bond carried a maturity of approximately 5.51 years from its date of purchase, exceeding the five-year limit **(See Schedule 7)**.

California Government Code §53601 prohibits investments with a remaining maturity of more than five years unless the legislative body has expressly authorized them at least three months in advance. For medium-term notes, which include corporate bonds, §53601(k) sets "a maximum remaining maturity of five years or less."[5] The City's Accounting and Investment Policies likewise limit medium-term notes to a maximum maturity of five years (Sec. 7.08) **(See Exhibits 12 and 13)**. Separately, the City's Municipal Code requires that "no long-term investment shall be made unless the Council has granted express authority to make the investment… no less than three months prior to the investment purchase date." In this regard, E&E has not identified any express authorization for the purchase of any bonds with a maturity exceeding five years.

[5] California Government Code § 53601. Available at: https://leginfo.legislature.ca.gov/faces/codes_displaySection.xhtml?sectionNum=53601.&nodeTreePath=6.2.1.11.1&lawCode=GOV

GFOA's Managing Market Risk in Investment Portfolios best practice states: "Generally, the longer the maturity of a security, the greater its market risk as measured by price volatility. Longer maturities have greater volatility because as the time to maturity increases, each change in interest rates has a greater impact on the present value of a security."[6]

This bond was not permitted by the City's Municipal Code and exceeded the maturity limit stated in California Government Code §53601(k) and the City's Accounting and Investment Policies. For a fund whose primary investment goal is to safeguard its principal, this bond carried a longer maturity and higher risk than allowed.

As described in Section VIII(5) below, E&E identified additional instances when SDI investments exceeded the 5-year statutory and policy maturity limit, beyond the corporate bond identified in this section.

e. Corporate Bonds Did Not Exist in the SDI Fund's Portfolio Prior to December 2020

From at least fiscal year 2012-13 through fiscal year 2019-20, a period of at least seven consecutive fiscal years, the SDI Fund's bond holdings consisted entirely of U.S. Government Issues. Corporate bonds were not held in the SDI Fund's portfolio at any point during the period E&E reviewed prior to December 2020. Corporate bonds first appear in the SDI Fund's holdings in fiscal year 2020-21, coinciding with SSDW's commencement as the SDI Fund's broker in December 2020 **(See Schedule 2.5)**.

[6] GFOA, Managing Market Risk in Investment Portfolios. Available at: https://www.gfoa.org/materials/managing-market-risk-in-investment-portfolios.

f. Corporate Bonds Carry Risk to the SDI Fund That Direct U.S. Government Obligations Do Not

It is widely understood that corporate bonds are riskier than government bonds.

A corporate bond depends on the issuing company's own financial condition for repayment, an obligation that carries a risk direct U.S. government obligations do not. This concept is explained by FINRA as follows:

> "Certain bonds—notably U.S. Treasury securities—are generally considered low risk since they're backed by the U.S. government. But this low risk status doesn't apply to other bonds."[7]

This is also confirmed by the SEC:

> "One key risk to a bondholder is that the company may fail to make timely payments of interest or principal. If that happens, the company will default on its bonds. This 'default risk' makes the creditworthiness of the company—that is, its ability to pay its debt obligations on time—an important concern to bondholders."[8]

Coutts & Co. states the comparison directly:

> "Corporate bonds are tools for companies to raise debt, funded by investors. They are typically seen as riskier than government bonds because companies are seen as more likely to default on repayments as they lack the authority of a government to increase income if

[7] SEC Office of Investor Education and Advocacy, What Are Corporate Bonds?, Investor Bulletin. Available at: https://www.investor.gov/introduction-investing/general-resources/news-alerts/alerts-bulletins/investor-bulletins/what-are.
[8] FINRA, Bond Investing and Due Diligence. Available at: https://www.finra.org/investors/insights/bond-investing-due-diligence.

needed... Given the nature of these bonds compared to government bonds, investors demand a higher return to compensate for the greater risk"[9]

When SSDW commenced as the SDI Fund's broker in December 2020, the SDI Fund immediately went from no corporate bonds to 31.26% of its entire portfolio **(See Schedule 2.4)**, a riskier investment strategy than the SDI Fund's history had seen.

4. Foreign Bank Notes Held by the SDI Fund Are Not Permitted by the City's Municipal Code or the City's Accounting and Investment Policies, and Do Not Appear to Be Consistent with California Government Code

   a. Foreign Bank Notes Held by the SDI Fund Are Not Permitted by the City's Municipal Code or the City's Accounting and Investment Policies

   The SDI Fund purchased notes issued by two foreign-domiciled banks: Royal Bank of Canada (CUSIP 78016FZW7, a 4.900% note due January 12, 2028) and The Toronto-Dominion Bank (CUSIP 89115A2M3, a 5.156% note due January 10, 2028). Both notes were purchased on September 27, 2023, in the par amount of $1,300,000 each.

   Neither note is guaranteed by a government agency of Canada or the United States. Per Royal Bank of Canada's own Pricing Supplement for this note, dated January 9, 2023: "The Notes are unsecured and are not savings accounts or insured deposits of a bank. The Notes are not insured or guaranteed by the Canada Deposit Insurance Corporation, the U.S. Federal Deposit Insurance Corporation or any other governmental agency or instrumentality of Canada or the United States." The Toronto-

[9] Coutts & Co., Corporate vs government bonds – a risk-return crossroad (Sept. 4, 2025). https://www.coutts.com/insights/global-finance/corporate-vs-government-bonds.html

Dominion Bank's Pricing Supplement for its note, dated January 3, 2023, contains the same statement.[10]

Neither note is included in the City's Municipal Code's list of permitted investments. The City's Municipal Code's list of permitted investments includes only specific categories of federally-guaranteed obligations, California state and local government instruments, and domestic bank deposits secured by federal insurance. The Royal Bank of Canada and Toronto-Dominion Bank notes are neither issued nor guaranteed by any of the entities identified in that list, nor are they secured by federal insurance. Accordingly, these two purchases do not fall within any of the eight categories of investments permitted under the City's Municipal Code.

The City's Accounting and Investment Policies likewise do not authorize these notes. They authorize medium-term notes only as "obligations of a domestic corporation or depository institution" (Appendix A), and state: "If a type of security is not specifically authorized by this policy, it is not a permitted investment." (Sec. 7.08) **(See Exhibits 12 and 13)**. Royal Bank of Canada and The Toronto-Dominion Bank are Canadian banks.

b. Foreign Bank Notes Held by the SDI Fund Do Not Appear to Be Consistent with California Government Code

The California Debt and Investment Advisory Commission ("CDIAC"), a unit of the California State Treasurer's Office, has published guidance stating that securities issued by "Royal Bank of Canada" are not allowable investments for California local agencies:

[10] The Toronto-Dominion Bank, Pricing Supplement dated January 3, 2023, 5.156% Senior Medium-Term Notes, Series C, Due 2028, filed with the SEC under Rule 424(b)(2). https://www.sec.gov/Archives/edgar/data/947263/000119312523001559/d240456d424b2.htm

> "Securities issued by 'Royal Bank of Canada' are not allowable investments for California local agencies because it is not a licensed and operating U.S. depository institution under the name of 'Royal Bank of Canada', but rather licensed and operating in the U.S. as 'RBC Bank'."[11]

The note purchased by the SDI Fund was issued in the name "Royal Bank of Canada." The Toronto-Dominion Bank note was likewise issued by the Canadian parent bank, not by a U.S.-licensed affiliate. Based on CDIAC's guidance, these notes do not appear to be consistent with the requirements of California Government Code §53601(k).

5. Approximately 17% of SDI Fund Bond Purchases Exceeded the Statutory and Policy Maturity Limit of 5 Years

E&E identified 64 bond purchase transactions, or approximately 17% of the 377 total bond purchase transactions for the years 2013 through 2025, in which the security purchased had a maturity date more than five years from its purchase date. These 64 transactions consisted of the following:

Security Type	Number of Purchases Exceeding 5 Years Maturity
Municipal Issues	47
U.S. Government/Agency Issues	16
U.S. Corporate Issues	1
Total	**64**

The 16 U.S. Government/Agency Issues were purchased between 2013 and 2014, with maturity dates in 2018 and 2019, predating SSDW's December 2020 commencement as the broker **(See Schedule 7)**. The 47 Municipal Issues were purchased primarily between 2021 and 2024. The one U.S.

[11] California Debt and Investment Advisory Commission, Investments under Government Code 53601 – Focus on Securities Issued by Foreign Entities and Foreign Affiliates – 2025 Update, CDIAC No. 25-01. Available at: https://www.treasurer.ca.gov/cdiac/publications/issue-brief/2025/25-01.pdf.

Corporate Issue, discussed in Section VIII(3) above, was purchased in 2024 **(See Schedule 7)**.

