

**ITEM 4**  
**INCORRECT REDUCTION CLAIM**  
**PROPOSED STATEMENT OF DECISION**

Government Code Section 53646, Subdivisions (a), (b) and (e)  
Statutes of 1995, Chapter 783  
As Amended by Statutes of 1996, Chapters 156 and 749

*Investment Reports*  
Fiscal Years 1995-1996, 1996-1997, 1997-1998, and 1998-1999  
02-9635802-I-47

City of Tustin, Claimant

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**EXECUTIVE SUMMARY**

The sole issue before the Commission is whether the Proposed Statement of Decision accurately reflects any decision made by the Commission at the July 29, 2010 hearing on the above named incorrect reduction claim.<sup>1</sup>

**Recommendation**

Staff recommends that the Commission adopt the Proposed Statement of Decision that accurately reflects the staff recommendation on the incorrect reduction claim. Minor changes, including those to reflect the hearing testimony and the vote count will be included when issuing the final Statement of Decision.

However, if the Commission's vote on Item 3 modifies the staff analysis, staff recommends that the motion on adopting the Proposed Statement of Decision reflect those changes, which would be made before issuing the final Statement of Decision. In the alternative, if the changes are significant, it is recommended that adoption of a Proposed Statement of Decision be continued to the September 30, 2010 Commission hearing.

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<sup>1</sup> California Code of Regulations, title 2, section 1188.1, subdivision (a).

BEFORE THE  
COMMISSION ON STATE MANDATES  
STATE OF CALIFORNIA

IN RE INCORRECT REDUCTION CLAIM  
ON:

Government Code Section 53646,  
Subdivisions (a), (b) and (e); Statutes 1995,  
Chapter 783, As Amended by Statutes 1996,  
Chapters 156 and 749

Fiscal Years 1995-1996, 1996-1997, 1997-  
1998, and 1998-1999

Filed on October 11, 2002, by City of Tustin,  
Claimant.

Case No.: 02-9635802-I-47

***Investment Reports***

STATEMENT OF DECISION  
PURSUANT TO GOVERNMENT CODE  
SECTION 17500 ET SEQ.; TITLE 2,  
CALIFORNIA CODE OF  
REGULATIONS, DIVISION 2,  
CHAPTER 2.5, ARTICLE 7

*(Proposed for Adoption on  
July 29, 2010)*

**STATEMENT OF DECISION**

The Commission on State Mandates (“Commission”) heard and decided this incorrect reduction claim during a regularly scheduled hearing on July 29, 2010. [Witness list will be included in the final Statement of Decision.]

The law applicable to the Commission’s determination of a reimbursable state-mandated program is article XIII B, section 6 of the California Constitution, Government Code section 17500 et seq., and related case law.

The Commission [adopted/modified] the staff analysis to [approve/deny] the incorrect reduction claim at the hearing by a vote of [vote count will be included in the final Statement of Decision].

**Summary of Findings**

This is an incorrect reduction claim filed by the City of Tustin (City) on reimbursement claims for costs incurred in four fiscal years from 1995-1996 through 1998-1999 on the *Investment Reports* program. The issues in dispute involve the preparation and submittal of the annual statement of investment policy, and the activities required to accumulate and compile the quarterly report of investments.

The Commission concludes that the State Controller’s Office incorrectly reduced the costs claimed by the City of Tustin for these activities for fiscal years 1995-1996 through 1998-1999. However, the City did not identify the actual time spent and cost incurred on each activity eligible for reimbursement, but rather identified the total time and cost for each employee. Thus, it cannot be determined from the reimbursement claims how long it took the city treasurer, city finance director, and the account clerks to perform the reimbursable activities.

Accordingly, the Commission hereby remands the reimbursement claims back to the State Controller’s Office for further review and reinstatement of those costs that are eligible for reimbursement in accordance with the Commission’s decision on this incorrect reduction claim. Pursuant to Section VII of the parameters and guidelines, all costs claimed by the City shall be traceable to source documents (e.g., employee time records, invoices, receipts, purchase orders,

contracts, worksheets, calendars, declarations, etc.) that show evidence of the validity of such costs and their relationship to the mandate. All documentation in support of claimed costs shall be made available to the State Controller as may be requested.

## **BACKGROUND**

This is an incorrect reduction claim filed by the City of Tustin on reimbursement claims for costs incurred in four fiscal years from 1995-1996 through 1998-1999 on the *Investment Reports* program.

The issues in dispute in this incorrect reduction claim involve the Controller's reduction of costs claimed following a desk audit for the salaries and benefits of County employees attending training, preparing and reviewing the annual statement of investment policy, investment tracking and balancing subsidiary ledgers "required for the preparation of the quarterly report of investments," and contracted services for city auditors to review policy and audit investment policy and quarterly reports to ensure compliance with state law.

### *Investment Reports Program (Statement of Decision and Parameters and Guidelines)*

In 1996, the County of Santa Clara and the City of Newport Beach filed a test claim on Government Code section 53646, subdivisions (a), (b), and (e), as amended in 1995 and 1996.<sup>2</sup> The test claim statutes were enacted following recommendations from the Task Force on Local and State Investment Practices.<sup>3</sup> The Task Force was assembled at the request of Governor Pete Wilson for the purpose of reporting recommendations and findings for possible investment guidelines to be considered by the Legislature as a result of the losses incurred by the Orange County investment pool.<sup>4</sup>

As amended, Government Code section 53646 stated the following:

(a)(1) In the case of county government, the treasurer shall annually render to the board of supervisors and any oversight committee a statement of investment policy, which the board shall review and approve at a public meeting. Any change in the policy shall also be reviewed and approved by the board at a public meeting.

(2) In the case of any other local agency, the treasurer or chief fiscal officer of the local agency shall annually render to the legislative body of that local agency and any oversight committee of that local agency a statement of investment policy, which the legislative body of the local agency shall consider at a public meeting. Any change in the policy shall also be considered by the legislative body of the local agency at a public meeting.

(b)(1) The treasurer or chief fiscal officer shall render a quarterly report to the chief executive officer, the internal auditor, and the legislative body of the local agency. The quarterly report shall be so submitted within 30 days following the

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<sup>2</sup> Statutes 1995, chapter 783; Statutes 1996, chapters 156 and 749.

<sup>3</sup> Analysis of Senate Committee on Local Government, March 30, 1995, Senate Bill 564 (1995-96 Leg. Sess.).

<sup>4</sup> The Task Force's report, dated March 14, 1995.

end of the quarter covered by the report. Except as provided in subdivision (e), this report shall include the type of investment, issuer, date of maturity par and dollar amount invested on all securities, investments and moneys held by the local agency, and shall additionally include a description of any of the local agency's funds, investments, or programs, that are under the management of contracted parties, including lending programs. With respect to all securities held by the local agency, and under management of any outside party that is not also a local agency or the State of California Local Agency Investment Fund, the report shall also include a current market value as of the date of the report, and shall include the source of this same valuation.

(2) The quarterly report shall state compliance of the portfolio to the statement of investment policy, or manner in which the portfolio is not in compliance.

(3) The quarterly report shall include a statement denoting the ability of the local agency to meet its pool's expenditure requirements for the next six months, or provide an explanation as to why sufficient money shall, or may, not be available.

