

# California Air Resources Board

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## Legacy Supplemental Environmental Projects Performance Audit



**February 2019**





February 15, 2019

Richard Corey  
Executive Officer  
California Air Resources Board  
1001 I St  
Sacramento, CA 95814

Dear Mr. Corey:

Enclosed is our report entitled 'Legacy Supplemental Environmental Projects Performance Audit.' This report was prepared on behalf of the California Air Resources Board (CARB) by Sjoberg Evashenk Consulting and includes our findings and observations. As it relates to CARB's legacy SEPs, our report addresses opportunities for achieving efficiency, improving effectiveness, and ensuring SEP Administrators and funding recipients were following appropriate agreements and guidelines. A draft report was discussed with program management on November 26, 2018 and management comments received were considered in drafting the final report.

Sjoberg Evashenk Consulting was pleased to work with the CARB on this important project.

Respectfully submitted,

A handwritten signature in blue ink, appearing to read "Lynda McCallum", is written over the text "Respectfully submitted,".

Lynda McCallum, Partner

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February 8, 2019

Ms. Lynda McCallum, Partner  
Sjoberg Evashenk Consulting, Inc.  
455 Capitol Mall, Suite 700  
Sacramento, California 95814

RE: Response to California Air Resources Board "Supplemental Environmental Projects Performance Audit"

Dear Ms. McCallum:

Thank you for completing the audit of the California Air Resources Board's (CARB) legacy supplemental environmental projects (SEP) as requested by CARB and in accordance with CARB's contract #17ED006. As you know, per our direction, the audit focused on three long-standing SEPs that CARB is in the process of closing and that were implemented prior to a new SEP program initiated in June 2017. The purpose for the audit was to assess whether funds allocated to these three long-standing SEPs were spent appropriately and to review accounting and project management procedures to develop lessons learned to apply to the updated SEP program.

Overall, the audit found that while program expenses appear to be consistent with the program objectives, CARB had not established an adequate and consistent system of controls necessary to hold recipients accountable for program implementation, especially in SEPs managed by the Enforcement Division (ED). These findings are important and are being addressed.

In June 2017, CARB halted additional payments, and began the process to close out the three long-standing SEPs that were the focus of the audit: the California Council for Diesel Education and Training, the Small Engine, and the School Bus SEP. During the same period, CARB implemented the new SEP program that was considered by the CARB board at a public hearing. Many of the procedures put into effect in the new SEP program address audit findings associated with the older program.

In the new program, CARB solicits project proposals, requiring a complete scope of work, budget, and implementation timelines. CARB also established internal

procedures for the selection of SEPs as eligible for funding, for the management and tracking of SEPs throughout funding and implementation, and for the guidance for SEP Administrators and funding recipients receiving, disbursing, transferring, or expending SEP funds. Each SEP defines clear goals, and a framework to measure outcomes and performance in meeting those goals. Further, SEPs that are approved for funding are posted on CARB's webpage to provide transparency for the public. In October 2018, CARB established a process to maintain a central and comprehensive universe of settlement agreement information and a process to periodically perform site visits to SEP administrators and funding recipients to spot check and inspect SEP activities.

Thus, CARB has already acted on several of the audit recommendations. However, other recommendations will take longer to address. Staff is developing a designed a schedule to implement each of these recommendations.

The audit proposes CARB establish new broad programmatic goals for the SEP program, and that staff track metrics to determine how these goals are being addressed over time. These goals are under development, and aim to reduce emissions, in support of CARB's mission to improve air quality. Examples of projects selected thus far for the SEP program include air filtration systems in schools, mobile asthma outreach to provide treatment to school age children and to educate impacted families, education on vehicle idling requirement in communities including no idling signs, and other projects that community members have developed to achieve air quality benefits and education.

The audit recommends staff implement improved procedures that will allow us to better track payments to, and expenditures from, each SEP. In response, staff is implementing new accounting procedures to address this recommendation; new processes should be fully implemented within the next several months.

The audit also calls for more formalized agreements between each SEP recipient and CARB. New legal templates, contractual requirements, and guidance will be developed and implemented over the next six months. New SEP recipients will be held to these higher standards going forward.

The attached matrix is a response to the audit findings and recommendations. The matrix outlines the findings and recommendations that have been addressed as well as timelines for CARBs next steps.

Ms. Lynda McCallum, Partner

February 8, 2019

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Thank you again for your diligent and comprehensive audit of our legacy SEP program. We appreciate your efforts to help us to identify areas for improvement and to establish a robust, effective program. Should you have any questions, please contact me at (916) 322-7077 or via email at [richard.corey@arb.ca.gov](mailto:richard.corey@arb.ca.gov).

Sincerely,



Richard Corey  
Executive Officer  
California Air Resources Board

Attachment

ED SEP Audit Recommendation Response Matrix

Number	Condition and/or Auditor's Expectations to Close Recommendation	Finding Corrective Action Plan/Actions Taken	Implementation Date
<b>Finding 1.1</b> <i>CARB's Legacy Supplemental Environmental Projects Program Lacked Adequate System of Controls to Ensure Proper Collection and Spending of Program Monies (pg.6)</i>			
1	The SEP program operated largely without the formal agreements, policies, procedures, processes and protocols necessary to hold program participants accountable for ensuring program monies were spent appropriately and in a manner that efficiently achieved program objectives. A strong system of controls for the SEP program was particularly important since SEP funding largely by-passed CARB and was paid directly to program administrators by responsible parties.	In the process developed in response to AB 1071 CARB maintains the responsibility of providing project oversight while and the violator funds the projects. Once the project is funded, CARB as the SEP funding administrator, ensures that the project milestones are met and all expenditures are funded according to the budget and timeline of the SEP project.	January-17
2	Reduce the individual handling of SEP payments associated with settlement agreements within CARB by establishing a consistent, coordinated, and centralized process for responsible parties to submit SEP funds, such as requiring all responsible parties to send SEP payments directly to SEP administrators and eliminating the ability for responsible parties to submit some SEP payments (e.g. wire transfers) to ASD for processing, handling, and forwarding. <b>(Recommendation #2)</b>	CARB ED has developed a centralized process to track all SEP payments. The violator send the SEP payments directly to the SEP recipient. After the SEP Recipient receives the payment they send CARD ED a copy of the payment and a signee payment acknowledgement form.	January-18
3	Establish a process for ED to track both SEP and non-SEP payments made by responsible parties associated with all settlement agreements and follow-up on settlement agreements with past due amounts to investigate the responsible party's adherence to the settlement agreement terms to ensure corrective actions have taken place and all required amounts remitted. <b>(Recommendation #3)</b>	ED has initiated a process with CARB's ASD to track penalties associated with settlement agreements.	Will be complete by Spring 2019
<b>Finding 1.2</b> <i>Supplemental Environmental Projects Guidance and Code Do Not Specifically Address Responsibilities Related to Administering SEP Funding. (pg.7)</i>			
4	In the absence of mandated administrative directives, there is an increased importance on the agency to fully develop the program to include appropriate guidance and controls to ensure funds are collected, spent appropriately, and performance measured.	Management of the SEP program was consolidated under a centralized team within ED, with assigned roles and responsibilities, to coordinate SEP program efforts across the Division and with other divisions. This also included development of program guidance and assistance to SEP recipients that includes recordkeeping and reporting requirements.	January-17
<b>Finding 1.3</b> <i>CARB's Settlement Penalty Payment Tracking Processes Were Not Centralized, Comprehensive, or Consistent (pg.7)</i>			
5	Establish within the Enforcement Division (ED) a process to maintain a central and comprehensive universe of settlement agreement information. Specifically, designate a single point of contact where all settlement agreements executed are immediately sent and key information, such as total settlement amounts, amounts designated to SEPs, dates paid, etc., is entered into a tracking mechanism, such as an electronic spreadsheet or database. <b>(Recommendation #1)</b>	The ED administrative team now tracks all information about SEPs approved for funding, funded, payments, project expenditures, project progress, through completion, for all SEPs selected by violators. SEP recipients are also required to provide monthly or quarterly project reports that detail the expenditures and progress.	December-18
	To compile a centralized universe of the total monies designated to each of the three SEPs as part of the many settlement agreements processed and the amounts paid by responsible parties, one would have had to combine information from multiple databases, individual investigators, ASD records, and SEP Administrator records.	The funding of the three legacy SEP programs was discontinued in June 2017. CARB ED is reconciling the remaining funds to ensure that they have been spent or recovered for the APCF. After reconciling the funds, an exit summary will be written to recap whether the project goals were met for each SEP, and how it supported the broader CARB SEP program goals.	Will be complete by the end of 2019
6	Work with ASD on tracking CARB's portion of penalties associated with settlement agreements. <b>(Recommendation #2)</b>	ED has initiated a process with CARB's ASD to track penalties associated with settlement agreements.	September-18