Of these 64 transactions, the longest maturity identified was a $3,900,000 municipal bond (CUSIP 55178CAG8, "LYNWOOD-TXBL"), purchased September 23, 2022, with a maturity date of September 1, 2029, approximately 6.95 years from its date of purchase, or nearly 39% longer than the five-year limit stated above.

California Government Code §53601 prohibits investments with a remaining maturity of more than five years unless the legislative body has expressly authorized them at least three months in advance. For medium-term notes, which include corporate bonds, §53601(k) sets a five-year maximum.

Separately, and applicable to all investment types, the City's Municipal Code states:

> "Investments may be short-term or long-term in nature. Long-term investments are those which comply with the requirements of Government Code Sections 53601 et seq. and with a stated maturity date greater than five years from the date of purchase. No long-term investment shall be made unless the Council has granted express authority to make the investment either specifically or as a part of an investment program no less than three months prior to the investment purchase date." (§3-2.501(c))

The City's Accounting and Investment Policies similarly state: "Unless matched to a specific requirement and approved by the City Council, no investment may be made with maturity greater than five (5) years." (Sec. 7.15) **(See Exhibits 12 and 13)**.

E&E has not identified any record of Council authorization, granted either specifically or as part of an investment program at least three months prior to purchase, for any of the 64 purchases identified above.

GFOA's Managing Market Risk in Investment Portfolios best practice states:

> "Generally, the longer the maturity of a security, the greater its market risk as measured by price volatility. Longer maturities have greater volatility because as the time to maturity increases, each change in interest rates has a greater impact on the present value of a security."[12]

The U.S. Securities and Exchange Commission similarly states:

> "The price of a bond moves in the opposite direction than market interest rates—like opposing ends of a seesaw. This presents investors with interest rate risk, which is common to all bonds. In addition, the longer the bond's maturity, the more time there is for rates to change and, as a result, affect the price of the bond. Therefore, bonds with longer maturities generally present greater interest rate risk than bonds of similar credit quality that have shorter maturities."[13]

For the SDI Fund, whose primary investment goal is to safeguard its principal, 64 purchases or approximately 17% of all purchases over a decade, carried a maturity longer than the five-year limit stated above, without any identified record of the Council authorization required for such purchases. Accordingly, these purchases were inconsistent with the City's Municipal Code, the City's Accounting and Investment Policies, California Government Code, and the stated investment goal of the SDI Fund.

[12] GFOA, Managing Market Risk in Investment Portfolios. Available at: https://www.gfoa.org/materials/managing-market-risk-in-investment-portfolios.
[13] SEC Office of Investor Education and Advocacy, What Are High-yield Corporate Bonds?, Investor Bulletin. Available at: https://www.investor.gov/introduction-investing/general-resources/news-alerts/alerts-bulletins/investor-bulletins/what-are-0.

6. SDI Purchased Six Bonds That Exceeded the City's and GASB's 5% Concentration of Credit Risk Threshold, Which Went Undisclosed

   a. The City's Accounting and Investment Policies Limit Investment in Any Single Issuer to 5%

   The City's Accounting and Investment Policies state the following:

   > "The City cannot invest any more than 5% maximum of the portfolio in any single issuer's bond debt, except U.S. Government, its agency or the State of California Local Agency Investment Fund and Kern County Investment Fund." (Sec. 7.03.01(A)(4)) **(See Exhibits 12 and 13).**

   Separately, the City's Accounting and Investment Policies state:

   > "The City of California City Portfolio at the time of investment will use a guideline of 5% limit per issuer. The exception will be U.S. Treasuries and U.S. Agencies." (Sec. 7.08) **(See Exhibits 12 and 13).**

   b. GASB Standard for Concentration of Credit Risk

   GASB Statement No. 40, Deposit and Investment Risk Disclosures[14], states the following:

   > "Governments should provide information about the concentration of credit risk associated with their investments by disclosing, by amount and issuer, investments in any one issuer that represent 5 percent or more of total investments based on the level of detail prescribed in paragraph 5. Investments issued or explicitly guaranteed by the U.S.

[14] GASB, Statement No. 40 of the Governmental Accounting Standards Board, Deposit and Investment Risk Disclosures, an amendment of GASB Statement No. 3. Available at: https://gasb.org/page/ShowPdf?path=gasbs-40.pdf&title=GASB%20STATEMENT%20NO.%2040,%20DEPOSIT%20AND%20INVESTMENT%20RISK%20DISCLOSURES%E2%80%94AN%20AMENDMENT%20OF%20GASB%20STATEMENT%20NO.%203

> government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement.
>
> Risk disclosures should also be made for governmental and business-type activities, individual major funds, nonmajor funds in the aggregate, or fiduciary fund types when the risk exposures are significantly greater than the deposit and investment risks of the primary government. For example, a primary government's total investments may not be exposed to concentration risk. However, if the government's capital projects fund has all of its investments in one issuer of corporate bonds, disclosure should be made for the capital projects fund's exposure to a concentration of credit risk."

The SDI Fund held six bonds from four issuers which exceeded 5% of their total investments.

c. SDI's Investment in a California ST Bond approximated 8-9% of SDI's Total Investments

The SDI Fund held a $7,550,000 California ST bond (CUSIP 13063DMA3) continuously from February 17, 2021, to May 2024, a period of approximately 40 consecutive months **(See Schedule 17)**. Based on the SDI Fund's total assets for this period including its U.S. Bank custodian account investments, this bond represented between 8.64% and 9.25% of the SDI Fund's total portfolio value throughout the entire holding period, exceeding the 5% threshold identified above for the full approximately 40 months it was held **(See Schedule 17)**.

d. SDI's Investment in a Mississippi Hospital Equipment and Facilities Authority Bond Approximated 10-12% of SDI's Total Investments

The SDI Fund purchased a Mississippi Hospital Equipment and Facilities Authority bond, repaid by Baptist Memorial Health Care Corporation

(CUSIP 605360SE7), in two lots, on January 26, 2023 (5,750,000 units) and January 31, 2023 (4,150,000 units), for a combined total of 9,900,000 units. This bond has been held continuously since January 31, 2023, a period of 42 consecutive months as of the most recent period reviewed. Based on the SDI Fund's total assets for this period including its U.S. Bank custodian account investments this bond has represented between 10.75% and 11.26% of the SDI Fund's total portfolio value throughout, exceeding the 5% threshold identified above for the entire period held to date **(See Schedule 17)**.

i. <u>The Mississippi Hospital Equipment and Facilities Authority Bond Is Also Not Included in the Permitted Investments of the City's Municipal Code or the City's Accounting and Investment Policies</u>

The City's Municipal Code's **(See Exhibit 9)** list of permitted investments includes:

> "(4) Registered state warrants or treasury notes or bonds of the State of California or by a department board, agency or authority of the State.
> (5) Bonds, notes, warrants for other evidences of indebtedness of any local agency within this state." (§3-2.501(a))

The bond was issued by the Mississippi Hospital Equipment and Facilities Authority, a Mississippi entity, and is repaid by Baptist Memorial Health Care Corporation. It was not issued by the State of California or by a local agency within California. The lists of permitted investments in the City's Municipal Code and the City's Accounting and Investment Policies include obligations of the State of California and of local agencies within California, and do not include obligations issued outside California (Sec. 7.08) **(See Exhibits 12 and 13)**.

e. SDI's Investment in a Georgia ST Bond Approximated 6% of SDI's Total Investments

The SDI Fund held a $4,800,000 Georgia ST Go Bds 2011 D bond (CUSIP 373384TP1). As of June 30, 2021, June 30, 2022, and June 30, 2023, this bond represented 6.20%, 5.94%, and 5.73% of the SDI Fund's total portfolio value, respectively, exceeding the 5% threshold identified above on each of these three dates **(See Schedule 17)**.

f. SDI's Investment in State of Mississippi Bonds Approximated 15-17% of SDI's Total Investments

The SDI Fund held three State of Mississippi general obligation bonds simultaneously (CUSIPs 605581EY9, 605581LL9, and 605581NA1). Combined, these bonds represented 17.34%, 16.85%, and 14.78% of the SDI Fund's total portfolio value as of June 30, 2021, June 30, 2022, and June 30, 2023, respectively, exceeding the 5% threshold identified above by more than at least double on each of these three dates **(See Schedule 17)**.

g. The City's Audited Financial Statements Do Not Disclose the SDI Fund's Concentration of Credit Risk

The City's independently audited financial statements for fiscal years 2020-21, 2021-22, and 2022-23 each contain the following statement, identical in each year:

> "Concentration of credit risk is the risk that the failure of any one issuer would place an undue financial burden on the City. The investment policy of the City has stipulations that limit the investment in any one issuer 5% for total investments. However, an exception to this policy has been made for investments in U.S. Treasuries and U.S. Agency Obligations, which have no limits place on the amount that can be invested in one issuer. As of June 30, [2021/2022/2023], the

City did not have any investments in one issuer other than those noted as being exceptions to the policy that exceeded 5% of the City total investments." **(See Exhibit 10).**

The audited financial statements address the City's total investments as a whole, not the SDI Fund specifically. As set forth in subsection (a) above, GASB Statement No. 40 separately requires fund-level disclosure of concentration of credit risk when a fund's risk exposure is significantly greater than that of the primary government as a whole.