(4) In the quarterly report, a subsidiary ledger of investments may be used in accordance with accepted accounting practices.

(c) Pursuant to subdivision (b), the treasurer or chief fiscal officer shall report whatever additional information or data may be required by the legislative body of the local agency.

(d) The legislative body of a local agency may elect to require the report specified in subdivision (b) to be made on a monthly basis instead of quarterly.

(e) For local agency investments that have been placed in the Local Agency Investment Fund, created by Section 16429.1, in Federal Deposit Insurance Corporation-insured accounts in a bank or savings and loan association, in a county investment pool, or any combination of these, the treasurer or chief fiscal officer may supply to the governing body, chief executive officer, and the auditor of the local agency the most recent statement or statements received by the local agency from these institutions in lieu of the information required by paragraph (1) of subdivision (b) regarding investments in these institutions.<sup>5</sup>

On March 27, 1997, the Commission adopted a Statement of Decision finding that Government Code section 53646, subdivisions (a), (b), and (e) constituted a reimbursable state-mandated program. The parameters and guidelines, adopted on November 20, 1997, describe the following activities as eligible for reimbursement:

1. Statement of Investment Policy

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<sup>5</sup> Government Code section 53646 has since been amended by Statutes 1997, chapter 825; Statutes 1998, chapter 82; Statutes 2000, chapter 687; Statutes 2002, chapter 454; Statutes 2004, chapter 889; and Statutes 2008, chapter 709. The amendments made in 2004 (AB 2853) changed the "shall" to "may" in subdivisions (a)(1) and (2), and (b)(1), to eliminate the mandate to render and approve the annual statement of investment policy and to render the quarterly report of investments.

Prepare and submit the annual statement of investment policy, and changes to:

- a. The legislative body and any oversight committee for consideration at a public meeting, effective January 1, 1996.
- b. The county board of supervisors and any oversight committee for review and approval at a public meeting, effective January 1, 1997.

2. Quarterly Reports of Investments

a. Implementation Costs

Develop or modify existing policies and procedures for accumulating and compiling data to prepare the quarterly report of investments, as required in section 53646, subdivisions (b)(1), (2), and/or (e).

b. Ongoing Costs

(1) Accumulate and compile data necessary to prepare the quarterly reports of investments, as required in Government Code section 53646, subdivisions (b)(1), (2), and (3) and/or (e).

(2) Render a quarterly report of investments to the chief executive officer, the internal auditor, and the legislative body of the local agency or school district, as required in Government Code section 53646, subdivision (b)(1).<sup>6</sup>

Section VI of the parameters and guidelines addresses claim preparation and instructs eligible claimants to include in their claim the salaries and benefits of employees performing the mandated activities. Employee costs “should be supported by name, position, productive hourly rate, hours worked, fringe benefits amount, and a brief description of assigned unit and function relative to the mandate.” Claimants are also instructed to include in their claim descriptions of services and supplies, and contract services, and to maintain the supporting data for all costs claimed to be “made available to the State Controller or his/her agent, as may be requested ...”

The claiming instructions were issued in January 1998. The reimbursable activities listed in the claiming instructions are consistent with the parameters and guidelines.

Reimbursement Claims Filed by the City of Tustin and the Controller’s Reductions

The reimbursement claims filed by the City of Tustin for fiscal years 1995-1996 through 1998-1999 identify claimed activities to prepare and submit the annual statement of investment policy and to accumulate and compile data to render the quarterly report of investments.

Annual Statement of Investment Policy

To prepare and submit the annual statement of investment policy, the City claimed reimbursement for the salaries and benefits of the following employees to perform the following list of activities:

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<sup>6</sup> Footnote 1 of the parameters and guidelines recognized potential offsetting revenue for counties with Treasury Oversight Committees when preparing and submitting the annual statement of investment policy to the county’s legislative body. The issues in this claim do not address the annual statement of investment policy.

1. City Treasurer:

- Research and review state statutes to determine what changes to the City's investment policy would be required.
- Attend meetings and seminars to be trained on the new requirements.
- Meet with staff and brokers to update investment policy and ensure compliance.
- Draft and edit new policy language.

2. City Finance Director:

- Review and edit annual statement of investment policy.
- Attend meetings with the City Treasurer with brokers to update investment policy.
- Implement the investment policies and procedures.
- Present new policy to the [governing body and/or any oversight committee].

Handwritten notes of the State Controller's Office are provided on copies of the reimbursement claims for fiscal years 1995-1996 through 1997-1998. These notes indicate that the amounts claimed for the above activities were reduced "for excessive time" to 10% and 4% of the amount claimed.

According to the State Controller's Office, the fiscal year 1998-1999 claim was reduced for the same reasons as those cited for the preceding three fiscal years.

Quarterly Reports of Investment

The City claimed reimbursement for the salaries and benefits of City employees to accumulate and compile data to render the quarterly report of investments as follows:

1. Senior Account Clerk(s):

For fiscal years 1995-1996 through 1997-1998

- Enter data into investment tracking system.
- Balance subsidiary ledgers required for the preparation of the quarterly investment report.
- Show all detail as required by the state.

For fiscal year 1998-1999

- Accumulate and balance investment data and balance "them to those reports submitted to their Bank or 'Safekeeping Agent'."
- Enter data into investment spreadsheets to monitor principal and interest earnings for each investment as required by state statute.

2. City Finance Director:

- Review quarterly investment report.
- Present quarterly investment report to city council.

3. Assistant Finance Director:

- Review and ensure the information in the subsidiary ledgers is accurate.
- Review and ensure the information in the quarterly report is accurate.
- Supervise, audits, and internal control procedures.

4. City Auditors (contract services):

- Review policy.
- Audit investment policy and quarterly reports to ensure compliance with all state laws.

The city auditors spent eight (8) hours each fiscal year on these activities.

Handwritten notes of the State Controller’s Office on copies of the reimbursement claims for fiscal years 1995-1996, 1996-1997, and 1997-1998, indicate the amounts claimed for the Senior Account Clerk were reduced to \$0 because “daily/monthly accounting activities are not mandated.” The amount claimed for the Assistant Finance Director for fiscal year 1995-1996 was also reduced to \$0. Finally, the amounts claimed for the services of the City Auditors were reduced to \$0, with a note indicating “not a mandated activity.”

According to the State Controller’s Office, the fiscal year 1998-1999 claim was reduced for the same reasons as those cited for the preceding three fiscal years.

Reduction of Costs

The State Controller’s Office also reduced the indirect costs claimed that correspond to the reductions made to the direct costs.

Total reductions made to the City’s reimbursement claims are identified in the table below.

	Fiscal Year 1995-1996	Fiscal Year 1996-1997	Fiscal Year 1997-1998	Fiscal Year 1998-1999
Costs claimed	\$21,691	\$41,468	\$47,699	\$36,418
Amount Reduced	(\$19,082)	(\$37,952)	(\$43,007)	(\$32,550)
Approved Payment Amount	\$2,609	\$3,516	\$4,692	\$3,868

**Claimant’s Position**

The City of Tustin contends that the State Controller’s Office incorrectly reduced its claims for reimbursement. The City argues that its claims were complete and were prepared in accordance with the parameters and guidelines and claiming instructions issued for this program.