Number	Condition and/or Auditor's Expectations to Close Recommendation	Finding Corrective Action Plan/Actions Taken	Implementation Date
<b>Finding 1.4 Adequate Agreements were not Always in Place to Ensure SEP Funds were Used Properly and Projects Met CARB Expectations. (pg.10)</b>			
7	Move away from funding on-going programs to a merit-based approach that provides funding to applicants for projects with defined scopes, discrete goals, and timelines for implementation. <b>(Recommendation #4 can also apply to Finding 1.6)</b>	CARB has instituted a merit-based SEP funding process, to support projects with discrete timelines and benchmarks, a project budget, and clear goals and objectives, that are pre-approved to receive funding, and for which a clear agreement exists between the violator and SEP recipients, and for which both parties sign.	January-17
8	Establish sufficient and formal agreements with each SEP administrator or with a single SEP administrator acting as a "clearinghouse" for all other SEPs. Agreements should contain adequate and formally agreed-upon provisions that protect CARB's interests, and ensure compliance with all applicable laws, regulations, rules, and best practices. Provisions should define expectations, roles, responsibilities, duties, and authorities and describe requirements related to project activities, schedules, funding disbursements, appropriate use rules, recordkeeping, project close-out, performance measuring and regular reporting of program achievements and outcomes. Agreements should also state when SEP administrators are required to enter into agreements with third-parties, such as when funding is disbursed to colleges or school districts, to ensure all program participants adhere to CARB's rules and expectations. <b>(Recommendation #5)</b>	CARB is acting as an administrator with respect to approving projects, ensuring projects are meeting their goals, and accounting for the proper expenditure of the funds. CARB has implemented a contract that the violator and the SEP recipient also sign, that provides the mechanism for recovering the funds in the event that the project cannot be completed or deviates from the approved plan. CARB is researching additional ways to strengthen this contract language. ED will be working with CARB's Office of Legal Affairs to add the recommended provisions to the contract language.	<i>Research ongoing. Date to be determined.</i>
	Agreements must contain a number of basic provisions that should be formally agreed upon in order to adequately protect CARB's interests, ensure compliance with all applicable laws, regulations, rules, and best practices, and measure performance of the program. Without adequate and formal agreements describing responsibilities and expectations. <b>(Pg.12)</b>	ED will be working with CARB's Office of Legal Affairs to add the recommended provisions to the contract language.	<i>Research ongoing. Date to be determined.</i>
<b>Finding 1.5 General Lack of Internal and External Policies and Procedures to Guide SEP Program Activities and Processes. (pg.12)</b>			
9	Establish comprehensive program guidance for SEP Administrators and program recipients in regards to receiving, disbursing, transferring, or expending SEP funds, including, but not limited to, general purchasing guidelines, such as requirements for appropriate use of SEP funds, competitive solicitations, thresholds for purchase approval, invoicing and expenditure supporting documentation, and management and disposal of capital assets purchased with SEP funds; timeliness of utilizing program funds and holding program funding in interest bearing accounts; and recordkeeping, performance measurement, project close-out, and regular status reporting of program information, outcomes, and achievements. <b>(Recommendations #7)</b>	ED will be working with CARB's Administrative Service Division and Office of Legal Affairs to add the recommended provisions to the contract language.	<i>Research ongoing. Date to be determined.</i>
<b>Finding 1.6 CARB Lacked Sufficient Management Oversight of SEP Program Processes and Performance (pg.13)</b>			
10	1. Establish within the Enforcement Division (ED) a process to maintain a central and comprehensive universe of settlement agreement information. Specifically, designate a single point of contact where all settlement agreements executed are immediately sent and key information, such as total settlement amounts, amounts designated to SEPs, dates paid, etc., is entered into a tracking mechanism, such as an electronic spreadsheet or database. <b>(Recommendation #1)</b>	See response #5.	January-18



ED SEP Audit Recommendation Response Matrix

Number	Condition and/or Auditor's Expectations to Close Recommendation	Finding Corrective Action Plan/Actions Taken	Implementation Date
11	Establish SEP-specific program goals as well as a framework to measure program outcomes and performance in meeting those goals. Consistent with AB 1071, program goals should provide a connection between a specific SEP project and an environmentally impacted community. To measure program performance, CARB should establish specific performance targets in the agreement and require SEP administrators to periodically report on ongoing progress in meeting those targets. <b>(Recommendation #8)</b>	CARB is in the process of updating the program and project goals to include measurable program outcomes. Currently, SEPs must meet the guidelines established within CARB's current policy, which reflects the criteria set forth in AB 1071 for SEP programs. In addition to the current policies, the individual projects have specific performance targets or goals that must be met. Depending on the scope of the project, CARB receives either monthly or quarterly project reports.	To be Complete by Spring 2019.
12	Establish a comprehensive set of internal policies and procedures that outline the roles and responsibilities of CARB management and staff involved in the SEP process. A comprehensive set of policies and procedures should include, but is not limited to, tracking SEP amounts owed from and paid by responsible parties and following up on collections or late payments; communicating funding expectations to recipients, ensuring program expenditures are reviewed for appropriateness; monitoring program performance by formally reviewing and approving regular SEP performance and outcomes reporting and providing feedback to program participants, including additional guidance on program management and administration; and developing formal project-close out processes. <b>(Recommendation #6)</b>	CARB is tracking SEP amounts paid for by responsible parties.  ED communicates with SEP recipients throughout the project selection process, all the way through project completion. ED also has posted SEP Settlement Agreement process detailing internal procedures. ED further requires the SEP recipient to sign a contract detailing the conditions under which CARB would recover the unused project funds in the event that the project cannot be completed or deviates from the approved plan, and the mechanisms for doing so.  <i>See responses #1 and 4 for additional info</i>	January-17
<b>Finding 2 Lack of Supporting Documentation Hampered Efforts to Evaluate Receipt and Use of SEP Funds (pg.16)</b>			
13	Establish comprehensive program guidance for SEP Administrators and program recipients in regards to receiving, disbursing, transferring, or expending SEP funds, including, but not limited to, general purchasing guidelines, such as requirements for appropriate use of SEP funds, competitive solicitations, thresholds for purchase approval, invoicing and expenditure supporting documentation, and management and disposal of capital assets purchased with SEP funds; timeliness of utilizing program funds and holding program funding in interest bearing accounts; and recordkeeping, performance measurement, project close-out, and regular status reporting of program information, outcomes, and achievements. <b>(Recommendation #7)</b>	In response to SEP recipients' requests for guidance for project funding and expenditure tracking, ED is in the process of developing a comprehensive guidance document for SEP recipients.  <i>See responses #2, 4, and 5 for further info.</i>	September-18
14	Establish a process to periodically perform site visits to SEP administrators and funding recipients to spot check and inspect SEP activities, including verifying large equipment purchased with SEP funds are adequately secured, stored, and maintained, and to ensure the program activities are consistent with progress reporting. <b>(Recommendation #9)</b>	CARB has already implemented a process to go onsite and verify the reporting that has been performed by SEP recipients.	January-17

# Executive Summary

**Audit Purpose:** The California Air Resources Board (CARB) engaged Sjoberg Evashenk Consulting, Inc. to conduct a performance audit of three long standing Supplemental Environmental Projects (SEP) and develop recommendations for improvement. The audit objectives set forth by CARB were to identify opportunities for achieving efficiency, improving effectiveness, and ensuring SEP Administrators and funding recipients were following appropriate agreements, guidelines, and fiscal/accounting standards.

## OVERALL RESULTS—CHAPTER 1

CARB provided funding to three SEPs through the settlement agreement over the last decade, ending in June 2017:

- California Council on Diesel Education and Technology
- School Bus and Diesel Emission Reduction
- Small Engine Maintenance & Repair Courses

Overall, our review of available information found that program expenses generally appeared to be related to the intent of the three SEPs, but CARB's Enforcement Division (ED) had not implemented an adequate and consistent system of controls necessary to hold funding recipients accountable for utilizing SEP funds appropriately. This issue is of particular concern because responsible parties directly paid external SEP administrators.

Specifically, the audit found that ED had not implemented coordinated and centralized processes to ensure that responsible parties submitted the agreed-upon funding to the SEPs and did not always ensure adequate agreements in place to establish the necessary compliance criteria to hold program participants accountable to specific responsibilities and expectations associated with receiving and utilizing SEP funding; however, CARB did establish a formal agreement with the School Bus SEP. Additionally, although ED provided staff with guidance related to soliciting and approving the appropriate types of SEPs, it did not provide formal written SEP-specific guidance to staff carrying out SEP activities to ensure necessary processes were employed and executed consistently and did not have corresponding regular and routine management review and approval processes of staff SEP activities. There was also an overall lack of formal guidance provided to the external SEP funding recipients to ensure CARB's expectations were met; however, CARB did provide program guidance to the School Bus SEP. CARB did not have processes, metrics, and methods in place to effectively evaluate SEP performance to ensure SEP-specific goals were achieved.