Since the SDI Fund did exceed the maximum level of concentration of credit risk, at times over double the 5% maximum, we have found that the City's audited financial statements did not disclose the SDI Fund's concentration of credit risk.

7. Municipal Bonds Issued Outside California, Approximating $73.4 Million, Are Not Permitted by the City's Municipal Code or Accounting and Investment Policies, and At Least $10.6 Million Also Do Not Appear to Be Permitted Under California Government Code

   a. The SDI Fund's Purchases of Municipal Bonds Issued Outside California

   Beginning in December 2020, the same month SSDW commenced as the SDI Fund's broker, the SDI Fund purchased 48 municipal bonds issued outside California at a cost of approximately $73.4 million (See Schedule 4.9). Municipal bonds issued outside California are not included in the permitted investments of the City's Municipal Code or the City's Accounting and Investment Policies. In addition, at least $10.6 million of these bonds do not appear to be of a type permitted under California Government Code §53601, as discussed below. In total, municipal bonds issued outside California represented approximately 51% of the SDI Fund's municipal bond purchases by cost **(See Schedules 4.9 and 4.9.1)**.

E&E reviewed the SDI Fund's custodian statements from July 2013 through August 2025 and found no municipal bond purchases of any kind before December 2020. Before that date, the SDI Fund's bond purchases consisted entirely of U.S. Government Issues **(See Schedule 15.2)**.

Twenty of the municipal bonds issued outside California were also inconsistent with other provisions of the City's Municipal Code and the City's Accounting and Investment Policies. Fifteen had maturities exceeding five years from purchase (Section VIII(5) above), and five exceeded the 5% single-issuer concentration limit (Section VIII(6) above) **(See Schedule 4.8)**.

b. The City's Municipal Code Limits Municipal Bond Investments to California Issuers

The City's Municipal Code **(See Exhibit 9)** list of permitted investments includes the following two categories of municipal obligations:

> "(4) Registered state warrants or treasury notes or bonds of the State of California or by a department board, agency or authority of the State.
>
> (5) Bonds, notes, warrants for other evidences of indebtedness of any local agency within this state." (§3-2.501(a))"

No category on the list includes obligations of any other state, or of cities, counties, school districts, or other local governments located outside California.

The City's Municipal Code further states:

> "In making investments of money in the SDI Fund, the City shall comply with the limitations contained in the Government Code, including Section 53601, and this Chapter. If there is a conflict

between State law and this Chapter, the most conservative investment rule shall prevail if the rule is permitted by State law." (§3-2.502(b))

c. The City's Accounting and Investment Policies Do Not Authorize Obligations Issued Outside California

The list of investments authorized by the City's Accounting and Investment Policies includes State of California obligations and obligations of local agencies within California. It does not include obligations of any other state or of any local agency outside California. The City's Accounting and Investment Policies state:

"If a type of security is not specifically authorized by this policy, it is not a permitted investment." (Sec. 7.08) **(See Exhibits 12 and 13)**.

d. California Government Code §53601 Permits Bonds of Other States, but Not Bonds of Local Agencies Outside California

California Government Code §53601 lists the investments permitted for California local agencies. It addresses municipal bonds in two subdivisions: subdivision (d) covers bonds of other states, and subdivision (e) covers bonds of local agencies.

Subdivision (d) permits investment in bonds issued by any of the other 49 states, and by their departments, boards, agencies, and authorities:

"(d) Registered treasury notes or bonds of any of the other 49 states in addition to California, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency, or authority of any of the other 49 states, in addition to California."

Subdivision (e) permits investment in bonds issued by local agencies, but only local agencies located in California:

> "(e) Bonds, notes, warrants, or other evidences of indebtedness of a local agency within this state"

Section 53600 defines "local agency" to include cities, counties, and school districts:

> "As used in this article, 'local agency' means county, city, city and county, including a chartered city or county, school district, community college district, public district, county board of education, county superintendent of schools, or any public or municipal corporation."

As a result, §53601 permits investment in bonds issued by other states, but not in bonds issued by cities, counties, school districts, or other local agencies located outside California.

By comparison, the City's Municipal Code list of permitted investments includes neither bonds of other states nor bonds of local agencies located outside California (§3-2.501(a)).

e. <u>CDIAC Educational Materials Describe Out-of-State Municipal Bonds as Requiring Additional Due Diligence</u>

Educational materials published by the California Debt and Investment Advisory Commission ("CDIAC") describe municipal bonds issued outside California as requiring additional research and due diligence beyond that required for California issuers. The City's Municipal Code provides that "the most conservative investment rule shall prevail" (§3-2.502(b)).

On June 24, 2015, CDIAC presented an educational webinar titled "The Public Investment Portfolio: When It Makes Sense to Buy Municipals." The webinar's stated topics included the "Interpretation of Government

Code sections 53601 (a), and 53601(c) (d) (e) and what local governments can and cannot do with regard to investing in munis" (Agenda, p. 1) **(See Exhibit 15)**. The presenters were the Chief Investment Officer of the City of Sacramento and the President of an investment firm serving California public agencies.

Regarding municipal bonds issued by other states, one presenter stated the following:

> "But it is a little bit different because you are not in that state, so there are a lot of things that can be going on out of the State of California that you are not aware of. So when you start looking at other states, we feel that your due diligence is paramount in looking at those arenas." (Transcript, p. 12) **(See Exhibit 15)**

The City of Sacramento's Chief Investment Officer stated the following:

> "Unlike bond issues from the State of California where the policies and economics are known, bonds from other states require additional research and investigation [in] getting to understand the state's particular GO requirements and budget and pension statuses" (Transcript, p. 12) **(See Exhibit 15)**

> "We tend to shy away from buying things outside of the state because it does take that extra effort and it does take that extra bit of due diligence. And there is really an unknown factor. And as we know in the investment world, lack of knowledge means inherited risk." (Transcript, p. 14) **(See Exhibit 15)**

CDIAC notes that the webinar content "is informational and does not constitute investment advice or the recommendation to invest in any or all of the investment instruments discussed." (Transcript, p. 1) **(See Exhibit 15)**

f. Seventeen Municipal Bonds Issued Outside California Also Do Not Appear to Be Permitted Under California Government Code §53601

Seventeen of the 48 municipal bonds issued outside California, purchased at a cost of approximately $10.6 million, do not appear to be permitted under California Government Code §53601. As described above, §53601 permits bonds issued by other states, but not bonds issued by local agencies outside California. These 17 bonds were issued by cities, counties, school districts, and other local public entities outside California. E&E identified the issuer and obligor of each bond using the Municipal Securities Rulemaking Board's Electronic Municipal Market Access ("EMMA") system **(See Schedule 4.9)**.

The remaining 31 bonds were issued by other states, by state-level agencies and authorities, or by the District of Columbia. Of these, 23 were issued by other states or by state-level agencies and authorities, the type of issuer §53601(d) permits. For the other 8, purchased at a cost of approximately $16.4 million, E&E could not determine with certainty whether they are permitted under §53601. Each was issued on behalf of a private or nonprofit organization, including hospitals, universities, and a public radio network, which is responsible for repaying it **(See Schedule 4.9)**:

- 6 were issued by state-level financing authorities
- 2 were issued by the District of Columbia

During CDIAC's webinar, the City of Sacramento's Chief Investment Officer described his city's experience with bonds issued by local agencies outside California:

> "Well, unfortunately, you can't own local agency money out of State of California, which we found out the hard way about nine months ago because we were buying New York state airport bonds, which we

> loved, and then our auditor came back and said, ahem, you can't own out of state local agency bonds." (Transcript, p. 25) **(See Exhibit 15)**

CDIAC's Education Manager, who moderated the webinar, responded:

> "Right. Not permitted in code." (Transcript, p. 25) **(See Exhibit 15)**

In summary, at least $10.6 million of municipal bonds issued outside California were not only excluded from the permitted investments of the City's Municipal Code and the City's Accounting and Investment Policies, but also do not appear to be permitted under California Government Code §53601. E&E could not determine with certainty whether an additional approximately $16.4 million of these bonds are permitted under §53601.

8. <u>The SDI Fund's Money Market Fund Holdings Exceeded the 20% Limit in California Government Code and the City's Accounting and Investment Policies Prior to SSDW's Engagement</u>

> Before SSDW's engagement, the SDI Fund held a substantial portion of its investments in a money market fund, First American Government Obligation Fund (CUSIP 31846V203). As discussed in Section VIII (9) below, cash generated by the SDI Fund's investments was automatically placed in this fund.

California Government Code §53601(l) permits investment in money market funds, but provides that such purchases "shall not exceed 20 percent of the agency's moneys that may be invested pursuant to this section" (§53601(l)(5)). The City's Accounting and Investment Policies set the same 20% limit (Sec. 7.08) **(See Exhibits 12 and 13)**.