The City further believes that the reductions made to the activities of rendering the quarterly reports of investments are incorrect. The incorrect reduction claim states the following:

The claims prepared for the City of Tustin included costs associated with the data entry of investment transactions and the time to prepare and utilize subsidiary ledgers of investments. These costs were identified as allowable activities in the

Parameters and Guidelines. Use and development of these ledgers are necessary to prepare the city's quarterly investment reports.

On October 27, 2003, the City of Tustin filed a reply stating the following:

There may [be] some confusion as to [the] meaning of "subsidiary ledgers." When CRS filed the Investment Reporting claims on behalf of the city, we assumed that spreadsheets developed in-house to track investments in compliance with the law, were entitled "subsidiary ledgers" due to the terminology used in the claiming instructions. We believe that it is unfair to disallow entry of investment data into an in-house systems (excel spreadsheets) when it is allowed for those city's [sic] utilizing proprietary software systems such as SYMPRO.

We disagree that our claims were "excessive or unreasonable" and believe that the State Controller's Office's review and disallowances were arbitrary and inconsistent. If more documentation was desired, they should have stated that in their correspondence so that the issue could have been addressed at the time. On page two of the State Controller's letter [dated August 11, 2003], they quote and emphasize, "... documentation in support of the claimed costs shall be made available to the State Controller or his/her agency, **as may be requested**."

Based on information available to me, the State Controller's Office never made a request to the City asking for additional documentation. All invoices for services were attached to the claims. The State's remittance advise simply states "COSTS NOT MANDATED" leaving the City to believe that the activities related to data entry and maintenance of investment data for production of the quarterly report was NOT ELIGIBLE.

According to the Ps and Gs at the time and claiming instructions issued "accumulating and compiling data" WAS a reimbursable activity. That is all that was claimed. Without data entry of the investment transactions into our investment software system, production of a report is not possible. Nowhere in the claim was there a mention of "daily" tracking or other "daily" activities. The State's correspondence unfairly assumes that daily input or reconciliation is taking place when there is NO reference whatsoever in the claim that would indicate that this is the case. [Emphasis in original.]

The claimant filed comments on the draft staff analysis disagreeing with the analysis and proposed conclusion that reimbursement is not required for entering, tracking, balancing, and auditing every investment transaction to prepare the quarterly report of investments. The claimant argues the following:

It is our opinion that recording each investment transaction is exactly what is meant by "accumulating and compiling data." It is a putting together or gathering investment data so that conclusions can be inferred. It did not say "photocopying pre-existing third party reports and investment statements at the end of each quarter and presenting this to the governing body." It appears that this is what the Commission staff is recommending.

Our claims requested approximately \$5,000 per year of staff salary and benefits per year for these activities relating to the preparation of the quarterly reports.



We don't believe this was excessive or unreasonable. By disallowing the cost of entering all investment transactions (the purchase and sale of investments, recording of interest, etc.) the report becomes a meaningless, potentially inaccurate document solely comprised of second hand information that has not been properly reviewed or verified. We do not believe that this was the intent of the legislation. The Treasurer of each jurisdiction must certify the accuracy of the investment report and data it contains to his or her governing body. Asking them to present and sign off on a compilation of unchecked, photocopied, second hand reports is not reasonable or responsible.

### **Position of the State Controller's Office**

Comments by the State Controller's Office on the incorrect reduction claim state the following:

The subject claims were reduced because many of the activities were not reimbursable, and there was a lack of source documentation. In addition to the inability to verify the claim, the lack of source documentation also makes it difficult to prorate reimbursement for those activities for which only a portion of the expense was reimbursable. The reductions were appropriate given the Parameters and Guidelines, the statement of decision, applicable statutes, and amount of documentation provided.

The State Controller's Office also submitted an "analysis of the incorrect reduction claim," dated April 16, 2003, which describes the adjustments and reductions for fiscal years 1995-1996 through 1997-1998.<sup>7</sup> With respect to each of these fiscal year reductions, the analysis states the following:

This claim was reduced for salaries and benefits and corresponding indirect costs for system maintenance and daily data download activities that were deemed by the State Controller's Office (SCO) Division of Accounting and Reporting (DAR) staff as activities not mandated or as non-reimbursable components of the Parameters and Guidelines (Ps & Gs). This claim contained ... costs that were deemed excessive to prepare and submit the annual statement of investment policies, which consists of changes to those existing policies, and the quarterly report of investments as required by the Investment Reports program. No time sheets or detailed tasks were available. DAR staff recognized that the county would have incurred a cost and made a reasonable effort to provide reasonable compensation for this activity.

On July 13, 2010, the State Controller's Office filed comments concurring with the draft staff analysis.

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<sup>7</sup> The State Controller's "analysis of the incorrect reduction claim" does not include information about the reduction made to the fiscal year 1998-1999 reimbursement claim. In addition, the "Sub Exhibit 1" to the analysis contains a "Claim Adjustment Detail List," which states that "no adjustment" was made to the 1998-1999 reimbursement claim and that \$8,593 was paid to the City of Tustin for that fiscal year. However, the State Controller's Office has confirmed by letter dated May 11, 2010, that a reduction to the 1998-1999 reimbursement claim was made for the same reasons as those cited for the preceding three fiscal years.

## **Position of the Department of Finance**

The Department of Finance filed comments on the draft staff analysis stating that “[t]he conclusions of the CSM staff appear reasonable; therefore, Finance does not have significant concerns with the staff recommendation.”

## **COMMISSION FINDINGS**

Government Code section 17561, subdivision (b), authorizes the State Controller’s Office to audit the claims filed by local agencies and school districts and to reduce any claim for reimbursement of state mandated costs that the State Controller’s Office determines is excessive or unreasonable.

Government Code Section 17551, subdivision (d), requires the Commission to hear and decide a claim that the State Controller’s Office has incorrectly reduced payments to the local agency or school district. That section states the following:

The commission, pursuant to the provisions of this chapter, shall hear and decide upon a claim by a local agency or school district filed on or after January 1, 1985, that the Controller has incorrectly reduced payments to the local agency or school district pursuant to paragraph (2) of subdivision (b) of Section 17561.

If the Commission determines that a reimbursement claim has been incorrectly reduced, section 1185.7 of the Commission’s regulations requires the Commission to send the Statement of Decision to the State Controller’s Office and request that the costs in the claim be reinstated.

**Issue 1: Did the State Controller’s Office incorrectly reduce the costs for the salaries and benefits of city treasurer and finance director to prepare and submit the annual statement of investment policy to the legislative body of the city?**

Beginning January 1, 1996, the parameters and guidelines and claiming instructions for this program allow reimbursement to prepare and submit the annual statement of investment policy, and changes to the legislative body and any oversight committee for consideration at a public meeting.

To prepare and submit the annual statement of investment policy, the City claimed reimbursement for the salaries and benefits of the city treasurer to perform the following activities:

- Research and review state statutes to determine what changes to the City’s investment policy would be required.
- Attend meetings and seminars to be trained on the new requirements.
- Meet with staff and brokers to update investment policy and ensure compliance.
- Draft and edit new policy language.