Further, due to the general lack of SEP adequate agreements, guidance, and compliance criteria, particularly with two SEPs, our analysis focused on understanding the amount of funding provided to the SEPs, the types of program expenses incurred, and whether expenses reasonably related to the intent of the SEPs. The audit found that the records of CARB and program participants did not always agree related to the amounts of SEP funding disbursed and received. Also, while two of the SEPs provided insufficient expenditure information to demonstrate that all activity was included for review, our analysis of available information found that program expenses appeared generally related to the intent of the two SEPs and were reasonably supported with just a few exceptions. We found no issues with expenditure information provided by the School Bus SEP. Also, the audit found the timeliness of utilizing SEP funding after receipt appeared reasonable.

## RECOMMENDATIONS—CHAPTER 2

As the three SEPs reviewed are completed or nearing completion, we offer 9 recommendations for CARB's overall SEP program and future SEPs, including the following five key recommendations summarized below:

- Establish a process to maintain a central and comprehensive universe of settlement agreement information.
- Reduce the individual handling of SEP payments associated with settlement agreements within CARB by establishing a consistent, coordinated, and centralized process for responsible parties to submit SEP funds.
- Establish sufficient and formal agreements with each SEP administrator or with a single SEP administrator acting as a "clearinghouse" for all other SEPs.
- Establish a comprehensive set of internal procedures that outline the roles and responsibilities of CARB management and staff involved in the SEP process.
- Establish comprehensive program guidance for SEP Administrators and funding recipients receiving, disbursing, transferring, or expending SEP funds.

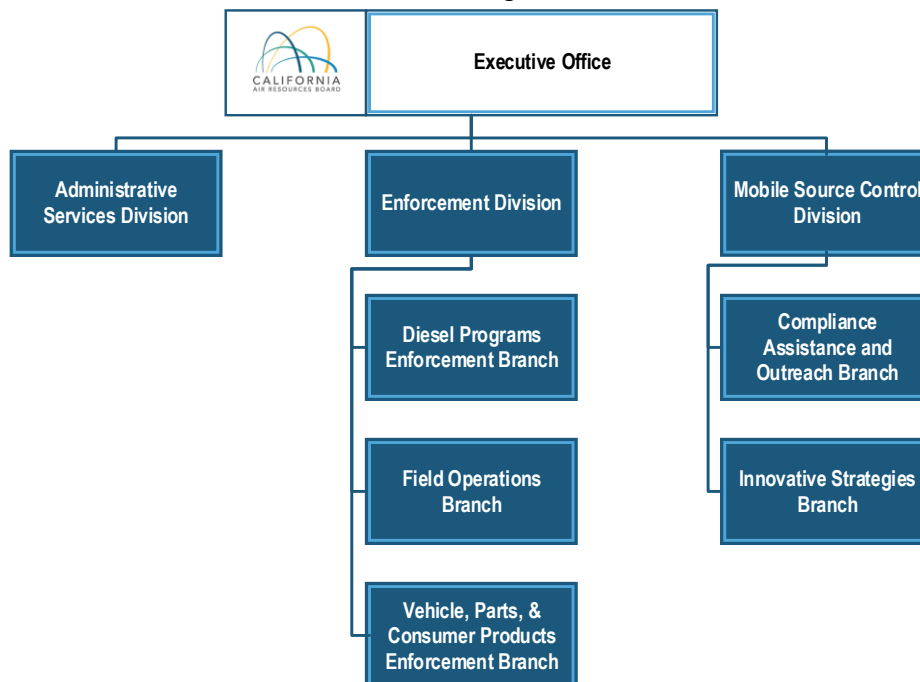
## Introduction and Background

The California Air Resources Board (CARB) is responsible for coordinating the State's efforts to achieve mandated and adopted air quality standards. These standards are generally intended to protect the public from air pollution and to address climate change. CARB's Enforcement Division helps achieve State air quality goals by identifying violations, taking enforcement action against a responsible party, and assessing monetary penalties. As part of the settlement agreement process, a responsible party can offset a portion of the penalty by either undertaking a Supplemental Environmental Project (SEP) or by donating funds to an existing SEP with the remainder of the assessment paid to CARB's Air Pollution Control Fund. SEPs are environmental beneficial projects intended to play a role in securing additional environmental and health protection such as emission reduction incentive programs and public education projects. Prior to 2017, there were three SEPs that responsible parties could designate to offset a portion of their penalty:

- California Council on Diesel Education and Technology (CCDET) SEP
- School Bus and Diesel Emission Reduction (School Bus) SEP
- Small Engine Maintenance & Repair Courses (Small Engine) SEP

In addition to staff in the Enforcement Division, two other CARB divisions are involved in SEP processes, as reflected in Exhibit 1—the Administrative Services Division administers CARB's portion of SEP payments made by responsible parties and the Mobile Source Control Division (MSCD) acts as the point of contact for the School Bus SEP.

**Exhibit 1. CARB Divisions Involved with the SEP Program**



## Scope and Methodology

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The California Air Resources Board (CARB) engaged Sjoberg Evashenk Consulting, Inc. to conduct a performance audit of three long-standing Supplemental Environmental Projects (SEP) and develop recommendations for improvement.

### Audit Objectives

The specific audit objectives set forth by CARB were to identify opportunities for achieving efficiency, improving effectiveness, and ensuring SEP Administrators and funding recipients were following appropriate agreements, guidelines, and fiscal/accounting standards.

### Audit Scope, Exclusions, and Limitations

The scope of the audit included reviewing the following three SEPs:

- California Council on Diesel Education and Technology (CCDET) SEP
- School Bus and Diesel Emission Reduction (School Bus) SEP
- Small Engine Maintenance & Repair Courses (Small Engine) SEP

The scope specifically excluded reviewing anything other than the three SEPs noted above, including more recently established SEPs and any associated processes or any other CARB programs.

The audit period included activity between January 2014 and December 2017.

We were provided revenue and expenditure reports for the entire audit period for the School Bus SEP. However, as a result of data limitations, we were not provided records and supporting documentation covering all revenue and expenditure activity for the period January 1, 2014, to December 31, 2017 for the CCDET and Small Engine SEPs, impacting the overall reliability and validity of information and limiting our ability to determine how funding was utilized. Specifically, we did not have access to a variety of key financial-related records and reports from two SEP Administrators and several program recipients because auditees were not contractually required to document program activities or retain records and many of the systems used to support program activities were no longer operational. Further, many of the recipients experienced turnover of key staff, resulting in a lack of historical knowledge of program operations. Although the two SEPs provided some revenue and expenditure records and reports, we found varying deficiencies related to the accuracy and completeness of the data made available to us, including:

- Revenue and expenditure activity for the period January 2014 through June 2014 was not included (CCDET SEP and Small Engine SEP).

- Expenditure and revenue records provided were not system generated reports, but rather manually created Excel tracking files and some information provided was not useful because it was commingled with the activity of other programs (CCDET SEP).

Audit fieldwork began in February 2018 and was completed in August 2018.

## **Audit Methodology**

To meet the audit objectives detailed above, we performed the following:

- Interviewed CARB management and staff in the Enforcement Division and Mobile Source Control Division involved in CARB's internal SEP processes and well as key SEP Administrator personnel for each of the three SEPs.
- Reviewed regulations and available agreements, guidance, policies and procedures, and financial/accounting and tracking records and reports related to program oversight and management, funding use, records retention, required reporting, project outputs and outcomes.
- Performed site visits at five of the six CCDET recipient colleges and conducted visual observations of large equipment purchased with SEP funding. We visited the American River College, Delta College, Los Angeles Trade Tech College, College of Alameda, and Santa Ana College.
- Compiled a universe of settlement agreements designating portions of penalties to the three SEPs and compared amounts obligated to amounts received and disbursed.
- Performed detailed expenditure testing for each of the three SEPs to determine whether the expenditures complied with rules and agreements (where applicable), appeared reasonable and linked to the intent of the SEP, was supported with adequate documentation, and reflected the use of best practices.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## Chapter 1—Audit Findings

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The California Air Resources Board (CARB) coordinates the state’s efforts to achieve and maintain health-based federal and state air quality standards. As part of its authority, CARB’s enforcement program includes the ability to issue citations, impose administrative penalties, refer cases to prosecutors for civil and criminal prosecution, and to settle cases with responsible parties (individuals or companies) that violate CARB’s rules and regulations. As a condition of a settlement agreement, CARB requires the responsible party to achieve and maintain compliance with air quality laws and regulations and to pay a monetary civil penalty. Between 2007 and 2017 CARB allowed responsible parties to satisfy part of the monetary penalty by offsetting a portion of their civil penalty by funding one of three approved Supplemental Environmental Projects (SEP):

- **California Council on Diesel Education and Technology (CCDET) SEP:** established in 2007 to improve diesel technology programs at six participating California community colleges. A focus of the funds was intended to work towards the reduction of emissions from heavy-duty diesel vehicles by providing training to fleet owners and diesel technician—such as on compliance with CARB requirements on smoke opacity emissions testing. The SEP Administrator for the CCDET SEP was Peralta College Foundation.
- **School Bus and Diesel Emission Reduction (School Bus) SEP:** established in 2011 to help public school districts and non-profit organizations to retrofit school buses in order meet updated emissions regulations. In addition to bus retrofits, funds were available for new bus purchases and filter replacements for school districts that submitted grant applications for funding. The SEP Administrator for the School Bus SEP was the San Joaquin Valley Air Pollution Control District.
- **Small Engine Maintenance & Repair Courses (Small Engine) SEP:** established in 2014 to fund emissions-controlled maintenance and repair courses at California community colleges. The purpose of funds included purchasing new equipment and instructional materials and providing student scholarships in vocation training for small off-road engines, such as in power lawn mowers, leaf blowers, chainsaws, generators, and small gas-powered scooters. The SEP Administrator for the Small Engine SEP was the Foundation of California Community Colleges.