E&E identified 34 months in which the SDI Fund's holdings in the First American Government Obligation Fund exceeded 20% of the SDI Fund's investments, all before SSDW's engagement in December 2020 **(See Schedule 2.4)**. The holdings reached 81.0% in February 2016 and 80.4% in June 2016, approximately $68.3 million and $68.4 million, respectively, and were 46.1%, approximately $41.1 million, in November 2020, the month before SSDW's engagement **(See Schedules 2.4 and 2.5)**. The holdings did not exceed 20% at any point after SSDW's engagement **(See Schedule 2.4)**.

The City's Municipal Code also provides that no investment shall be purchased "[w]hich are shares of beneficial interest issued by diversified management companies as described in Government Code Section 53601(l)" (§3-2.501(b)(4)) **(See Exhibit 9)**. Section 53601(l) includes money market funds registered with the Securities and Exchange Commission. E&E did not determine whether the SDI Fund's shares in the First American Government Obligation Fund fall within this provision. If they do, the Municipal Code may prohibit the SDI Fund's money market fund holdings entirely, not only those exceeding 20%.

9. <u>SDI's Idle Cash Was Automatically Held in a Money Market Fund Rather Than LAIF</u>

The City's Municipal Code **(See Exhibit 9)** states:

> "When the investments mature or when other monies are available for investment, the monies may be invested in the Local Agency Investment Fund ('LAIF') pending more permanent investment." (§3-2.502(d)).

In practice, whenever an investment matured, paid interest, or otherwise generated cash, that cash was automatically used to purchase additional shares of a money market fund, First American Government Obligation Fund (CUSIP 31846V203), rather than being placed in LAIF. This occurred automatically, generally on the same day the cash became available,

functioning as the account's default destination for idle cash in place of the LAIF placement contemplated by §3-2.502(d).

For example, on January 30, 2019, a $5,750,000 U.S. government agency note matured, generating $5,750,000 in principal and $27,312.50 in final interest, for a combined $5,777,312.50. That same day, per the custodian statement, the full amount was used to purchase additional shares of the money market fund. This pattern repeats throughout the custodian statements reviewed for the entire period: cash generated by interest payments and bond maturities alike was placed into the money market fund automatically.

E&E compared the SDI Fund's actual historical portfolio value to a modeled scenario holding every other variable constant, including the trading activity exactly as it occurred, and changing only the destination of idle cash from the money market fund to LAIF, for the period July 1, 2013 through the most recent period reviewed. Had idle cash been placed in LAIF instead of the money market fund, the SDI Fund's portfolio would have reached a value of $91,633,641.47 by fiscal year-end 2024-25, compared to its actual value of $90,747,955.41, a difference of $885,686.06 **(See Schedule 8)**.

10. Historical Performance of SDI Investments vs. Benchmark Indices

E&E compared the SDI Fund's performance for each fixed-income asset class held to a benchmark index selected for comparability, for each fiscal year the asset class was held:

- U.S. Government Issues → Bloomberg US Government/Credit AA or Higher Index
- Corporate Issues → Bloomberg US Corporate 1-5 A or Higher Index
- Municipal Issues → S&P Municipal Bond Index.

These comparisons are a general indication only, as each index is a broad market measure that does not exactly match the SDI Fund's holdings.

a. U.S. Government Issues

The SDI Fund held U.S. Government Issues from fiscal year 2013-14 through fiscal year 2019-20. Over this period, the SDI Fund's U.S. Government Issues underperformed the Bloomberg US Government/Credit AA or Higher Index in five of six fiscal years, by an average of 2.83% per fiscal year **(See Schedule 6)**.

b. Corporate Issues

The SDI Fund held Corporate Issues from fiscal year 2020-21 through fiscal year 2024-25. Over this period, the SDI Fund's Corporate Issues underperformed the Bloomberg US Corporate 1-5 A or Higher Index in three of four fiscal years. Across all four fiscal years, the SDI Fund's Corporate Issues underperformed the index by an average of 4.92% per fiscal year **(See Schedule 6)**. As discussed above, Corporate Issues are not a permitted investment under the City's Municipal Code.

c. Municipal Issues

The SDI Fund held Municipal Issues from fiscal year 2021-22 through fiscal year 2024-25. Over this period, the SDI Fund's Municipal Issues outperformed the S&P Municipal Bond Index in all four fiscal years, by an average of 5.66% per fiscal year **(See Schedule 6)**.

11. Ratio Analysis and the Excessive-Trading Standard

Department of Enforcement v. Howard, 2000 NASD Discip. LEXIS 16 (NAC, Nov. 16, 2000), a National Adjudicatory Council decision, states that annualized turnover ratios between 3 and 4 have triggered liability for

excessive trading, and that there is little question of excessiveness when a turnover ratio exceeds 6. The same decision states that cost-to-equity ratios between 15% and 30%, or more, have been found excessive.

The annual turnover ratio measures the level of trading activity in an account and is calculated by dividing total purchases by the average account equity for the year. A higher turnover ratio indicates a greater level of trading activity while a lower turnover ratio indicates a lower level of trading activity.

The annual cost-to-equity ratio measures the cost of trading relative to the account's average equity and is calculated by dividing annual trading costs by average account equity. A higher cost-to-equity ratio indicates that a greater return is required for the account to recover its trading costs.

E&E attempted to calculate the SDI Fund's annual turnover ratio and annual cost-to-equity ratio for each year of the period reviewed, using the SDI Fund's total purchases, costs, and average account equity for each full calendar year.

As described in Section IX below, E&E was able to conduct independent online research to obtain information from Electronic Municipal Market Access ("EMMA") a publicly available source that discloses transactions of Municipal Securities. Using this database E&E was able to identify indications of markups charged by the City's brokers in certain transactions. However, E&E was unable to verify or confirm the commission and markup data for any transactions in the account, despite several requests for such information (See Report Sections V and X). Accordingly, E&E was unable to calculate the annual cost to equity ratio.

The highest annual turnover ratio identified was 2.16 in 2016 with the remaining years less than 1 **(See Schedule 9)**. While the turnover ratios were less than the excessive trading requirements, it should be considered that the primary goal of the SDI Fund is to safeguard principal.

12. The Cost to the SDI Fund of SSDW's Change in Investment Composition

To assess the impact of SSDW's change in the SDI Fund's investment composition, E&E prepared a scenario modeling what the SDI Fund's portfolio value would have been had SSDW not commenced as the SDI Fund's broker in December 2020. These scenarios are presented to measure the financial effect of the SDI Fund's actual investments; they do not represent investment advice or E&E's recommendation of how the SDI Fund should have been invested. E&E also prepared two additional scenarios, modeling the SDI Fund's portfolio value. Each scenario holds a different set of assumptions constant regarding the vehicle used for the SDI Fund's idle cash and the period over which the scenario is modeled.

a. In the first scenario, beginning in December 2020, the SDI Fund's matured investments and idle cash are assumed to be invested in the money market fund historically used by the SDI Fund for its uninvested cash. In this scenario, the SDI's investments would be placed in this money market account and none of the investment decisions of SSDW would have occurred. Under this scenario, the SDI Fund's portfolio would have reached a value of $101,298,075 by fiscal year-end 2024-25, compared to its actual value of $90,747,955, a difference of $10,550,119 **(See Schedule 8)**. Extended through August 31, 2025, the most recent period analyzed, the difference under this scenario is $10,296,155 **(See Schedule 8)**.

b. In the second scenario, beginning in July 2013, the SDI Fund's matured investments and idle cash would be invested in LAIF as opposed to the money market funds that SDI historically placed its uninvested funds. In this scenario, the SDI's investments would be placed in LAIF and none of the investment decisions of SSDW would have occurred. Under this scenario, the SDI Fund's portfolio would have reached a value of $101,027,653 by fiscal year-end 2024-25,

compared to its actual value of $90,747,955, a difference of $10,279,698 **(See Schedule 8)**.

c. In the last scenario, beginning fiscal year 2017, SDI Fund's matured investments and idle cash would be invested in LAIF as opposed to the money market funds that SDI historically placed its uninvested funds. In this scenario, the SDI's investments would be placed in LAIF and none of the investment decisions of SSDW would have occurred. Under this scenario, the SDI Fund's portfolio would have reached a value of $99,625,019 by fiscal year-end 2024-25, compared to its actual value of $90,747,955, a difference of $8,877,064 **(See Schedule 8)**.

Across all three scenarios, the SDI Fund's portfolio value would have been materially greater by amounts ranging from $8,877,064 to $10,550,119, had SSDW never been engaged as the SDI Fund's broker in December 2020, and the investments instead been placed in the money market fund or LAIF.