The City also claimed the time of its finance director to:

- Review and edit annual statement of investment policy.
- Attend meetings with the City Treasurer with brokers to update investment policy.
- Implement the investment policies and procedures.

- Present new policy to the [governing body and/or any oversight committee].

The City of Tustin has not identified the actual time spent and cost incurred by the city treasurer and finance director on each activity listed above. However, as identified in the table below, the City claimed reimbursement for the total hours worked by the city treasurer and finance director to perform all of the above activities for each fiscal year at issue. The State Controller’s Office reduced the time claimed as “excessive time,” and for fiscal year 1995-1996, allowed reimbursement for ten percent (10%) of the time and costs claimed. Reimbursement was allowed for four percent (4%) of the time and costs claimed for fiscal years 1996-1997 and 1997-1998. Although the record does not reflect the exact amount reduced in fiscal year 1998-1999 to prepare and submit the annual statement of investment policy, the State Controller’s Office states that the fiscal year 1998-1999 claim was reduced for the same reasons as those cited for the preceding three fiscal years.

<u>Fiscal Year</u>	<u>Hours Worked by City Treasurer</u>	<u>Hours Worked by City Finance Director</u>	<u>Total Hours Claimed</u>	<u>Hours Allowed by State Controller’s Office</u>
1995-1996	104	130	234	23
1996-1997	200	250	450	18
1997-1998	208	260	468	19
1998-1999	1	1	2	?

**A. The State Controller’s Office incorrectly reduced the costs for salaries and benefits of the city treasurer and finance director to prepare and submit the annual statement of investment policy**

Staff finds that the reduction by the State Controller’s Office of the salary and benefit costs of the treasurer and finance director regarding the annual statement of investment policy is arbitrary, not based on the parameters and guidelines, and not based on any evidence in the record. In this respect, staff finds that these reductions are incorrect.

The amount of reimbursement approved for preparing and submitting the annual statement of investment policy, at 4% and 10% of the costs claimed, is arbitrary. There is no evidence in the record to explain or justify the percentages allowed and the amounts reduced. Nor does the record indicate whether the Controller’s Office analyzed the activities claimed by the City of Tustin to prepare and submit the annual statement of investment policy. The percentages allowed do not appear to correlate to the activities performed by the treasurer and finance director to prepare and submit the annual statement of investment policy. Although the Controller’s Office argues that the lack of source documentation made it difficult to verify the costs claimed, the reductions in this case were made following a desk audit and there is no evidence in the record that the Controller’s Office asked for any supporting documentation. Section VII of the parameters and guidelines states that “all documentation in support of claimed costs shall be made available to the State Controller ..., *as may be requested.*” (Emphasis added.)

Moreover, the State Controller's Office does not have the authority to adopt a uniform allowance of costs, such as the percentages allowed in this case. At the time the parameters and guidelines were adopted in 1997, the Commission had the authority to adopt a uniform allowance in lieu of requiring actual cost claims for time spent on a mandated activity for inclusion in the parameters and guidelines.<sup>8</sup> The parameters and guidelines, however, do not include a uniform allowance for time spent preparing and submitting the annual statement of investment policy. Rather, Section VI of the parameters and guidelines (Claim Preparation) allows reimbursement for the actual costs of salaries and benefits to perform the mandated activities. The parameters and guidelines state that "claimed reimbursement for employee costs should be supported by name, position, productive hourly rate, hours worked, fringe benefits amount, and a brief description of assigned unit and function relative to the mandate." Pursuant to Government Code section 17558, as the statute existed in 1997<sup>9</sup> and today, the claiming instructions prepared by the Controller's Office are required to be derived from the adopted parameters and guidelines. Thus, the Controller's reduction of time to a uniform allowance of a percentage of time identified by the claimant is not consistent with the parameters and guidelines.

Accordingly, the Commission finds that the State Controller's Office incorrectly reduced the salary and benefit costs of the city treasurer and finance director for the time spent preparing and submitting the annual statement of investment policy to the legislative body of the city.

**B. The City's reimbursement claims to prepare and submit the annual statement of investment policy contain costs that are not reimbursable**

As described below, staff finds that the City's reimbursement claims contain costs for activities that go beyond the scope of the mandate and are not reimbursable. Although these investment activities may be required by the City's local policy, the issue is whether these activities are mandated by the state and reimbursable under the test claim statute, the Statement of Decision, and the parameters and guidelines.<sup>10</sup>

Generally, the same rules of construction and interpretation that apply to statutes will govern the construction and interpretation of an administrative agency's rules, such as the parameters and guidelines.<sup>11</sup> The interpretation of an administrative agency rule, like the parameters and guidelines, is a question of law.<sup>12</sup> Under the rules of statutory construction, when the language of an administrative agency's rule, such as the parameters and guidelines, is plain, the court is

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<sup>8</sup> Government Code section 17557, subdivision (b) (as amended by Stats. 1995, ch. 945) stated the following: "In adopting parameters and guidelines, the commission may adopt an allocation formula or uniform allowance which would provide for reimbursement of each local agency or school district of a specified amount each year."

<sup>9</sup> Former Government Code section 17558, as amended by Statutes 1996, chapter 45, operative on July 1, 1996.

<sup>10</sup> In this respect, the Commission no longer has jurisdiction to exercise discretion to add reimbursable activities to the parameters and guidelines that are "reasonable methods of complying with the mandate," pursuant to section 1183.1 of the Commission's regulations. The issue is what the Commission intended when it adopted the parameters and guidelines in 1997.

<sup>11</sup> *Cal. Drive-in Restaurant Ass'n v. Clark* (1943) 22 Cal.2d 287, 292.

<sup>12</sup> *Culligan Water Conditioning v. State Board of Equalization* (1976) 17 Cal.3d 86, 93.

required to enforce the provisions according to the terms of the document. The California Supreme Court determined that:

In statutory construction cases, our fundamental task is to ascertain the intent of the lawmakers so as to effectuate the purpose of the statute. We begin by examining the statutory language, giving the words their usual and ordinary meaning. If the terms of the statute are unambiguous, we presume the lawmakers meant what they said, and the plain meaning of the language governs. [Citations omitted.]<sup>13</sup>

Moreover, the language of the parameters and guidelines must be construed in the context of the entire statutory scheme in which the test claim statute is a part, so that every provision of the statutory scheme may be harmonized and have effect.<sup>14</sup> The court may not disregard or enlarge the plain provisions of the administrative rule, nor may it go beyond the meaning of the words used when the words are clear and unambiguous. Thus, the court is prohibited from writing into an administrative rule, by implication, express requirements that are not placed in the law.<sup>15</sup> In addition, it is presumed that the administrative agency, like the Commission when it adopted the parameters and guidelines, did not adopt a rule that alters or enlarges the terms of a legislative enactment.<sup>16</sup>

Applying these rules of construction, the Commission finds that the City's reimbursement claims contain costs for activities that go beyond the scope of the mandate and are not reimbursable. A reduction of these costs would be correct and in accordance with the test claim statute, the Statement of Decision, the parameters and guidelines, and claiming instructions.

- 1) Reimbursement is not required to implement and ensure compliance with the City's investment policies.