According to CARB’s Enforcement Division (ED), these SEPs were to span multiple years and intended to fund community-based projects to improve public health, reduce pollution, increase environmental compliance, and bring public awareness to neighborhoods most burdened by environmental harm. Between January 2014 and December 2017, a total of nearly \$8 million was designated to be paid to the three SEPs by responsible parties as part of settlement agreements executed during this period.

Overall, the audit has two key findings: (1) CARB’s Enforcement Division had not implemented an adequate and consistent system of internal controls to ensure responsible parties paid amounts as agreed-upon or those receiving SEP funds were accountable for expending funding appropriately, efficiently, and effectively and for achieving program goals; and (2) a general lack of sufficient processes, criteria, and data hampered

efforts to fully evaluate the receipt and use of SEP funding. We discuss each of these findings throughout Chapter 1 in the pages that follow and provide recommendations for improvement in Chapter 2.

### **Finding 1. CARB's Legacy Supplemental Environmental Projects Program Lacked an Adequate and Consistent System of Controls to Ensure Proper Collection and Spending of SEP Monies**

The “control environment” refers to the actions of the organization regarding the significance of control, which provides discipline and structure for the achievement of program objectives. The control environment is the foundation for ensuring the effectiveness of all other components of internal control within a program. Through our meetings with CARB staff in ED and Mobile Source Control Division (MSCD), SEP Administrators, and funding recipients, we found CARB's SEP program lacked an adequate and consistent system of controls, including sufficient internal and external guidance and compliance criteria. A strong system of controls for the SEP program was particularly important since SEP funding largely by-passed CARB and was paid directly to external SEP Administrators by responsible parties.

Specifically, while ED had robust settlement agreements in place with responsible parties to ensure lasting compliance with air quality laws and regulations, once monies had been paid by responsible parties to a SEP Administrator, the necessary agreements in place to adequately hold funding recipients accountable to specific responsibilities and expectations associated with receiving and utilizing SEP funding were not always in place. However, we did note that CARB established a formal agreement with the School Bus SEP that included many, but not all, basic components expected of an entity receiving SEP funding, yet, the other two SEPs lacked formal agreements entirely. Additionally, although ED provided staff with guidance related to soliciting, approving, and establishing the appropriate types of SEPs, it had not established formal written internal policies and procedures for the overall SEP program necessary to ensure SEP-specific processes and activities were employed and executed consistently by staff. Regular and routine management review and approval processes associated with the SEP-specific activities carried out by staff were also not in place. There was also an overall lack of formal guidance provided to the external SEP funding recipients to ensure CARB's expectations were met; however, CARB did provide guidance for the School Bus SEP. Lastly, CARB lacked processes, metrics, and methods to effectively evaluate SEP performance to ensure SEP-specific goals were achieved.

#### **Supplemental Environmental Projects Guidance and Code Do Not Specifically Address Responsibilities Related to Administering SEP Funding**

A SEP is an environmentally beneficial project that a person or entity subject to an enforcement action voluntarily agrees to undertake in settlement of the action and to offset a portion of a civil penalty. During much of the audit period, California Environmental Protection Agency's (CAL EPA) Recommended Guidance on SEPs dated October 2003 suggested up to 25 percent (increased to 50 percent in 2016 under PRC 71118) of the enforcement action penalty could be offset by implementing a SEP. PRC 71118 required CARB to solicit SEPs from disadvantaged communities, maintain a list of approved SEPs, and ensure SEPs have a nexus between the activities supported by the funding and regulatory enforcement responsibilities.

CAL EPA's guidance and PRC 71118 focused on processes to establish and approve SEPs and neither stipulates oversight activities to be conducted by the enforcement agency or for other parties involved in SEP administration and delivery. It appears that the guidance and code may have envisioned that only a single responsible party would be involved in a SEP and that single party would receive the benefit of the penalty offset by undertaking all aspects of the SEP from development through implementation. Under this scenario, responsible parties would remain accountable for the SEP until the project was successfully completed and met CARB's satisfaction.

However, in practice, CARB's SEP program allowed multiple parties to be involved in a SEP where many responsible parties provided SEP funds to support preexisting, ongoing projects and programs administered and implemented by others, such as colleges, foundations, air pollution control districts, and other non-state entities, instead of completing a new SEP. For example, the Lower Emission School Bus Program (LESBP) is a program approved by CARB in December 2000 to purchase new, lower-emitting school buses and retrofit existing buses with diesel particulate filters to reduce particulate emissions. In 2011, over a decade after the LESBP was established, the School Bus SEP was created to provide support to the LESB where many responsible parties offset portions of their penalties by contributing funds to the School Bus SEP. As such, once responsible parties fulfil their obligation to provide agreed-upon funding to a SEP Administrator as delineated in a settlement agreement, they are no longer responsible for the results of the ongoing SEP project, leaving a defined accountability gap in the oversight of the SEPs.

According to CARB, directives in CAL EPA's 2003 guidance limited CARB's ability to provide oversight of the activities of SEP Administrators as the memo states that "Government should not retain authority to manage or administer the SEP." However, the section of the CAL EPA guidance cited by CARB also appears to apply to SEPs where responsible parties directly undertake and manage all aspects of a single project to CARB's satisfaction in exchange for an offset to the penalty money owed, and thus, would not involve CARB managing or administering the project. The guidance goes on to state that enforcing agencies are entitled to oversee SEP implementation and suggests that it is acceptable for SEPs to make a donation to a third party, but does not provide any guidance as to how SEPs receiving donations as part of settlement agreements should be overseen to ensure the projects were implemented as required and monies were spent appropriately.

Nevertheless, it is important that sufficient processes be established to ensure appropriate oversight of entities receiving SEP monies as the result of CARB offsetting a portion of a responsible party's assessed penalty. In the absence of mandated administrative directives, there is an increased importance on the agency to fully develop the program to include appropriate SEP-specific guidance and controls to ensure SEP funds are collected and spent appropriately and projects are implemented to CARB's satisfaction.

### **CARB's Settlement Payment Tracking Processes Were Not Centralized, Comprehensive, or Consistent**

CARB's SEP program allows community-based environmental improvement SEPs to be funded to offset a portion of the penalties during settlement of enforcement actions. Although CARB's Administrative Services



Division (ASD) had processes in place to establish receivables in the financial system to track the CARB portion of settlement penalty payments paid, CARB did not have a similar process for the SEP-portion of settlement payments. Instead, it relied upon the responsible party to comply with the settlement agreement and pay SEP funds directly to the SEP Administrators. Further, there were no processes to alert the external administrators of upcoming payments nor an expectation of the external administrator to pursue collection of the assessment. Without centralized and comprehensive processes to establish receivables and track collections, CARB cannot ensure the SEP-portions of penalty payments had been paid. Such controls are necessary, particularly since these payments were generally paid directly to the SEP Administrator without assistance or oversight from CARB.

A number of conditions contributed to these weak controls. We noted that multiple investigators from several branches within ED negotiated settlement agreements with responsible parties, but, there were no centralized or consolidated processes to track amounts owed when portions of the settlement agreed-upon payments were designated to one of the three SEPs. CARB did not establish a central database to record outstanding SEP receivables or to track the receipt of these payments. Rather, investigators were aware of the payment terms negotiated on the settlement agreements where they were personally involved and the many investigators had individual tracking processes, or no processes, to follow-up to ensure the agreed-upon payments to the SEPs were made.

Further, while settlement agreements typically set forth details regarding payment processes, responsible parties often utilized inconsistent methods to make SEP settlement payments. Not only did the external administrators of the three SEPs receive payments directly from responsible parties, others also collected SEP payment and then distributed those payments to SEP Administrators, including various investigators in the ED and accounting staff within ASD, creating confusion and uncertainty if payments were appropriately credited. This also required additional handling of the payments by multiple individuals to forward the SEP payments to the external Administrators. Various payment methods by responsible parties included:

<b>Two checks, both mailed to ED Investigator</b>	One check payable to the Air Pollution Control Fund for CARB's portion of the settlement payment and a second check payable to the SEP Administrator for its portion of the settlement payment. Investigators forwarded the CARB check to ASD and sent the SEP Administrator check to the entity designated on the check.
<b>Two checks, both mailed to ASD</b>	One check payable to the Air Pollution Control Fund for CARB's portion of the settlement payment and a second check payable to one of the three SEP Administrators for the SEP portion of the settlement payment. CARB forwarded the SEP-related check to the designated entity.
<b>Two checks mailed separately, to ASD and SEP Administrator</b>	One check payable the Air Pollution Control Fund and mailed to ASD for CARB's portion of the settlement payment and a second check payable and mailed directly to the designated SEP Administrator for its portion of the settlement payment.
<b>One wire transfer for the full amount to ASD</b>	One wire for the entire settlement payment sent to CARB's Air Pollution Control Fund bank account. ASD researched the payment and settlement and wrote the designated SEP Administrator a check for its portion of the settlement payment.