13. <u>The City's Records Do Not Reflect the Treasurer or Finance Director Approving the SDI Fund's Bond Trades</u>

E&E reviewed the SDI Fund's records of 239 bond transactions between December 2020 and August 2024 **(See Schedule 15.3)**. For all 239 trade tickets reviewed, the accompanying email communications do not show the City Treasurer or the Finance Director approving the trade. Kenny Cooper is listed as the trader on 238 of the 239 transactions, or 99.6%. During the period reviewed, Mr. Cooper held the position of City Accountant and later City Finance Manager; he did not hold the position of Treasurer or Finance Director at any point. Under Ordinance No. 98-552, Section 9-6.202(c), "The City Treasurer and Finance Director shall select the proper mix of investments" for the SDI Fund.

IX. Broker Engagement, Disciplinary Actions, Compensation, and Documentation

1. Timeline of Broker Relationships

From at least January 2013 through October 2016, brokerage services for the SDI Fund's investments were provided through Stifel. Ronald C. Gross was registered with Stifel during this period and based on our understanding, was a broker assigned to the SDI Fund. The last identified transaction on the account during this period is dated October 17, 2016, the same date FINRA records reflect the end of Mr. Gross' registration with Stifel.

From October 2016 through December 2020, no brokerage activity occurred on the SDI Fund's investment account. Beginning in December 2020, SSDW commenced as the broker for the SDI Fund. Per a letter dated December 16, 2020 from Kenny Cooper, U.S. Bank was authorized, as custodian, to receive investment instructions from three individuals at SSDW: Ron Gross, Jennifer Jennings, and Carey Paret **(See Exhibit 11)**. Per FINRA BrokerCheck records, Mr. Gross's registration with SSDW ended in July 2025; whether SSDW has continued to serve as the SDI Fund's broker as of the date of this report has not been confirmed.

2. Requirements for Investment Intermediaries Under the City's Municipal Code Were Not Provided and May Not Have Been Followed

The City's Municipal Code states:

> "If a permitted investment can be obtained only through a broker-dealer, underwriter or other intermediary, the Treasurer may make the investment through the intermediary, provided the City Council approves a written agreement with the intermediary covering the transaction." (§3-2.507(a)) **(See Exhibit 9)**.

The Municipal Code further states:

- "Intermediaries must be pre-qualified as described in this section for the City to judge the integrity and competence of such persons and to familiarize such persons with the investment policies of the City." (§3-2.507(b)) **(See Exhibit 9)**.

  Any intermediary seeking to conduct transactions with the City must file a written application for pre-qualification with the Finance Director, containing the intermediary's name, account representative, assets, proposed depository of securities, last quarterly financial statement, and amount of insurance coverage for each account. If the Finance Director determines the application accurate, the applicant must present to the City Manager to be interrogated on qualifications and investment philosophy, after which a Memorandum of Understanding, acknowledging the intermediary's understanding of the scope and content of the City's Municipal Code, must be presented to Council for approval.

- "When it is advantageous to the City to use the services of an intermediary, the Treasurer shall solicit proposals from all intermediaries who have entered into Memoranda of Understanding with the City. The Treasurer shall then deal with the intermediary which has made the most favorable proposal." (§3-2.507(e)) **(See Exhibit 9)**.

The City's Accounting and Investment Policies contain additional, related requirements as follows:

- "All brokers and dealers that desire to become qualified bidders for investment transactions with the City must respond to a "Broker Dealer Questionnaire" and submit related documents relative to

eligibility. This includes a current audited financial statement, proof of state registration, proof of NASD registration and a certification they have received and reviewed the City's Investment Policy and agree to comply with the provisions outlined in the Investment Policy." (Sec. 7.07.02) **(See Exhibits 12 and 13)**.

- It will be the responsibility of the personnel involved in each transaction to produce and retain written records, including the name of the financial institutions solicited, price/rate quoted, general description of the security, bid/offer selected, and any consideration that had an impact on the decision.' (Sec. 7.09) **(See Exhibits 12 and 13)**.

- "The City shall send annually, or as updated, a copy of its current Investment Policy to all financial institutions and broker/dealers approved to do business with the City. Receipt of the Investment Policy including confirmation that it has been received and reviewed by the person(s) handling the City's account, shall be acknowledged in writing within thirty (30) days." (Sec. 7.07) **(See Exhibits 12 and 13)**.

In response to E&E's document requests to the City, it stated outright that hiring and retention documents, including applications for pre-qualification and memoranda of understanding, do not exist for bond traders and investment managers, including Ron Gross and SSDW. The City similarly stated that portfolio management agreements and other written instruments governing the City's brokerage relationships do not exist. The City did not respond to E&E's separate request for City Manager's Office correspondence concerning the SDI Fund.

Based on the City's responses that hiring and retention documents, such as applications for pre-qualification and memoranda of understanding, do not

exist, there is a risk that the City's Municipal Code requirements for investment intermediaries may not have been followed.

3. Absence of Documentation in Response to Document Requests

Across E&E's three document requests to the City, 26 items addressed SDI Fund bond traders, investment managers, and account signers, and the SDI Fund's brokerage relationships with SSDW and Stifel specifically. Of these 26 items, 100% were either not responded to at all or the city stated that the requested records "do not exist." (17 were answered with a statement that the requested records "do not exist," and nine received no response at all):

Req. #	Req. Section	Item Requested (Verbatim)	Response Category
61	VI	List of all bond traders and investment managers of the SDI Fund by year during the years 7/1/2014 – Current.	Per Response Does Not Exist
63	VI	Hiring, retention documents, or formalization of any relationship including applications for pre-qualification, memorandums of understanding, offer letters, contracts, job descriptions, resumes/application materials and employment agreements of all bond traders and investment managers, whether formally signed or informally communicated, including but not limited to Ron Gross, SouthState|DuncanWilliams, and Stifel, Nicolaus & Co., Inc.	Per Response Does Not Exist
64	VI	Any terminations of agreements and contracts or correspondence related to any relationship between the City, the SDI Fund, or any investment service providers for bond trading, investment management, or other financial services, including but not limited to Ron Gross, Stifel, Nicolaus & Co., Inc., and SouthState|DuncanWilliams.	Per Response Does Not Exist
65	VI	Any and all documents or correspondence related to broker and investment manager performance, including but not limited to emails, City Council Meeting minutes, and other forms of communication for the years 7/1/2014 – Current.	Per Response Does Not Exist
66	VI	Disciplinary actions, disciplinary memos, and HR complaints of all bond traders, finance managers, and investment managers for the years 7/1/2014 – Current.	No Response and No Documents Received
68	VI	Compensation records for all bond traders and investment managers including salaries, commissions, W-2's, 1099s, bonuses, incentives, payroll records, perks, and benefits for the years 7/1/2014 – Current.	Per Response Does Not Exist
69	VI	Commission criteria for all bond traders and investment managers including policies, performance-based payout reports, commissions, incentives, perks, and benefits for the years 7/1/2014 – Current.	Per Response Does Not Exist
70a	VI	Communications including emails, internal memos, and board meeting minutes involving licensing, hiring, bonuses, performance reviews, personnel changes, and red flags including but not limited to communication with traders during the fiscal years ended 6/30/2014 - Current.	No Response and No Documents Received
70b	VI	Communications including emails, internal memos, and board meeting minutes involving licensing, hiring, bonuses, performance reviews, personnel changes, and red flags including but not limited to communication with Finance Director / Treasurer during the fiscal years ended 6/30/2014 - Current.	No Response and No Documents Received
70c	VI	Communications including emails, internal memos, and board meeting minutes involving licensing, hiring, bonuses, performance reviews, personnel changes, and red flags including but not limited to communication with City manager / oversight officials during the fiscal years ended 6/30/2014 - Current.	No Response and No Documents Received