The City claims costs for the treasurer and finance director to "implement the investment policies and procedures" and to "ensure compliance" with the investment policy. Although the annual statements of investment policies adopted by the City of Tustin for the years in question impose duties on the treasurer and financial director to implement the investment policy, implementation of the investment policy is not mandated by the test claim statute, or identified in the Statement of Decision, the parameters and guidelines, or claiming instructions as a reimbursable activity.

For example, the City of Tustin's annual investment policies adopted for the years in question require that the treasurer review, authorize and document every investment transaction; that the investments be transacted only through brokers/dealers that have been reviewed by the finance director or treasurer; that the treasurer periodically obtain economic forecasts from economists and financial experts through bankers and brokers in order to assist the treasurer with the formulation of investment plans; and that the treasurer execute investment transactions that conform to current and anticipated cash requirements, interest rate trends, and stated investment strategy. These activities are not mandated by the state. Rather, reimbursement is required only

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<sup>13</sup> *Estate of Griswald* (2001) 25 Cal.4th 904, 910-911.

<sup>14</sup> *City of Merced v. State of California* (1984) 153 Cal.App.3d 777, 781-782.

<sup>15</sup> *Whitcomb v. California Employment Commission* (1944) 24 Cal.2d 753, 757.

<sup>16</sup> *Wallace v. State Personnel Board* (1959) 168 Cal.App.2d 543, 547.

to prepare and submit the annual statement of investment policy, and any changes to the policy, to the legislative body and any oversight committee for consideration at a public meeting.

This conclusion is further supported by the report prepared by the Task Force on Local and State Investment Practices, which recommended the amendment to Government Code section 53646 and is cited in the analysis prepared by the Senate Local Government Committee for the test claim statute. The report recognizes that “[b]y requiring that each local agency to have a written annual statement of investment policy, *the State is not mandating specific investment objectives, practices and procedures; the State is simply requiring that each local agency address those issues itself by adopting a written annual statement of investment policy.*” (Emphasis added.)

Thus, the Commission finds that the costs claimed to implement and ensure compliance with the City’s investment policy are not reimbursable, and that a reduction of these costs is correct and in accordance with the test claim statute, the Statement of Decision, the parameters and guidelines, and claiming instructions.

2) Reimbursement is not required for training in this case.

The City also claims costs for its treasurer to “attend meetings and seminars to be trained on the new requirements.” Part D of Section VI of the parameters and guidelines authorizes reimbursement for training of personnel on the mandated program, and requires that the claim for “specialized training must be justified by the claimant.” The claiming instructions similarly state the following:

Only the cost for a reasonable number of employees attending the training is reimbursable. *Special training must be justified in writing by the claimant. Give the class title, dates, location, and name(s) of the employee(s) attending training classes associated with the mandate. Reimbursable costs may include salaries and benefits for time spent, the registration fee, transportation, lodging, and per diem. Reimbursement for travel expenses, lodging, and per diem will be reimbursed in accordance with the travel rules of the local jurisdiction.* (Emphasis added.)

Based on the plain language of the parameters and guidelines and claiming instructions, “specialized” training is allowable only as it relates directly to the preparation of the annual statement of investment policy and submittal to the legislative body and any oversight committee for consideration at a public meeting. Reimbursement for training regarding the implementation of the City’s investment policies or investment planning of City funds goes beyond the scope of the mandate and is not reimbursable here.

Moreover, the City did not comply with the requirements of the parameters and guidelines and claiming instructions by providing justification in writing with the reimbursement claims for “specialized” training costs that may be related directly to the mandated activity. Nor has any justification for “specialized” training costs been provided in the City’s incorrect reduction claim filing.

Accordingly, the Commission finds the costs incurred by the City for training are not reimbursable, and that a reduction of the training costs claimed would be correct and in accordance with the test claim statute, the parameters and guidelines, and claiming instructions.

### **C. Reinstatement of costs for salaries and benefits**

Pursuant to section 1185.7 of the Commission's regulations, if the Commission determines that a reimbursement claim has been incorrectly reduced, the Commission is required to send the Statement of Decision on the incorrect reduction claim to the State Controller's Office and request that the costs in the claim be reinstated.

In this case, the Commission finds that the State Controller's Office incorrectly reduced the reimbursement claims for salaries and benefits on the ground that the reductions are arbitrary and not based on the evidence in the record. However, the reimbursement claims include activities and costs for implementing the City's investment policy and for training that are not reimbursable. Thus, not all the costs claimed by the City for salaries and benefits are reimbursable and can be reinstated.

However, the City did not identify the actual time spent and cost incurred on each activity, but rather identified the total time and cost for each employee. Thus, it cannot be determined from the reimbursement claims how long it took the city treasurer and finance director to perform the reimbursable activities.

Accordingly, the Commission hereby remands the reimbursement claims back to the State Controller's Office to further review the City's claims for the costs of the salaries and benefits of the city treasurer and finance director to perform the reimbursable activities required to prepare and submit the annual statement of investment policy, and in accordance with the Commission's decision on this incorrect reduction claim, to reinstate the costs that are eligible for reimbursement. Pursuant to Section VII of the parameters and guidelines, all costs claimed by the City shall be traceable to source documents (e.g., employee time records, invoices, receipts, purchase orders, contracts, worksheets, calendars, declarations, etc.) that show evidence of the validity of such costs and their relationship to the mandate. All documentation in support of claimed costs shall be made available to the State Controller as may be requested.

**Issue 2: Did the State Controller's Office incorrectly reduce the costs for the salaries and benefits of City employees to accumulate and compile the data necessary to prepare the quarterly report of investments and to render the reports to the chief executive officer, the internal auditor, and the legislative body of the local agency?**

The parameters and guidelines, and claiming instructions for this program allow reimbursement to accumulate and compile the data necessary to prepare the quarterly reports of investment and to render the reports to the local agency. As indicated by the plain language of Government Codes section 53646, as amended by the test claim statutes, the quarterly investment report shall include the following information:

1. Type of investment, issuer, date of maturity, par and dollar amount invested on all securities, investments and moneys held by the local agency.
2. Description of any of the local agency's funds, investments, or programs, that is under the management of contracted parties, including lending programs.
3. Current market value as of the date of the report, and source of this same valuation of all securities held by the local agency, and under management of any outside party that is not also a local agency or the State of California Local Agency Investment Fund.

4. Statement that the portfolio is in compliance with the statement of investment policy, or the manner in which the portfolio is not in compliance.
5. Statement denoting the ability of the local agency to meet its pool's expenditure requirements for the next six months, or provide an explanation as to why sufficient money shall, or may not be available.

To accumulate and compile the data necessary to prepare the quarterly reports of investment and to render the reports to the local agency, the City claimed the salaries and benefits of senior account clerk(s) for the time spent (from 65 to 125 hours per fiscal year) performing the following activities:

For fiscal years 1995-1996 through 1997-1998

- Enter data into investment tracking system.
- Balance subsidiary ledgers required for the preparation of the quarterly investment report.
- Show all detail as required by the state.

For fiscal year 1998-1999

- Accumulate and balance investment data and balance “them to those reports submitted to their Bank or ‘Safekeeping Agent’.”
- Enter data into investment spreadsheets to monitor principal and interest earnings for each investment as required by state statute.