While CARB established receivables for its portion of the settlement penalty payment, it was up to individual investigators to ensure collections for the SEP-portion of the payment. Additionally, processes were not in place to notify SEP Administrators when settlement agreements were executed with portions of the penalty designated to their SEP so administrators could follow-up on missing payments.

Additionally, having payments made through multiple methods without a centralized and coordinated process to track amounts owed and paid increases risk. Payments could be misplaced, not applied to the correct settlement agreement, not forwarded to the appropriate receiving entity, or not paid at all. Such weaknesses reduces CARB's ability to hold responsible parties accountable to payment obligations and to ensure each of the three SEP Administrators received all of the payments received that were designated to the project. We noted just a few examples, including:

- \$1,500 check was sent to the School Bus SEP Administrator, but should have been sent to CCDET according to the settlement agreement.
- MSCD staff and the School Bus SEP Administrator indicated they often had to contact ASD to investigate the status of payments due to the School Bus SEP per settlement agreements—they noted that settlements were posted to the CARB website, but were not dispersed to the SEP Administrator.

As a result of the lack of consistent and coordinated processes to track the amounts designated to the three SEPs and the amounts received from responsible parties, CARB is unable hold responsible parties accountable to payment obligations and ensure SEP Administrators received all payments designated to the projects. To compile a centralized universe of the total monies designated to each of the three SEPs as part of the many settlement agreements processed and the amounts paid by responsible parties, one would have had to combine information from multiple databases, individual investigators, ASD records, and SEP Administrator records.

### **Adequate Agreements were not Always in Place to Ensure SEP Funds were Used Properly and Projects Met CARB Expectations**

External entities implement projects with support from SEP funds contributed by responsible parties that have offset portions of penalties assessed by CARB. As CARB relies on external entities to implement SEP projects, adequate agreements are essential to ensure compliance with policies, rules, regulations, and laws, as appropriate, and to ensure SEP funds are used appropriately and projects meet CARB's expectations. Adequate contracting describes expectations, compliance criteria, responsibilities, duties, and authorities, as well as provides information related to project activities, schedules, funding disbursements, appropriate use rules, recordkeeping, project close-out, and reporting requirements.

Settlement agreements<sup>1</sup> between CARB and those found to have violated California's air quality laws explicitly describe the responsibilities of the violators (responsible parties) to satisfy settlement agreement terms, including payment provisions. Some agreements permit a violator to make a financial contribution to

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<sup>1</sup> Cases settled in lieu of litigation.

an existing SEP to offset a portion of the penalty assessment to be payable by the responsible party directly to one of the three external SEP Administrators, with the balance payable to CARB's Air Pollution Control Fund. However, while we noted robust settlement agreements were in place, adequate agreements were not always in place with external administrators and funding recipients to ensure SEP funds were used properly and projects met CARB expectations.

Specifically, we found that CARB executed a formal agreement with only one of the three SEP Administrators. The agreement with the administrator of the School Bus SEP detailed the intent of the SEP funding, the responsibilities of the parties involved in the SEP including eligible sub-recipients, how the funds were to be used, the timeline for implementation, and allowed for a seven percent administration fee to the SEP Administrator. Further, the agreement required School Bus SEP funding to be used in accordance with existing LESBP guidelines, including selection criteria, contracts, required reporting, and recordkeeping. The LESBP guidelines covered program and administrative requirements in detail; for example, the guidelines detailed both the types of documentation that must be maintained as well as the necessary support for each document. Although the agreement with the School Bus SEP Administrator included many basic components expected of an agreement associated with program funding, the agreement lacked certain components, such as performance metrics to measure on-going progress or a section addressing potential conflicts of interest.

Conversely, there were no formally executed agreements between CARB and the CCDET or Small Engine SEP Administrators. We found only informal and vague documents that lacked almost all of the basic components one would expect of an adequate agreement following leading practices, particularly where program funding is involved. As shown in Exhibit 2, the CCDET SEP and Small Engine SEP documents each had a few key components mentioned, however, these sections were insufficient and lacked detail.

**EXHIBIT 2. COMPONENTS INCLUDED IN THREE SEP AGREEMENTS**

Basic Key Agreement Components	CCDET	Small Engine	School Bus
Roles and responsibilities of each party to the agreement	X	✓-	✓
Project activities and schedules	X	✓-	✓-
Funding information, project budgets, and payment distributions	✓-	✓-	✓
Specific rules, policies, and procedures required to be followed for administering and expending funds, including appropriate uses and excluded costs	X	X	✓
Specific timeframe in which program funds must be utilized after receipt	X	X	✓
Sub-recipient agreements detailing the specific responsibilities to ensure compliance with program expectations	X	X	✓
Recordkeeping requirements	X	✓-	✓
Detailed reporting requirements	✓-	X	✓
Project close-out processes	X	X	✓
Performance metrics	X	X	X
Code of Conduct/Conflicts of Interest	X	X	X
Effective agreement execution and expiration dates	X	X	✓
Signatures of all parties to the agreement	X	X	✓

Key: X agreement did not contain the component; ✓- agreement partially contained the component; ✓ agreement contained the component.

Additionally, while the CCDET SEP and Small Engine SEP agreements each had a few component areas mentioned in their informal agreement documents, these sections were insufficient and required additional detail. In one example, while the CCDET SEP agreement document included some annual reporting requirements, the document only indicated that the SEP Administrator must provide an annual accounting of the SEP funding and did not specify reporting requirements to be included, such as total SEP monies received by the SEP Administrator, amounts disbursed to CCDET receipt colleges, SEP funds spent, or SEP account balances retained at colleges at year-end. While we noted that the document indicated that each recipient college submit an annual report as to how the funding is used to improve diesel programs, it did not specify

what the required components of the report, such as amounts and types of purchases made with SEP money and how the purchases would benefit the program. Further, it did not require accounting of the amount of SEP funds received.

In a second example, the Small Engine SEP agreement document included a record keeping provision that stated the SEP Administrator was required to maintain records of where the money was distributed and retain the records for a minimum of five years. However, this requirement did not provide any further specifics, such as line item level versus annual totals or types of supporting documentation and only proposed that course enhancements could begin as soon as the academic year starting in fall of 2014 if funding was secured by the prior June. Other than that, the project timeline was left open-ended in an “ongoing” status as funding was available. Although not required, the SEP Administrator provided CARB two annual status reports for 2015 and 2016. These reports included information about plans for remaining and future funds, and activities and accomplishments of the program.

Agreements must contain a number of basic provisions that should be formally agreed upon in order to adequately protect CARB’s interests, ensure compliance with all applicable laws, regulations, rules, and best practices, and measure performance of the program. While the School Bus SEP had a formal agreement, without adequate and formal agreements for all SEPs describing responsibilities and expectations, CARB cannot hold those receiving SEP funding accountable in ensuring monies were spent appropriately, efficiently, and effectively and achieved program goals, particularly since current SEP funding largely bypasses the CARB organization and is paid by responsible parties directly to external entities.

### **General Lack of Internal and External Policies and Procedures to Guide SEP Program Activities and Processes**

ED had the overall responsibility for SEP program activities and oversight. While ED had provided internal staff with guidance related to soliciting the appropriate types of SEPs, at the time that the three SEPs were implemented, there were no formal, written policies, procedures, and guidance for staff to utilize while carrying out SEP-related activities and overseeing the SEP programs and its participants. In addition, there was also a general lack of formal program-specific guidance, policies, or procedures provided or available to SEP Administrators and program recipients relative to receiving, disbursing, or expending SEP funds to establish compliance criteria and ensure consistency and accountability; however, CARB did provide program guidance for the School Bus SEP

Specifically, CARB staff within the ED and MSCD are responsible for performing a variety of activities related to the three SEP programs, including establishing settlement agreements, serving as the point of contact for SEP-related questions, and working with SEP Administrators to ensure that they received the portion of the settlement designated to the SEP. Additional program activities important in overseeing the program, but not always consistently conducted, included tracking SEP amounts owed from and paid by responsible parties, following up on collections or late payments, ensuring appropriate expenditures of SEP funds at all levels, or approving the close-out of projects. While some of these activities occurred, ED had not developed formal internal SEP-specific policies and procedures to assign staff with roles and responsibilities associated with

program-required activities. Such formal guidance is particularly important since staff across multiple branches and divisions must work together for CARB’s overall SEP program to be successful. The lack of established SEP-specific policies and procedures to guide staff was exacerbated by the loss of institutional knowledge of SEP processes when the key leaders in ED left the program.