70d	VI	Communications including emails, internal memos, and board meeting minutes involving licensing, hiring, bonuses, performance reviews, personnel changes, and red flags including but not limited to communication with Fund custodians or brokers during the fiscal years ended 6/30/2014 - Current.	No Response and No Documents Received
70e	VI	Communications including emails, internal memos, and board meeting minutes involving licensing, hiring, bonuses, performance reviews, personnel changes, and red flags including but not limited to communication with City attorneys during the fiscal years ended 6/30/2014 - Current.	No Response and No Documents Received
71	VI	Broker/custodian agreements and KYC records.	No Response and No Documents Received
72	VI	Communications, agreements, invoices, and any other documents with outside investment consultants or advisors during or in effect during the fiscal year ending 6/30/2014 - Current.	No Response and No Documents Received
74	VI	Any subpoenas, legal notices, or settlements related to the SDI Fund.	No Response and No Documents Received
75	VI	Access logs from trading platforms used by the traders, even if the access logs are maintained by the City's investment service providers.	Per Response Does Not Exist
113	XIII (SSDW)	S&P Reports generated by SouthState|DuncanWilliams for the years 7/1/2014 – Current.	Per Response Does Not Exist
115	XIII (SSDW)	All Investment Reports prepared by SouthState|DuncanWilliams, Ron Gross, Carey Paret, and Jennifer Jennings for the years 7/1/2014 – Current.	Per Response Does Not Exist
116	XIII (SSDW)	All account statements prepared and maintained by SouthState|DuncanWilliams for the years 7/1/2014 - Current, whether transmitted directly the City or accessible online.	Per Response Does Not Exist
118	XIII (SSDW)	Any and all contracts, agreements, and correspondence relating to investment services, advice, and planning between the City, the SDI Fund, SouthState|DuncanWilliams, Ron Gross, Carey Paret, and Jennifer Jennings for the years 7/1/2014 – Current.	Per Response Does Not Exist
119	XIII (SSDW)	Any and all records sufficient to identify, document, and support all compensation, fees, commissions, markups, spreads, per-share increases, or other remuneration paid to or retained by SouthState|DuncanWilliams, Ron Gross, Carey Paret, and Jennifer Jennings in connection with any investment advisory, brokerage, trading, or custodial services performed for the City, for the period 7/1/2014 through the present, regardless of the City fund, account, department, or payment source involved.	Per Response Does Not Exist
120	XIV (Stifel)	Any reports provided by Stifel, Nicolaus & Co., Inc. including public company ranking, investment quality, ratio analyses, valuation, and other information provided to or made accessible to the City in order to make investment decisions for the years 7/1/2014 - 12/31/2020.	Per Response Does Not Exist
122	XIV (Stifel)	All Investment Reports prepared by Stifel, Nicolaus & Co., Inc. and Ron Gross for the years 7/1/2014 – Current.	Per Response Does Not Exist
123	XIV (Stifel)	All monthly, quarterly, and annual account statements prepared and maintained by Stifel, Nicolaus & Co., Inc. for the years 7/1/2014 - Current.	Per Response Does Not Exist
125	XIV (Stifel)	Any and all contracts, agreements, and correspondence relating to investment services, advice, and planning between the City, the SDI Fund, Stifel, Nicolaus & Co., Inc., and Ron Gross for the years 7/1/2014 – Current.	Per Response Does Not Exist
126	XIV (Stifel)	Any and all records sufficient to identify, document, and support all compensation, fees, commissions, markups, spreads, per-share increases, or other remuneration paid to or retained by Stifel, Nicolaus & Co., Inc. or Ron Gross in connection with any investment advisory, brokerage, trading, or custodial services performed for the City, for the period 7/1/2014 through the present, regardless of the City fund, account, department, or payment source involved.	Per Response Does Not Exist

GFOA's Government Relationships with Securities Dealers best practice[15], approved by the GFOA Executive Board on October 31, 2012, states the following:

- "Regardless of the method of communicating with a broker, a government investor needs to perform due diligence on all securities dealers prior to adding them to their list of approved brokers/dealers for transacting trades."

- "Use a defined internal process to select, qualify, renew, or terminate brokers and dealers: Use a questionnaire, conduct an interview, and/or conduct peer references to help determine that the broker understands the public entity's needs/objectives."

- "Require that brokers provide written acknowledgement or certification of their review and understanding of the government entity's investment policy to assure compliance with its objectives, portfolio risk constraints, and investment trading requirements."

4. Ronald C. Gross's Disciplinary History

Per FINRA BrokerCheck records[16], Mr. Gross was the subject of a customer dispute filed in 1995 and resolved in 1997 (NASD Arbitration No. 96-01304), alleging churning, unsuitable recommendations, failure to supervise, and breach of fiduciary duty. The customer sought $450,000 in damages. The dispute was settled for $206,000, paid by Mr. Gross's then-employing firms (Smith Barney and Prudential, $103,000 each). Mr. Gross's BrokerCheck record reflects that he denied the allegations.

[15] Government Finance Officers Association, Government Relationships with Securities Dealers (best practice, approved October 31, 2012). Available at: https://www.gfoa.org/materials/government-relationships-with-securities-dealers
[16] FINRA. BrokerCheck Report, Ronald Clifford Gross. Available at: https://files.brokercheck.finra.org/individual/individual_1078889.pdf

FINRA BrokerCheck records also reflect that Mr. Gross was separately the subject of an NASD regulatory action (NASD Case No. C3B970010), initiated in 1997 and resolved in 1998 by consent, finding violations of NASD Rules 2110 and 2310 relating to unsuitable trading recommendations. The action resulted in a 120-day suspension from association with any NASD member firm and a requirement that Mr. Gross pass a requalification examination, which he passed on November 5, 1998. No monetary penalty was imposed.

In addition, FINRA BrokerCheck records reflect that Mr. Gross has disclosed three outstanding federal tax liens: $744,454.00, filed February 18, 2015; $55,816.71, filed October 29, 2015; and $39,997.00, filed March 29, 2017, totaling $840,267.71. These liens were outstanding, per Mr. Gross's own disclosures, during the period he served as the SDI Fund's registered representative.

GFOA's Government Relationships with Securities Dealers best practice recommends:

"Record and retain pertinent information on the firm and the individual broker including an annual review of the Central Registration Depository (CRD®) information for both maintained by the Financial Industry Regulation Authority (FINRA). Violations or sanctions imposed by a regulatory agency or government should be carefully reviewed for termination of relationship."

5. Broker Compensation and Commissions

E&E requested records sufficient to identify, document, and support all compensation, fees, commissions, markups, spreads, per-share increases, or other remuneration paid to or retained by SSDW, Ron Gross, Carey Paret, Jennifer Jennings, and Stifel, in connection with any investment advisory, brokerage, trading, or custodial services performed for the City. As described in Section IX(3) above, the City stated that no records responsive to these

requests exist. E&E separately requested compensation records and commission criteria for all bond traders and investment managers generally, which the City similarly stated do not exist.

In the absence of complete records from the City, E&E conducted independent online research using Electronic Municipal Market Access ("EMMA"), a publicly available source disclosing transactions of municipal securities, administered by the Municipal Securities Rulemaking Board. For certain SDI Fund municipal bond transactions, E&E identified multiple transactions recorded in EMMA on the same trade date, for the same CUSIP, and for the same trade amount, occurring within minutes of one another but reported at different prices **(See Schedule 10)**. E&E used the difference between these prices as an indication of markups charged in connection with the SDI Fund's transactions.

E&E identified the commissions earned by SSDW on the SDI Fund's bond transactions that could be traced through the Electronic Municipal Market Access (EMMA) database, by comparing the price the SDI Fund paid or received on each transaction to the price of the corresponding inter-dealer trade reported on EMMA for the same security. Using the first inter-dealer trade identified for each security as the point of comparison, E&E identified total commissions of $2,379,078 for the period December 2020 through September 2024 **(See Schedule 13.6)**. Using the second inter-dealer trade identified for each security as the point of comparison, E&E identified total commissions of $2,346,764 for the same period **(See Schedule 13.5).**

For example, on September 23, 2022, the SDI Fund purchased a trade amount of $3,900,000 of CUSIP 55178CAG8 (Lynwood Housing Authority Taxable Revenue Bonds, Series 2018, 4%) **(See Schedule 10)**. EMMA records show two inter-dealer trades in the same CUSIP and trade amount at 8:56 AM, at prices of 93.065 and 93.125, indicated as trades between brokers. Seventeen minutes later, at 9:13 AM, EMMA records show a "customer bought" transaction for the same CUSIP and trade amount at a price of 95.625,

reflecting the SDI Fund's purchase. The difference between this price and the higher of the two inter-dealer prices is 2.50 points, or $97,500 on this transaction.

Of the 218 municipal bond transactions for which E&E identified matching EMMA records **(See Schedules 10, 11.1)**, 184 were also cross-verified against trade tickets the City provided, confirming an exact match on trade amount, trade date, and settlement date across the trade ticket, EMMA, and brokerage statement records **(See Schedule 15)**. The City did not provide trade tickets for all transactions in the account.

Of 218 municipal bond purchase and sale transactions for which E&E identified matching EMMA records, E&E was only able to calculate trading costs for 192 transactions.

Of SDI's 522 total bond purchase and sale transactions, E&E was only able to obtain commission information for 192 transactions or approximately 37%. No commission information could be identified for the remaining 330 transactions **(See Schedule 11)**.

Without additional information, E&E was unable to confirm with absolute certainty the commissions or markups of SDI's brokers for any transaction in the account with the documents available.