In addition, the City claimed costs for the salary and benefits of its assistant finance director for the time spent each fiscal year (6 to 24 hours) to:

- Review and ensure the information in the subsidiary ledgers is accurate.
- Review and ensure the information in the quarterly report is accurate.
- Supervise, audits, and internal control procedures.

Finally, the City claimed the contract service costs for the eight (8) hours spent by city auditors each fiscal year to perform the following activities:

- Review policy.
- Audit investment policy and quarterly reports to ensure compliance with all state laws.

Handwritten notes of the State Controller’s Office on copies of the reimbursement claims for fiscal years 1995-1996, 1996-1997, and 1997-1998, indicate the amounts claimed for the Senior Account Clerk were reduced to \$0 because “daily/monthly accounting activities are not mandated.” The amount claimed for the Assistant Finance Director for fiscal year 1995-1996 was also reduced to \$0. Finally, the amounts claimed for the services of the City Auditors were reduced to \$0 in all fiscal years, with a note indicating “not a mandated activity.”

According to the State Controller’s Office, the fiscal year 1998-1999 claim was reduced for the same reasons as those cited for the preceding three fiscal years.



**A. The State Controller's Office incorrectly reduced the costs for salaries and benefits of the senior account clerks and the assistant finance director**

The Commission finds that the reduction by the Controller's Office of the salary and benefit costs of the senior account clerks and the assistant finance director to \$0 is arbitrary and not consistent with the evidence in the record. In this respect, staff finds that the reductions of salary and benefit costs are incorrect.

The City's reimbursement claims are filed under penalty of perjury and show that the senior account clerks worked on the quarterly report of investments by entering data into the investment tracking system and helping to prepare the quarterly investment reports. The total time claimed by the senior account clerks for all work performed on the quarterly report of investments ranged from 65 to 125 per fiscal year, or from 16.25 hours to 31.25 hours per quarterly report.

In November 2003, the Commission adopted amendments to the parameters and guidelines for this program clarifying that reimbursement was allowed for one-time data entry into investment reporting applications or software to describe the type of investment and issuer, date of maturity, and par and dollar amount investment for *each investment held on the last day of each quarter*. Although the period of reimbursement for the parameters and guidelines amendment is effective for costs incurred beginning in fiscal year 1998-1999 (one and two years after some of the reductions were made to the reimbursement claims in this case), the Commission's analysis and findings can be used to determine what the Commission intended when it adopted the original parameters and guidelines in 1997 because the parameters and guidelines amendment simply clarified the mandated activities. Pursuant to the rules of statutory construction, a clarification of existing law may be applied to transactions predating its enactment without being considered a retroactive application of the law. The clarified law is merely a statement of what the law has always been.<sup>17</sup> In this case, the parameters and guidelines amendment was merely a clarification of what the reimbursable activities have always been. Thus, to the extent the senior account clerks performed the one-time activity of entering data into the investment tracking system for each investment held on the last day of the quarter, those costs would be eligible for reimbursement. A denial of all costs incurred for the senior account clerks is not consistent with the parameters and guidelines or the evidence provided in the reimbursement claims.

In addition, the City's reimbursement claim for fiscal year 1995-1996 shows that the assistant finance director worked on the quarterly report of investments by reviewing the information in the quarterly reports to ensure accuracy. The 1995-1996 reimbursement claim is signed under penalty of perjury by the assistant finance director.

Although the State Controller's Office recognizes that the City "would have incurred a cost and made a reasonable effort to provide reasonable compensation for this activity,"<sup>18</sup> a reduction of the salaries and benefits of the senior account clerks and assistant finance director to \$0 does not take into account the requirements of the test claim statute, the parameters and guidelines, and the evidence in the record.

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<sup>17</sup> *McClung v. Employment Development Dept.* (2004) 34 Cal.4th 467, 471, quoting *Western Security Bank v. Superior Court* (1997) 15 Cal.4th 232, 243; *Riley v. Hilton Hotels Corp.* (2002) 100 Cal.App.4th 599, 603.

<sup>18</sup> Analysis of Incorrect Reduction Claim dated April 16, 2003.

Accordingly, the Commission finds that the State Controller's Office incorrectly reduced the salary and benefit costs for the senior account clerks and the assistant finance director to \$0.

**B. But the City's reimbursement claims for the quarterly report of investments contain costs for activities that go beyond the scope of the mandate and are not reimbursable**

The Commission finds, however, that the City's reimbursement claims contain costs for activities identified below that go beyond the scope of the mandate and are not reimbursable.

1) Reimbursement is not required for the costs to prepare a quarterly report of investments for the Tustin Community Redevelopment Agency.

On January 16, 2004, the City filed copies of its quarterly investment reports from fiscal years 1995-1996 through 1998-1999. Included in the filing are the quarterly reports of the Tustin Community Redevelopment Agency for each fiscal year in question.

The Tustin Community Redevelopment Agency was created in 1976 and is made up of members of the Tustin City Council. Pursuant to Health and Safety Code section 33200, the city council may, by the adoption of an ordinance, declare itself to be a redevelopment agency and have all the rights and duties of a redevelopment agency under the Community Redevelopment Law (Health and Saf. Code §§ 33000 et seq.). Thus, even though city employees may do the work of a redevelopment agency, the redevelopment agency is a body separate from the city and the work is performed under the Community Redevelopment Law.

Redevelopment agencies, including the Tustin Community Redevelopment Agency, do not receive their revenue from proceeds of taxes, but instead primarily receive revenue through tax increment financing. Tax increment financing is described as follows:

Tax increment revenues are computed as follows: The real property within a redevelopment project area is assessed in the year the redevelopment plan is adopted. Typically, after redevelopment, property values in the project area increase. The taxing agencies (e.g., city, county, school or special district) keep the tax revenues attributable to the original assessed value and pass the portion of the assessed property value which exceeds the original assessment on to the redevelopment agency. (Health & Saf. Code, §§ 33640, 33641, 33670, 33675). In short, tax increment financing permits a redevelopment agency to take advantage of increased property tax revenues in the project areas without an increase in the tax rate.<sup>19</sup>

Pursuant to Health and Safety Code section 33678, revenue received through tax increment financing shall not be deemed to be the proceeds of taxes within the meaning of article XIII B of the California Constitution. Thus, expenditures made by a redevelopment agency from tax increment financing are not eligible for reimbursement under article XIII B, section 6.<sup>20</sup>

In addition, a city council is authorized to grant or loan money to a redevelopment agency for

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<sup>19</sup> *Redevelopment Agency of the City of San Marcos v. Commission on State Mandates* (1997) 55 Cal.App.4th 976, 982.

<sup>20</sup> *Id.* at p. 986-987; *City of El Monte v. Commission on State Mandates* (2000) 83 Cal.App.4th 266, 280-281.

administrative expenses.<sup>21</sup> Money received and expended through grants or loans are not eligible for reimbursement. Subvention is required under article XIII B, section 6 only when the costs can be recovered solely from proceeds of taxes.<sup>22</sup>

Redevelopment agencies are authorized to invest money,<sup>23</sup> and the test claim statute applies to all “local agencies,” defined to include any public agency.<sup>24</sup> Although a redevelopment agency may be required to comply with the test claim statute, the costs incurred by a redevelopment agency, or on behalf of a redevelopment agency, to accumulate and compile the data necessary to prepare the quarterly report of investments and to render the reports to the legislative body are not subject to the reimbursement requirement of article XIII B, section 6 of the California Constitution.