Additionally, except for a brief document describing certain types of allowable expenditures for the CCDET SEP, ED had not provided the CCDET or Small Engine SEP Administrators or program recipients with any program guidance, such as appropriate methods to disburse program funding, approval levels needed for different expenditure thresholds, requirements for competitive purchasing methods, and reviewing and monitoring expenditures. A document describing allowable expenditures was consistently noted among CCDET recipient colleges as the only written guidance from CARB. In regards to the School Bus SEP, CARB applied the associated LESBP guidelines in the contract with the SEP Administrator, which described allowable use of funds, funding/award agreements with program recipients, and contracting, disbursing, and invoicing provisions.

Further, two of the three SEP Administrators, the CCDET and Small Engine SEP Administrators, provided funding directly to “sub-recipients”, generally colleges. We found that neither the two SEP Administrators nor CARB developed any guidance—either internally or for the program recipients—particularly related to processes involving receiving and transferring SEP monies, providing required annual reports to CARB, and ensuring program expenditures were reviewed for appropriateness. According to the CCDET and Small Engine SEP Administrators and many of the recipient colleges, general internal procedures of each entity were utilized for carrying out activities related to receiving and expending monies. Also, the lack of SEP-specific guidance surrounding CCDET SEP program processes was exacerbated by the loss of institutional knowledge within the SEP Administrator leadership.

A comprehensive set of formal policies together with current, complete, and well-documented procedures are essential to an effective system of internal controls as well as ensure CARB’s expectations were met, processes were employed consistently, program objectives were achieved, and funds administered on a consistent basis.

### **CARB Lacked Sufficient Management Oversight of SEP Program Processes and Performance**

Management oversight, review and approval, and monitoring activities are critical to ensuring internal controls continue to operate effectively; however, we found ED’s overall management oversight of the SEP program was inadequate, including a lack of regular and routine reviews and approvals of SEP processes and activities executed by staff and absence of metrics and methods to effectively evaluate ongoing SEP performance.

As described earlier, CARB staff performed various SEP-related activities, but the activities were not regularly reviewed or approved by management. One factor that appears to have impacted management’s ability to provide sufficient oversight of CARB’s overall SEP program was the decentralized structure of internal SEP processes. Specifically, ED did not institute a coordinated management approach across the divisions

involved with the SEP program to ensure staff carried out internal SEP activities consistently, accurately, and as expected by management. For example, staff in the MSCD was responsible for performing various activities related to the School Bus SEP, such as reconciling settlements received by the SEP Administrator to data posted to CARB's website and following-up with other CARB staff to determine the status of late payments. However, settlement agreements were established by investigators working in a separate division and these employees also received SEP payments and forwarded the funds directly to the School Bus SEP Administrator without any involvement or coordination with MSCD. Additionally, the lack of internal control policies and tracking processes we noted earlier further hampered our ability to identify any coordinated and unified approach to management oversight of internal SEP process. Regular and routine management review and approval processes of SEP activities carried out by staff can enable CARB management to identify and correct problems on a timely basis, provide greater assurances as to the accuracy and reliability of information used in decision-making, improve program efficiencies and success, and ensure the appropriate collection and use of SEP funds.

Additionally, ensuring that the SEPs accomplish their goals requires a mechanism for measuring and evaluating performance. However, we found that ED did not have the ability to measure the performance of its overall SEP program due to a lack of SEP-specific goals and objectives in which to measure success; rather the three SEPs acted primarily as a mechanism to support other larger programs with their own unique goals and objectives. For example, the School Bus SEP supported CARB's significant LESB program with the SEP funds accounting for a very small portion of LESB's overall support. Similarly, the CCDET and Small Engine SEPs supported preexisting college courses and did not have their own SEP-specific goals and objectives. While one can see SEP inputs (e.g. funding) and outputs (e.g. purchases of equipment and materials), this information alone cannot reveal if the SEP's intended results, such as improvements to air quality and decreases in human exposure to pollution, were achieved. To determine the performance of a program, one must establish criteria and objectives and collect relevant data, and measure these factors to assess outcomes and results, such performance measurement allows management to determine if program efforts and funds achieve goals and are operating effectively and efficiently.

Further, programs with appropriate oversight require regular status reporting, particularly when funding involves external entities, so that the program's ongoing progress toward meeting expectations, goals, and objectives can be tracked and evaluated over time. Regular performance reporting—typically annually and at the close of a program or project—also provides program participants a vehicle to communicate the program's accomplishments and impact achieved. The following describes the type of status reporting followed by the administrators of the three SEPs and how CARB utilized the information to monitor the programs and projects:

- School Bus SEP—On a semi-annual basis, the SEP Administrator reported each settlement received, including the amount of funds to be used for projects and the amount designated for administration as well as the amount of funds spent to date and the amount of funds remaining. It also provided copies of all invoices received and paid during each reporting period, including evidence of approval and payment and the required supporting documentation. However, the record of funds spent to date in the semi-annual reports lacked sufficient detail to allow CARB to adequately

monitor and measure progress in completing retrofits and replacements. Although such detail was not in the semi-annual reports, the SEP Administrator provided informal updates to the MSCD, including information on the completion status of the retrofits and replacements. MSCD staff used settlement information included in reports to try to reconcile the settlement received by the SEP Administrator against the settlement agreements posted on the CARB website.

- Small Engine SEP—The SEP Administrator provided CARB with annual program status reports for 2015 and 2016. These reports provided data about SEP monies received, use of funds, plans for remaining and future funds, and activities and accomplishments of the program. The reports also indicated how the funding was used to implement small engine repair programs at the three community colleges and provided an outline to the types of purchases made with SEP money. According to CARB staff, the reports were reviewed to match CARB’s record of settlement designations to the financial information reported in the status report. Additionally, CARB staff performed a high-level review to determine if program expenses reported in the status report were in line with the expectations of the project; however, expectations were vague and not clearly defined.
- CCDET SEP—The SEP Administrator did not provide any status reports to CARB. However, some of the recipient colleges did submit annual reports, but the reports were inconsistent because CARB staff did not provide guidance on reporting format or content for the annual reports. For example, not all reports included beginning and ending SEP balances and expenditure information was not always provided. It is not clear if any of the reports were reviewed by CARB staff or if actions were taken as a result of the reported information.

In conclusion, as discussed throughout Finding 1, to improve the system of controls and ensure proper collection and spending of SEP monies, CARB should establish a process to maintain a central and comprehensive universe of settlement agreement information. According to ED, new processes have been implemented establishing a single point of contact within the Division where all settlement information, obligations, and payments will be tracked. Although the three SEPs assessed as part of this audit have since been completed or are nearing completion, ED should ensure that all SEPs going forward have agreements that contain important contract provisions such as defined expectations, roles, responsibilities, duties, and authorities and detailed requirements related to project activities, schedules, funding disbursements, appropriate use rules, recordkeeping, project close-out, performance measuring and regular reporting of program achievements and outcomes. According to ED, efforts are underway to improve agreements between CARB, SEP Administrators, and program recipients. Additionally, CARB should ensure that formal written policies and procedures are developed to guide CARB staff in carrying out SEP-specific activities and to guide external parties in administering all aspects of SEPs. CARB has made progress in this area with updated external SEP guidance developed in 2016 that provides basic directions related to the responsibilities of SEP Administrators, including managing financial contributions to SEPs and monitoring projects. Further, CARB should implement regular and routine management review and approval processes of the SEP processes and activities carried out by staff. Lastly, SEP program goals should be established and a mechanism implemented to measure program outcomes and performance in meeting those goals.



## **Finding 2. Lack of Supporting Documentation Hampered Efforts to Evaluate the Receipt and Use of SEP Funds**

As described in Finding 1, although the School Bus SEP had an established agreement and program guidance, we found there was an overall lack of an adequate and consistent control system covering CARB's SEP program, including internal and external guidance and compliance criteria, necessary to hold SEP Administrators or program participants accountable for utilizing SEP funds appropriately, particularly related to the CCDET and Small Engine SEPs. Nevertheless, we requested revenue and expenditure activity reports from the Administrators and funding recipients of each of the three SEPs to determine the amount of funding provided, the types of program expenses incurred, and if the expenditures appeared to be reasonably related to the intent of the SEPs.

While we were provided revenue and expenditure reports for the entire audit period for the School Bus SEP, as a result of data limitations, we were not provided records and supporting documentation covering all revenue and expenditure activity during the audit period for the CCDET or Small Engine SEPs, impacting the overall reliability and validity of information and limiting our ability to determine how funding was utilized. Specifically, we did not have access to a variety of key financial-related records and reports from two SEP Administrators and several program recipients because auditees were not contractually required to document program activities or retain records and many of the systems used to support program activities were no longer operational. Further, many of the recipients experienced turnover of key staff, resulting in a lack of historical knowledge of program operations. Although the two SEPs provided some revenue and expenditure records and reports, we found varying deficiencies related to the accuracy and completeness of the data made available to us, including:

- Revenue and expenditure activity for the period January 2014 through June 2014 was not included (CCDET SEP and Small Engine SEP).
- Expenditure and revenue records provided were not system generated reports, but rather manually created Excel tracking files and some information provided was not useful because it was commingled with the activity of other programs (CCDET SEP).