X. The City Continues to Report a $20,684,224 Allowance Against Two RDA Loans Without Producing Evidence Supporting the Basis for That Determination

1. Background: The Two RDA Promissory Notes Funded by the SDI Fund

The City loaned SDI Fund money to its own Redevelopment Agency ("RDA") in 1990 and 1993, in an amount approximating $10 million, under two promissory notes **(See Exhibit 14)**.

a. A note dated March 14, 1990, later superseded by an amended note dated September 27, 1993, in the amount of $4,500,000, to acquire land for housing development.

   i. This note names only the City as payee. The SDI Fund is not mentioned in it as follows: "The city of California City Redevelopment Agency (Agency) promises to pay the city of California City (City) the sum of four million five hundred thousand dollars ($4,500,000.00)..."

   ii. Interest was set as follows: "The unpaid balance shall bear interest at the rate of 12% per annum from March 14, 1990, to January 26, 1993. From January 27, 1993, the unpaid balance shall bear interest at the rate of 6.6% per annum."

b. A note dated July 1, 1993, in the amount of $5,902,000, to fund improvements to the City's wastewater treatment plant.

   i. This note names the SDI Fund directly as payee: "the City of California City Redevelopment Agency (Agency) promises to pay the City of California City Sub-Division Deferred Improvement Fund (SDI Fund) the sum of...$5,902,000.00..."

   ii. Interest was set as follows: "The unpaid principal balance shall bear interest at the rate of seven and three tenths' percent (7.3%) per annum."

The City's Municipal Code prohibits investment in notes issued by the Redevelopment Agency, with one exception. Section 9-6.202(a) of Ordinance No. 98-552 states: "The money shall not be invested in notes issued by the City or the Redevelopment Agency of the City of California City except in connection with a project contemplated by the SDI Agreements."

2. Recording of the Two Loans on the City's Audited Financial Statements

For the fiscal year ended June 30, 2013, the SDI Fund's balance sheet recorded the two loans as a single combined receivable, "Successor Agency Receivable," in the amount of $20,684,224. This amount was recorded as an asset, with no offsetting allowance.

For the fiscal years ended June 30, 2014 and June 30, 2015, the balance sheet added a new offsetting entry, "Allowance - Successor Agency receivable," in the same amount, $20,684,224, reducing the net receivable to $0 **(See Schedule 16)**. The notes to the financial statements for these two years did not explain the addition of this allowance and they continued to describe only the loan terms and outstanding balances.

For the fiscal year ended June 30, 2016, the notes to the financial statements explained the allowance for the first time:

> "The Department of Finance has disallowed payments for these loans and an allowance for uncollectible debt has been established in the Subdivision Deferred Improvements fund for the entire balance. Additionally, as a result of the DOF's determination, the City stopped accruing interest on the debt. However, the City is still attempting to obtain authorization from the Department of Finance allowing repayment by the Successor Agency to the City. Accordingly, the City has not removed the loans and related accumulated interest from the Successor Agency's balance sheet."

For fiscal years 2016 through 2024, the financial statements have reported the same amounts each year: principal of $9,877,142 and accrued interest of $10,807,082, totaling $20,684,224, fully offset by a 100% allowance. The explanatory language quoted above has continued, substantially unchanged, through the most recent fiscal year 2024 financial statements.

3. The City's 2018 Resolutions

On May 8, 2018, the City Council adopted Resolution No. 05-18-2740, approving new loan agreements for the two notes. The Successor Agency approved the same loan agreements that same day, and the Oversight Board approved them the following day, May 9, 2018. The recitals to the City Council resolution state the purpose as follows:

> "The parties desire to enter into this Agreement in [order] to ratify the existence and validity of the RDA Promissory Notes, and to authorize the repayment to the City of remaining amount owed to the City."

The 2018 loan agreements recalculated both notes at a 3% simple interest rate.

For the $5,902,000 treatment plant note, the 2018 agreement stated:

- "It is the understanding and agreement of the parties that the total outstanding amount of the loan owed to the City under the RDA Promissory Note dated September 27,1993, as of June 30, 2018 was approximately $12,580,203.73, and no payments have been made to reduce the original principal amount of $5,902,000."

- "Section 5 of the RDA Promissory Note is amended to read, the unpaid principal balance of the loan shall bear interest at the rate of 3% per annum as allowed by Health and Safety Code section 34191.4."

For the $4,500,000 land note, the 2018 agreement stated:

- "It is the understanding and agreement of the parties that the total outstanding amount of the loan owed to the City under the RDA Promissory Note dated September 27,1993, as of June 30, 2018 was

approximately $8,734,822.77 and no payments have been made to reduce the original principal amount of $4,500,000."

- "Section 2 of the RDA Promissory Note is amended to read, 'The unpaid principal balance of the loan shall bear interest at the rate of 3% per annum as allowed by Health and Safety Code section 34191.4.'"

Despite these 2018 resolutions, the balances reported on the City's audited financial statements have not been updated to reflect the recalculated amounts. As discussed above, the financial statements have continued to report the pre-2018 principal and interest figures ($9,877,142 and $10,807,082, respectively) every year through fiscal year 2024.

4. The City Has Not Produced Evidence Supporting the Basis for the Allowance

Across three rounds of document requests, E&E specifically asked the City to produce the records that would show the basis for treating these two loans as uncollectible: the loan agreements and supporting documentation, interest calculation schedules, payment history, correspondence with the City's auditors regarding these loans, and the source documents and calculations underlying the specific financial statement accounts for this receivable and allowance.

Req. #	Section	Item Requested (Verbatim)	Response Category
VII	77	Identification and list of all loans active, outstanding, or in effect at any time during the period 7/1/2009 – Current, from the SDI Fund to the City.	No Response and No Documents Received
VII	78	Identification of all loans to or from the SDI Fund and any third-party including advances to RDA for the years 7/1/2009 – Current.	No Response and No Documents Received
VII	79	Supporting documentation for all loans active, outstanding, or in effect at any time during the period 7/1/2009 – Current, between SDI Fund and the City, including but not limited to loan agreements, promissory notes, escrow statements, board meeting minutes, legal documents, court rulings, correspondence, internal reports, internal calculations, and any other supporting documentation.	No Response and No Documents Received
VII	80	Supporting documentation for all loans active, outstanding, or in effect at any time during the period 7/1/2009 – Current, between SDI Fund and any other third party including advances to RDA, including but not limited to loan agreements, promissory notes, escrow statements, board meeting minutes, legal documents, court rulings, correspondence, internal reports, internal calculations, and any other supporting documentation.	No Response and No Documents Received

VII	81	Supporting documentation reflecting the existence and use of SDI loans held by the City including but not limited to bank records, investment statements, invoices, receipts, financial reports, and expenditure breakdowns.	No Response and No Documents Received
VII	82	City auditor reports, findings, and correspondence by Bryant L. Jolley, Price Paige & Company, and Moss Levy Hartman LLP related to SDI Fund loans for the years 7/1/2009 – Current.	Partially Available Online
VII	83	Payment history, including but not limited to amortization schedules and receipts for loan repayments or settlements.	No Response and No Documents Received
VII	84	Interest calculation schedules, accounting journals, or policies related to interest accrual for SDI Fund accounts for the years 7/1/2009 – Current.	No Response and No Documents Received
VII	85	Any and all documents relating to the sale of "the 317" properties by the City, the RDA, or successor agency for the years 7/1/2009 – Current.	No Response and No Documents Received
I	22	All source documents provided to the City's auditors including Bryant L. Jolley, Price Paige & Company, and Moss Levy Hartman LLP for the fiscal years 2010 – 2025. Please produce all "Prepared By Client" (PBC) request lists and the City's responses thereto for fiscal years 2010–2025. Please provide explanations of (1) the method by which audit documentation was transmitted (email, portal, physical delivery), (2) which City department(s) is responsible for responding to audit requests, and provide a point of contact's e-mail and phone number within that department(s), (3) whether such records are maintained by the auditors instead of the City.	Per Response Does Not Exist
III	33	Identification and list of all transactions including loans or promissory notes between the SDI Fund, the City, and/or the Redevelopment Agency (Successor Agency) for the years 1/1/1990 - Current, including but not limited to loans to the Redevelopment Agency (Successor Agency) on 3/14/1990 for $4.5 million and 7/1/1993 for $5.9 million, in addition to any other loans or transactions. All records sufficient to identify and document all transactions, transfers, advances, borrowings, or loans between the SDI Fund and any other City fund, account, department, or City-controlled entity for the period 1/1/1990 through the present.	Per Response Does Not Exist
XV1	136	Supporting documentation and supporting calculations for the SDI financial statement account "Reserve for RDA Loan" (Account 72-03119) and "Def Notes Receivable" (Account 72-02505), including but not limited to amortization schedules, list of transactions, loan agreements, and interest calculations for the years 7/1/2014 – Current. All records sufficient to identify, calculate, and support the balances reflected in account 72-03119 for the period 7/1/2014 - Current. Responsive records are not limited to documents labeled "support" and include any document that reflects detail, calculations, or justification related to adjustments and balance modifications. If the City maintains these records are the same as the detail ledger excerpts and the reconciliation file, please provide a written explanation as to how the City determines the balances in the accounts, what items it classifies as "Reserve for RDA Loan" and "Def Notes Receivable," what documents are reviewed to calculate the balances, and what causes the balances to change.	Incorrect Documents Received

Based on the City's own responses to these document requests, no documentation has been produced showing what basis supports the statement in the financial statements that "the Department of Finance has disallowed payments for these loans," or what basis supports the City's determination to stop accruing interest as a result. E&E has not been provided with, and is not aware of, any document identifying a specific DOF determination disallowing payment on these two loans since 2014.