Accordingly, to the extent the City of Tustin’s reimbursement claims include costs incurred to render the quarterly report of investments for the Tustin Community Redevelopment Agency, those costs are not reimbursable.

2) Reimbursement is not required for the cost of contracted city auditors to review and audit the investment policy and quarterly reports to ensure compliance with all state laws.

The City claimed the contract service costs for eight (8) hours spent by city auditors each fiscal year to “review” and “audit the investment policy and quarterly reports to ensure compliance with all State laws.” These costs are not reimbursable.

Although the City’s investment policy requires the Tustin Audit Committee to annually review the City’s investment policy, the test claim statute does not require a local agency to audit the investment policies and quarterly reports. Nor do the parameters and guidelines and claiming instructions include this activity as a reimbursable activity.

Thus, reimbursement is not required to review and audit the investment policy and quarterly reports to ensure compliance with state law.

3) Reimbursement is not required for entering, tracking, balancing, and auditing every investment transaction.

The City contends that all costs associated with data entry of investment transactions and time to prepare and use subsidiary ledgers of investments are reimbursable. The incorrect reduction claim states the following:

The claims prepared for the City of Tustin included costs associated with the data entry of investment transactions and the time to prepare and utilize subsidiary ledgers of investments. These costs were identified as allowable activities in the Parameters and Guidelines. Use and development of these ledgers are necessary to prepare the city’s quarterly investment reports.

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<sup>21</sup> Health and Safety Code section 33610.

<sup>22</sup> *County of Fresno v. State of California* (1991) 53 Cal.3d 482, 486-487; *City of El Monte, supra*, 83 Cal.App.4th at page 280.

<sup>23</sup> Health and Safety Code section 33603.

<sup>24</sup> Government Code section 53020.

The City in its response to the draft staff analysis further argues that:

It is our opinion that recording each investment transaction is exactly what is meant by “accumulating and compiling data.” It is a putting together or gathering investment data so that conclusions can be inferred. It did not say “photocopying pre-existing third party reports and investment statements at the end of each quarter and presenting this to the governing body.” It appears that this is what the Commission staff is recommending.

Our claims requested approximately \$5,000 per year of staff salary and benefits per year for these activities relating to the preparation of the quarterly reports. We don’t believe this was excessive or unreasonable. By disallowing the cost of entering all investment transactions (the purchase and sale of investments, recording of interest, etc.) the report becomes a meaningless, potentially inaccurate document solely comprised of second hand information that has not been properly reviewed or verified. We do not believe that this was the intent of the legislation. The Treasurer of each jurisdiction must certify the accuracy of the investment report and data it contains to his or her governing body. Asking them to present and sign off on a compilation of unchecked, photocopied, second hand reports is not reasonable or responsible.

Thus, the City has included the following activities in its reimbursement claims:

Senior account clerks -

- Enter data into investment tracking system (for every transaction).
- Balance subsidiary ledgers required for the preparation of the quarterly investment report.
- Accumulate and balance investment data and balance “them to those reports submitted to their Bank or ‘Safekeeping Agent’.”
- Enter data into investment spreadsheets to monitor principal and interest earnings for each investment as required by state statute.

Assistant finance director -

- Review and ensure the information in the subsidiary ledgers is accurate.
- Supervise, audits, and internal control procedures.

These activities are consistent with City’s local investment policy, and they may be reasonable and responsible as argued by the claimant. The local policy requires that *every* investment transaction be reviewed, authorized and documented. In addition, the policy states that the City strives to maintain the level of investment of all funds at 100 percent if possible, through daily and projected cash flow determinations.

These activities, however, are overly broad and go beyond the scope of the state mandate. Entering, tracking, balancing, and auditing every investment transaction to comply with the local investment plan is not reimbursable.

Government Code section 53646, subdivision (b), requires the treasurer or chief financial officer to prepare and render a quarterly report within 30 days following the end of the quarter. The

report shall include the investments and money held by the local agency. With respect to securities held by the local agency under the management of an outside party that is not the local agency or the State of California Local Agency Investment Fund, the report shall include a current market value as of the date of the report. This statutory language is different than former Government Code section 53646 enacted in 1984, that sunsetted in 1991, which required monthly reports of investments and a *detailed monthly report of transactions* involving repurchase and reverse purchase agreements. Although a detailed “report of transactions” for the reporting period was required by the 1984 statute, it is not required by the test claim statutes. The mandate here is to report on *investments held* at the end of the reporting period. When different words and phrases are used by the Legislature in the same statutory scheme, it is presumed the Legislature intended a different result.<sup>25</sup>

Further, the Commission expressly denied the request for reimbursement for the daily activity of maintaining subsidiary ledgers when it adopted the parameters and guidelines in November 1997.<sup>26</sup> As reflected in the analysis adopted by the Commission, the claimant requested reimbursement for:

Subsidiary ledger of investments – cost to input transactions of various reports to be included in the investment report. Costs to reconcile the subsidiary ledger to the control accounts, cost to update any subsidiary ledger and make necessary adjustments discovered during reconciliation process, and cost to adjust the subsidiary ledger to market value.

The Commission denied these activities and adopted the following finding:

There is disagreement on the issue of whether local entities are entitled to reimbursement for use of “subsidiary ledgers of investments.” Government Code section 53646, subdivision (b)(4), states: “In the quarterly report, a subsidiary ledger may be used in accordance with accepted accounting practices.” The Department of Finance recommended deletion of claimant’s proposed language regarding subsidiary ledgers. Government Code section 53646, subdivision (b)(4) authorizes but does not require the use of subsidiary ledgers. Therefore, it is not a mandated activity. However, staff concludes that if “subsidiary ledgers” are necessary to “accumulate and compile data necessary to prepare the quarterly report of investments” under section 53646, subdivision (b)(1), (2), and (3), and/or subdivision (e), it is reimbursable.<sup>27</sup>

Furthermore, when the Commission addressed the request to amend the parameters and guidelines in 2003, the Commission considered and denied arguments that daily investment

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<sup>25</sup> *Briggs v. Eden Council for Hope and Opportunity* (1999) 19 Cal.4th 1106, 1117.

<sup>26</sup> See staff analysis for Item 3, Proposed Parameters and Guidelines, adopted by the Commission on November 20, 1997.

<sup>27</sup> See also, transcript of the November 20, 1997 Commission hearing, Exhibit G, pages 856-857, where the Commission’s former Chief Legal Counsel explained that if a subsidiary ledger is necessary to accumulate and compile data necessary for the report of investment, it would be “subsumed” within the reimbursable activity to accumulate and compile the data, and would not stand on its own as a reimbursable activity.

monitoring and investment compliance activities are “necessary” in order to make the statements required by the test claim statute to be included in the investment report that the portfolio is in compliance with the statement of investment policy, or the manner in which the portfolio is not in compliance, and denoting the ability of the local agency to meet its pool's expenditure requirements for the next six months, or provide an explanation as to why sufficient money shall, or may not be available. The Commission, however, clarified the mandated activities with respect to required statements as follows:

Determining if, *on the last day of each quarter*, the portfolio complies with the statement of investment policy, and providing an explanation if the portfolio does not comply. (Gov. Code, § 53646, subd. (b)(2).)