In the discussion that follows, we provide information related to the amount of funding provided to the SEPs and the types of program expenses incurred during the audit period based on the information provided.

Based on the information provided, between January 2014 and December 2017, there were 986 settlement agreements executed between CARB and responsible parties found to have violated California's air quality laws. These settlement agreements reflected total assessed penalties of \$74,011,671, of which \$7,946,260 (11 percent) was designated to one of the three SEPs, as reflected in Exhibit 3.

### **Exhibit 3. Comparison of Payments Identified from Settlement Agreements to Amounts Identified as Designated to SEPs, to Amounts Identified as Received by SEP Administrators**

Designation	Number of Settlement Agreements	Total Penalties in Settlement Agreement	Total Penalties Designated to the Three SEPs	Total Payments Received by SEP Administrator
CCDET	349	\$7,930,094	\$1,981,980	\$2,004,921
School Bus	120	\$19,964,012	\$5,530,687	\$4,682,700
Small Engine	4	\$1,844,372	\$433,593	\$433,593
No SEP designation	513	\$44,273,192	\$0	\$0
<b>Total</b>	<b>986</b>	<b>\$74,011,671</b>	<b>\$7,946,260</b>	<b>\$7,121,214</b>

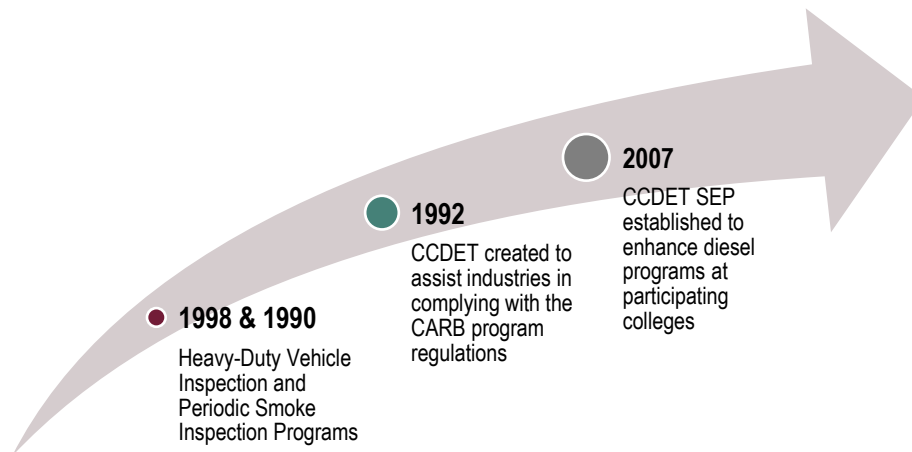
Overall, our analysis of documentation provided revealed CARB and program participant’s records did not always agree related to the amounts of SEP funding disbursed and received, likely due to the lack of complete records as well as a combination of timing issues and some misapplications of payments. Also, while two of the SEPs provided insufficient expenditure information to ensure all expenditure activity was included for review, our analysis of available information found that program expenses for the two SEPs appeared generally related to the intent of the SEPs and were reasonably supported with just a few exceptions. We found no issues with expenditure information provided the School Bus SEP. Also, the timeliness of utilizing SEP funding after receipt appeared reasonable. However, we noted purchasing best practices were not always followed.

In the following sections, we provide our analysis as it relates to each of the three SEPs individually.

### **California Council on Diesel Education and Technology (CCDET) SEP**

In response to new air quality programs adopted into law, a partnership between the CARB, diesel truck and bus engine manufacturers and dealers, and California community colleges worked together to form the CCDET to enhance communication between state regulators and industry stakeholders and coordinate diesel training provided through community colleges. Later, CARB established the CCDET SEP to enhance the diesel programs offered at each of the participating community colleges, as reflected in Exhibit 4.

#### EXHIBIT 4. KEY MILESTONES DATES LEADING UP TO THE CCDET SEP



As of the end of December 2017, there were six community colleges that provided CCDET classes and received SEP funding: College of Alameda, American River College, Los Angeles Trade Tech College, Palomar College, San Joaquin Delta College, and Santa Ana College. The Administrator of the CCDET SEP was Peralta College Foundation.

Overall, our review of available program information revealed that CCDET program participants, including CARB, the CCDET SEP Administrator, and funding recipients, provided records reflecting some discrepancies in SEP funding distributed and received. While expenditure information reviewed suggests program funding was largely spent on costs related to the program's intent and expenses were adequately supported, certain purchasing best practices were not always adhered to by funding recipients, although no requirements were in place to ensure specific practices were followed. Additionally, the timeliness of utilizing SEP funding after receipt appears reasonable.

#### Program Participant Records Reflect Some Discrepancies in CCDET Funding

As described in Finding 1, we found CARB's SEP program lacked consistent and coordinated processes to track the amounts designated to the SEPs and amounts received from responsible parties and paid to program participants to fund the SEPs. As it relates to the CCDET SEP specifically, we noted the following.

- *Amounts Designated to the SEP Compared to Payments Received by the Administrator Differed*

Between January 2014 and December 2017, 349 settlement agreements between CARB and responsible parties reflected total assessed penalties of \$7,930,094, of which \$1,981,980 (25 percent) was designated to the CCDET SEP. The SEP Administrator provided records reflecting that a total of \$2,004,921 was received from either CARB or directly from responsible parties during this time period—a difference of nearly \$23,000, or about one percent greater than expected. In addition to the lack of complete records, the difference is also likely due to a combination of issues, including:

- Some additional payments were received by the SEP Administrator after December 2017 or not received at all,

- Some payments received by the SEP Administrator related to settlement agreements executed prior to January 2014,
  - Few small overpayments made by responsible parties to the SEP, and
  - One payment designated to the CCDET SEP was incorrectly paid to the School Bus SEP Administrator by the responsible party.
- *Some Payments Received Could Not Be Readily Associated with Settlement Agreements*  
 Of the \$2,004,921 that the SEP Administrator reported receiving, we were able to associate \$1,457,108 of the payments to 205 of the 349 settlement agreements. For the remaining \$547,813 received, the naming convention reflected on the payment information could not easily be associated with a settlement agreement. For example, payments totaling \$388,456 were received from CARB (“State of California”), but there were no other identifiers to match the payments to specific responsible parties or settlement agreements.
  - *Discrepancies in Amounts Reported as Disbursed to Program Recipients*  
 Of the \$2,004,921 received by the SEP Administrator, \$100,246 (5 percent) was deposited into a separate general fund for the administrative fee allowed by CARB with the remainder to be spent on programmatic activities related to enhancing diesel programs and distributed equally between each of the six recipient colleges. While the records provided by the SEP Administrator reflected that \$1,904,581 was distributed to the six colleges during the audit period, records provided by the colleges reflected a total of \$1,801,496 was received, or about 5 percent less than expected, as reflected in Exhibit 5. We were unable to determine the reasons for the differences in the amounts reported as distributed to and received by colleges due to the lack of available and complete data.

**EXHIBIT 5. COMPARISON OF CCDET SEP FUNDS DISPERSED TO FUNDS RECEIVED**

<b>Recipient College</b>	<b>Amounts Dispersed to Colleges Per Peralta Records</b>	<b>Amounts Received from Peralta Per College Records</b>
<b>LA Trade Tech College</b>	\$363,758 <sup>2</sup>	\$412,792
<b>San Joaquin Delta College</b>	\$313,017	\$218,792
<b>Palomar College</b>	\$313,017	\$319,523
<b>Santa Ana College</b>	\$313,017	\$302,646
<b>College of Alameda</b>	\$313,017	\$266,978
<b>American River College</b>	\$288,757 <sup>3</sup>	\$280,764
<b>Total</b>	<b>\$1,904,581</b>	<b>\$1,801,496</b>

<sup>2</sup> The total reported as distributed to LA Trade Tech College was more than the other colleges because the settlement agreement with the County of Los Angeles directed that its payment be distributed only to LA Trade Tech College.

<sup>3</sup> The total reported as distributed to American River College was less than the other colleges because the American River College was newly accepted to the CCDET consortium in 2014 and the first distribution occurred in March of 2014.

Our review of available program information revealed that CCDET program participants, including CARB, the SEP Administrator, and funding recipients, provided records reflecting some discrepancies in SEP funding distributed and received. Improved and centralized tracking of SEP funding receipts and disbursements is needed.

Expenditures Appear Related to Program Intent and were Adequately Supported, but Certain Purchasing Best Practices were not Followed

The purpose of the CCDET SEP is to provide funding to improve the diesel programs at community colleges. While the six recipient colleges' records reflected that they received a total of \$1,801,496 between January 2014 and December 2017, their records also reflected that they expended a total of \$1,872,862 in SEP funding. As such, they spent about \$71,366 more than they received during the same period, likely due to SEP funding received before January 2014 that was available for purchases during the audit period.