5. GASB's Framework for Recognizing Assets and Loss Contingencies

Under GASB Concepts Statement No. 4[17], ¶8, an asset is a resource with "present service capacity that the government presently controls."

GASB Statement No. 62[18] addresses the uncollectibility of a receivable as a category of loss contingency as follows:

- "An estimated loss from a loss contingency (as defined in paragraph 96) should be accrued if both of the following conditions are met:

  a. Information available prior to issuance of the financial statements indicates that it is probable that an asset had been impaired or a liability had been incurred at the date of the financial statements. It is implicit in this condition that it should be probable that one or more future events will occur confirming the fact of the loss.
  b. The amount of loss can be reasonably estimated." **(Paragraph 102)**

- "When a loss contingency exists, the likelihood that the future event or events will confirm the loss or impairment of an asset or the incurrence of a liability can range from probable to remote….

  a. Probable. The future event or events are likely to occur.

  b. *Reasonably possible*. The chance of the future event or events occurring is more than remote but less than likely.

[17] GASB, Concepts Statement No. 4 of the Governmental Accounting Standards Board, Elements of Financial Statements (June 2007). Available at: https://www.gasb.org/page/document?pdf=GASBCS-4.pdf&title=GASB+CONCEPTS+STATEMENT+NO.+4%E2%80%94ELEMENTS+OF+FINANCIAL+STATEMENTS

[18] GASB, Statement No. 62 of the Governmental Accounting Standards Board, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements (December 2010), paragraphs 96–113. Available at: https://storage.gasb.org/GASBS%2062%20combined.pdf

c. *Remote.* The chance of the future event or events occurring is slight." **(Paragraph 100)**

GASB does not provide for deferring a receivable; a receivable is either carried as an asset, reduced by an allowance for any portion not expected to be collected, or written off. From an accounting standpoint, a 100% allowance of the loan receivable is a determination that collection is not probable. That finding, under paragraph 102, must have a basis. The City's financial statements have carried this exact allowance against the two RDA loans since fiscal year 2014, representing every year since that collection on the notes is not probable. Based on the City's responses to E&E's document requests, the basis for that determination has not been produced.

If the City genuinely believed collection of the two RDA loans was not probable, as a 100% allowance reflects, its treatment of these loans since 2014 is difficult to reconcile. The City's 2016 financial statement notes state that it was "still attempting to obtain authorization from the Department of Finance allowing repayment." In 2018, the City Council and the Successor Agency formally approved new loan agreements ratifying the notes and authorizing their repayment, recalculating specific amounts owed under a revised interest rate. Neither action reflects a determination that collection was not probable. The City has not explained how these actions are consistent with the 100% allowance carried on its financial statements for the past 12 years.

Because the loans are offset by a 100% allowance, they do not appear as a net asset on the SDI Fund's balance sheet. For the past 12 years, the public has seen the SDI Fund's assets reported as $20,684,224 lower (excluding additional interest) than they would be if the loans were carried as collectible.

6. Interest Calculated Through Current Date Under Alternative Methodologies

E&E calculated cumulative interest on the two loans through current dates under three scenarios **(See Schedule 14)**. Neither of the RDA promissory notes states whether unpaid interest is simple or compound. The following reflects our interest calculations under the three scenarios:

	Land Note	Plant Note	Total
Principal	$ 4,080,000	$ 5,797,142	$ 9,877,142
Scenario 1: Simple interest at the contractual rate (through 6/30/2025)			
Annual Interest Rate	12% Through 1/26/1993 6.60% from 1/27/1993 - 6/30/2025	7.30%	
Interest	$ 10,137,067	$ 13,542,124	$ 23,679,191
Total	**$ 14,217,067**	**$ 19,339,266**	**$ 33,556,333**
Scenario 2: Compound interest at the contractual rate (through 6/30/2025)			
Annual Interest Rate	12% Through 1/26/1993 6.60% from 1/27/1993 - 6/30/2025	7.30%	
Interest	$ 40,947,603	$ 49,462,115	$ 90,409,718
Total	**$ 45,027,603**	**$ 55,259,257**	**$ 100,286,860**
Scenario 3: Simple interest at 3%, recalculated quarterly (through 6/30/2025)			
Annual Interest Rate	3.00%	3.00%	
Interest	$ 3,886,452	$ 5,573,833	$ 9,460,284
Total	**$ 7,966,452**	**$ 11,457,932**	**$ 19,424,384**

For comparison, the City's audited financial statements report interest of $10,807,082, which has remained unchanged since at least fiscal year 2013, when the City stopped accruing interest on the debt.

XI. E&E Recommendations

E&E's recommendations below are intended to address the specific deficiencies identified in this report. They do not constitute legal advice and are not a substitute for any further action the SDI Advisory Committee, City Council, or other governing body may determine appropriate.

1. Supporting Documentation

   - Retain complete supporting documentation for all SDI Fund transactions and account determinations, including the basis for any allowance, reserve, or write-off recorded against a SDI Fund asset.

   - Require that any determination materially affecting an SDI Fund account balance be supported by a specific, identifiable source document at the time the determination is made, rather than relied upon retroactively.

2. General Ledger and Internal Accounting Controls

   - Document the basis for the $113,643 negative balance in the SDI Fund's general ledger cash account, and correct the general ledger for any portion that cannot be supported.

   - Record cash disbursements individually, with a payee and description, at the time each transaction occurs, rather than as periodic lump-sum entries.

   - Update the SDI Fund's investment balance in the general ledger no less frequently than monthly, reconciled to the SDI Fund's custodian statements.

   - Require a written description for every journal entry that adjusts an account balance, including "opening balance created/modified" entries, sufficient to identify its source and purpose.

   - Require review and approval, by someone other than the preparer, for adjusting journal entries above a defined dollar threshold.

3. Public Financial Reporting

- Reconcile the SDI Fund's investment balance to the SDI Fund's custodian statements before each monthly financial statement is published.

- Disclose on the City's monthly financial statements that the statements are unaudited and have not been reviewed, consistent with AICPA guidance for presenting unaudited financial information.

- Establish a documented review process, separate from the preparer, for monthly financial statements prior to publication.

4. Street Maintenance Reserve

- Complete and publish the accounting of Street Maintenance Reserve expenditures the City has represented as pending in nine consecutive years of audited financial statements.

- Restore itemized reporting of individual reserve accounts within the Street Maintenance Fund, rather than a single consolidated balance.

- Require documentation of the basis, supporting calculation, and approving individual for any future adjustment to a reserve account balance.

5. Investment Oversight and Broker Relationships

- Require documented approval from the City Treasurer and Finance Director for every SDI Fund investment transaction before execution, consistent with Ordinance No. 98-552.

- Fill the Finance Director position to ensure this requirement can be met on an ongoing basis.

- Complete the pre-qualification review required under the City's Municipal Code including a Council-approved Memorandum of Understanding, before engaging or continuing to engage any broker or intermediary.

- Review current SDI Fund holdings for compliance with all requirements of the City's Municipal Code, the City's Accounting and Investment Policies, and California Government Code Section 53601, including the types and issuers of investments permitted, maturity limits, percentage and concentration limits, credit rating requirements, and required Council authorizations, and develop a remediation plan for any holdings found non-compliant.

- Implement periodic monitoring of portfolio composition against these same policy limits going forward.

- Prepare and present quarterly reports on the SDI Fund's cash flow and investments to the SDI Advisory Committee, City Manager, and City Council, as required by the SDI Ordinance (Section 9-6.203(a)) and the City's Accounting Policies and the City's Accounting and Investment Policies (Sec. 7.18), including each item of information the ordinance specifies.

6. RDA Loans Receivable

- Document the basis for the allowance carried against the RDA loans receivable, including any Department of Finance determination relied upon, or reassess the allowance in light of the City's 2018 resolution acknowledging the loans (Resolution No. 05-18-2740).

- Determine the loan terms currently in effect for the RDA Promissory Notes and reconcile the City's audited financial statements to accurately reflect them.

- Establish a periodic reassessment process for long-standing receivables, consistent with GASB Statement No. 62 and Concepts Statement No. 4.

7. Segregation of Duties

- Ensure that no single individual has authority to both execute and approve an SDI Fund investment transaction; trade execution and the Treasurer/Finance Director approval required under Ordinance No. 98-552 should remain functions performed by different individuals.

- Ensure that the individual preparing or posting a general ledger adjusting entry is not also the individual responsible for reviewing or approving it.

- Separate the recording of SDI Fund cash transactions from the reconciliation of those transactions to bank and custodian statements, so no single individual performs both functions.

Our findings and opinions contained in this report are subject to change should new documents or information become available.

Respectfully submitted on
October 9, 2026

Brandon J. Engel

Brandon J. Engel, CPA, CFE, ABV