Compiling the cash flow information necessary to provide a statement, and any required explanation, denoting the local agency's ability to meet its pool's expenditure requirements for the next six months. Cash flow information needed to provide this statement includes forecasted expenditure requirements and non-investment revenue, plus investment revenue anticipated from securities *held at the end of the quarter*. (Gov. Code, § 53646, subd. (b)(3).)

The Commission also clarified that the following activities are *not* reimbursable:

- a. Duplicate entry of investment transactions (type of investment and issuer, date of maturity, and par and dollar amount invested) into custodian bank records or other databases.
- b. Producing and presenting reports of transactions related to securities not held at the end of the quarter.
- c. Determining if investment transactions related to securities not held at the end of the quarter comply with the investment policy.

As indicated above, the Commission's clarification of existing law may be applied to reimbursement claims for costs that predate the parameters and guidelines amendment. The Commission's clarification is merely a statement of what the law has always been.<sup>28</sup>

Finally, these legal conclusions are supported by the report prepared by Conny Jamison, the consultant retained by the Commission for the incorrect reduction claim filed by the County of Los Angeles, and relied upon by the City in this claim.<sup>29</sup> Ms. Jamison's report states in relevant part the following:

The County should be reimbursed for the costs of ascertaining whether their portfolio is in compliance with its investment policy, which the Treasurer is required to affirm under Section 53646. I do not believe, however, that they should be reimbursed for the cost of ascertaining whether *every transaction* is in compliance with their policy. While such care may be both prudent and

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<sup>28</sup> *McClung v. Employment Development Dept.* (2004) 34 Cal.4th 467, 471, quoting *Western Security Bank v. Superior Court* (1997) 15 Cal.4th 232, 243; *Riley v. Hilton Hotels Corp.* (2002) 100 Cal.App.4th 599, 603.

<sup>29</sup> In this respect, the Commission disagrees with the claimant's interpretation of Ms. Jamison's report.

conservative, Government Code Section 53646 (b)(2) requires only that, “The quarterly report shall state compliance of the portfolio to the statement of investment policy ...”

It is my opinion that the use of the words “portfolio” in conjunction with “the quarterly report” implies that the statement refers simply to the portfolio which accompanies the report, which is the portfolio as of the last day of the reporting period. This is a standard convention in the industry, and even Los Angeles county does not include 20+ separate portfolios (one for each day of the month) with its monthly report. I do not agree with the County’s position that the statement of compliance of CGC Section 53646 applies to every transaction during the reporting period.”

Accordingly, the following activities performed by the senior account clerks and assistant finance director, as identified in the reimbursement claims are *not* reimbursable:

- Enter data into investment tracking system for *every* transaction.
- Balance subsidiary ledgers required for the preparation of the quarterly investment report.
- Accumulate and balance investment data and balance “them to those reports submitted to their Bank or ‘Safekeeping Agent’.”
- Enter data into investment spreadsheets to monitor principal and interest earnings for each investment as required by state statute.
- Review and ensure the information in the subsidiary ledgers is accurate.
- Supervise, audits, and internal control procedures.

### **C. Reinstatement of costs for salaries and benefits**

Pursuant to section 1185.7 of the Commission’s regulations, if the Commission determines that a reimbursement claim has been incorrectly reduced, the Commission is required to send the Statement of Decision on the incorrect reduction claim to the State Controller’s Office and request that the costs in the claim be reinstated.

In this case, the Commission finds that the State Controller’s Office incorrectly reduced to \$0 the reimbursement claims for salaries and benefits of the senior account clerks and the assistant finance director with respect to the quarterly report of investments. However, the reimbursement claims include activities and costs that are not reimbursable. Thus, not all the costs claimed by the City for salaries and benefits are reimbursable and can be reinstated.

The costs that should be reinstated to the City are identified in the amendment to the parameters and guidelines that clarified the reimbursable activities for the *Investment Reports* program as follows:

- a. For each investment that is held on the last day of each quarter and included in a quarterly report of investments, the following activities are eligible for reimbursement:
  1. One-time data entry into investment reporting application or software:
    - the type of investment and issuer,

- date of maturity, and
  - par and dollar amount invested.
2. Providing a description of any of the local agency's funds, investments or programs, including lending programs that are under the management of contracted parties.
  3. Obtaining and reporting current market value as of the date of the quarterly report, and reporting the source of this valuation for all investments held by the local agency and under management of any outside party that is not also a local agency or the State of California Local Agency Investment Fund.
  4. Providing required copies of the most recent statement(s) received by a local agency from the Local Agency Investment Fund, the Federal Deposit Insurance Corporation-insured accounts in a bank or savings and loan association, a county investment pool, or any combination of these. [Unit Cost Per Page.]
  5. Determining if, on the last day of each quarter, the portfolio complies with the statement of investment policy, and providing an explanation if the portfolio does not comply. (Gov. Code, § 53646, subd. (b) (2).)
- b. Compiling the cash flow information necessary to provide a statement, and any required explanation, denoting the local agency's ability to meet its pool's expenditure requirements for the next six months. Cash flow information needed to provide this statement includes forecasted expenditure requirements and non-investment revenue, plus investment revenue anticipated from securities held at the end of the quarter (Gov. Code, § 53636, subd. (b)(3)).

The City's claims indicate that the senior account clerks and the assistant finance director worked on the quarterly report of investments. However, it cannot be determined from the claims how long it took those employees to perform the reimbursable activities. Thus, staff recommends that the Commission remand the reimbursement claims back to the State Controller's Office to further review the City's claims for the costs of the salaries and benefits of the senior account clerks and assistant finance director to perform the reimbursable activities required to render the quarterly report of investments and, in accordance with the Commission's decision on this incorrect reduction claim, to reinstate the costs that are eligible for reimbursement. Pursuant to Section VII of the parameters and guidelines, all costs claimed by the City shall be traceable to source documents (e.g., employee time records, invoices, receipts, purchase orders, contracts, worksheets, calendars, declarations, etc.) that show evidence of the validity of such costs and their relationship to the mandate. All documentation in support of claimed costs shall be made available to the State Controller as may be requested.

### **CONCLUSION**

For the foregoing reasons, the Commission concludes that the State Controller's Office incorrectly reduced the costs claimed by the City of Tustin in their reimbursement claims filed for the *Investment Reports* program for fiscal years 1995-1996, 1996-1997, 1997-1998, and 1998-1999.

The City's reimbursement claims for fiscal years 1995-1996, 1996-1997, 1997-1998, and 1998-1999 are hereby remanded back to the State Controller's Office for further review and



reinstatement of those costs that are eligible for reimbursement in accordance with the Commission's decision on this incorrect reduction claim. Pursuant to Section VII of the parameters and guidelines, all costs claimed by the County shall be traceable to source documents (e.g., employee time records, invoices, receipts, purchase orders, contracts, worksheets, calendars, declarations, etc.) that show evidence of the validity of such costs and their relationship to the mandate. All documentation in support of claimed costs shall be made available to the State Controller as may be requested.