While program recipients did not have formal agreements with CARB or the SEP Administrator that described required processes related to receiving and expending SEP funding, our review of the expenditure information provided by the colleges found that the SEP funding appeared to be generally spent on programmatic items that were related to the program's intent, such as equipment and advanced instructional supplies, as shown in Exhibit 6. We also performed site visits at five CCDET colleges and visually inspected certain large equipment and materials purchases.

**EXHIBIT 6. BRIEF DESCRIPTIONS OF CCDET SEP COLLEGES' EXPENDITURES**

<b>Recipient College</b>	<b>Amounts Expended</b>	<b>Brief Description of Expenditures</b>
<b>College of Alameda</b>	\$429,019.31	Truck and truck parts, training modules, instructional parts and tools, classroom materials, and student scholarships
<b>American River College</b>	\$282,975.37	Shop equipment, tools, consumables (i.e. oil, gaskets, filters), and classroom supplies, instructors and training
<b>Los Angeles Trade Tech College</b>	\$215,655.2	Diesel engine, equipment, stands, tools and parts, smartboards and software for instruction
<b>Palomar College</b>	\$398,481	Truck, diesel engine and stand, instructional aides, and training equipment
<b>San Joaquin Delta College</b>	\$303,637.08	Truck, equipment, and tools, instructional supplies, and student certificates, awards and scholarships
<b>Santa Ana College</b>	\$ 243,093.72	Diesel engine, equipment, tools, and parts, and classroom electronics
<b>Total</b>	<b>\$1,872,861.68</b>	

Of the \$1,872,862 in program expenditures incurred during the audit period, we performed a detail review of 72 expenditure items (12 from each of the six colleges) totaling \$968,465. Our review noted that only \$571, or less than 0.1 percent, was spent by three colleges on what appeared to be non-programmatic items, namely food and drinks.

Additionally, without detailed guidance from CARB or the SEP Administrator, the six colleges relied solely on internal purchasing policies, which varied by each entity. Specifically, three colleges utilized their accounting department to manage SEP funding and purchased program materials through their respective colleges' procurement office; these colleges utilized fairly rigorous purchasing policies that required competitive bidding. However, the three colleges' SEP funding was managed through a college foundation and, as such, their purchasing policies were lenient and only required two authorizing signatures to expend program funding, even for large purchases.

Although none of the colleges had agreements to follow specific purchasing policies as it relates to SEP funding, our detailed review of the 72 expenditure items looked for reasonable purchasing activities and found the following:

- Most of the items were reasonably supported by an invoice, quote, or receipt. However, 10 items totaling \$19,794 did not have sufficient support. In one example, a college paid a vendor \$11,691 twice for the same diesel engine purchase. In another example, the college only provided the signed requisition with a description of the charges, such as to pay down \$1,500 of a Cal Card balance, but did not include any support for the original charges.
- The six colleges were able to provide approval documentation for 68 of the 72 expenditure items reviewed. For four expenditures totaling \$15,992 where supporting documentation was not provided by three of the colleges, the colleges either explained that records older than three years were not retained per internal record retention policies or simply did not have any supporting documentation to provide.
- All six colleges were unable to provide evidence, where reasonable, of multiple quotes, competitive bidding, or sole source justification, including the three colleges that followed rigorous college policies with purchasing policy requirements. Typically, dollar thresholds are established to control purchasing activities, such as requiring multiple quotes for items over \$5,000 or competitive bidding for items over \$50,000, for example. Of the 72 expenditure items reviewed in detail, we found that 21 were over \$5,000, which would reasonably require competitive purchasing processes, and three colleges provided some documentation that a competitive purchasing method was used for just four of the 21 items.

Overall, while expenditures information provided could not be confirmed as complete, our testing suggests expenditures reviewed related to the intent of the CCDET SEP and were generally reasonably supported with just a few exceptions, but best purchasing practices were not always followed.

### Timeliness of Utilizing CCDET SEP Funding Appears Reasonable

Because SEP funding was based on when settlements were executed and responsible parties' submitted payments rather than based on program needs, there was not a predictable method for the Administrator or funding recipients to anticipate how much or when program funding would be available to be distributed at any given time. Additionally, there was no guidance provided to the program participants regarding funding expectations; rather, program participants simply deposited funding as it was distributed by the Administrator. As a result, the colleges reported that there were challenges budgeting the money each year and would allow balances to accumulate until a large purchase could be made. For example, when a college planned to purchase an expensive piece of equipment, such as a Freightliner truck, it was common practice to reserve SEP funds until sufficient funds were accumulated to pay for the equipment. Due to the lack of sufficient accounting records, we were unable to determine the balances for all of the colleges.

Further, according to the six colleges and the SEP Administrator, none of the SEP program-related funding was held in interest bearing accounts.

### **School Bus and Diesel Emission Reduction (School Bus) SEP**

Administered by the San Joaquin Valley Air Pollution Control District, the School Bus SEP was established in 2011 to help program participants—public school districts, Joint Power Authorities, and private school bus companies transporting school children in California—comply with updated emissions regulations by providing funding to offset the cost of compliance. Initially, the focus of the SEP was to help fund new bus purchases as well as retrofitting existing buses to comply with updated emissions regulations, but was later expanded to also cover the replacement of recalled filters. Program participants applied to the SEP Administrator for the following types of assistance:

Requests for removal and replacement of recalled filters

The SEP Administrator paid a specialty vendor directly to provide those services on behalf of the program participants.

Requests for purchases of new school buses and retrofits of existing buses

The SEP Administrator conducted a competitive funding application and solicitation processes. Program participants were awarded funding for the purchases on a reimbursement basis.

Overall, our analysis of documentation provided revealed CARB and the School Bus SEP Administrator provided records reflecting some discrepancies in the SEP funding received. However, our testing of expenditure information provided found that the expenses appeared related to the intent of the SEP, were adequately supported, and complied with contract requirements. Additionally, the timeliness of utilizing School Bus SEP funding after receipt appears reasonable.

### Program Participant Records Reflect Some Discrepancies in School Bus Funding

As described previously, we found CARB's SEP program lacked consistent and coordinated processes to track the amounts designated to the SEPs and amounts received from responsible parties and paid to program participants to fund the SEPs. As it relates to the School Bus SEP specifically, we noted discrepancies in program participant records of funding amounts received.

Specifically, between January 2014 and December 2017, 120 CARB settlement agreements, reflecting total penalties of \$19,964,012, designated \$5,530,687 (27.7 percent) of the penalties to the School Bus SEP. The SEP Administrator provided records reflecting that it received \$4,682,700 in SEP payments during this time period—a difference of nearly \$848,000. In addition to the lack of complete records, the difference is also likely due to a combination of issues, including:

- Some additional payments were received by the SEP Administrator after December 2017 or not received at all,
- Some payments received by the SEP Administrator related to settlement agreements executed prior to January 2014,
- Few small overpayments made by responsible parties to the SEP, and
- One payment designated to the CCDET SEP was incorrectly paid to the School Bus SEP Administrator by the responsible party.

Like the CCDET SEP, our review of available program information revealed that CARB and the School Bus SEP Administrator provided records reflecting some discrepancies in SEP funding distributed and received. Improved and centralized tracking of SEP funding receipts and disbursements is needed.

### Expense Items Reviewed Appear Related to Program Intent, were Adequately Supported, and Complied with Requirements

Of the \$4,682,700 received by the SEP Administrator, \$327,789 (7 percent) was set-aside for the administrative fee allowed by the contract with CARB with the remaining \$4,354,911 to be spent on programmatic costs for bus retrofits and filter replacements on behalf of school districts that submitted grant applications for funding. According to high-level system reports, through December 2017, the SEP Administrator had encumbered or expended a total of \$3,389,970, leaving about \$0.96 million remaining available. Of the \$3,389,970, only \$722,336 was expended through December 2017 and the remaining \$2,667,634 was encumbered in executed contracts but not yet spent.

CARB had a formal agreement with the SEP Administrator that described requirements related to expending SEP funding and our review of about \$120,000 of the \$722,336 expenditures (16.6 percent) found that the Administrator complied with those requirements with no exceptions. Specifically, invoices were approved by multiple individuals employed by the SEP Administrator, included the required support, invoiced amounts were consistent with the standard parts list included in the agreement between the Administrator and CARB, and applicable invoice packets included the required California Highway Patrol inspection reports confirming



the retrofit services were performed as invoiced. Additionally, for each invoice packet reviewed, we requested the associated required annual mileage reports to ensure the buses were not sold within five years of purchase or retrofit, consistent with the program requirements—all bus purchases and retrofits complied with the requirements.

Overall, we found the expenditures reviewed appeared related to program intent, were adequately supported, and complied with contract requirements between CARB and the SEP Administrator.

Timeliness of Utilizing of School Bus SEP Funding Appears Reasonable

Like the CCDET SEP, the School Bus SEP funding was based on when settlements are executed and responsible parties submitted payments rather than based on program needs, there was not a predictable method for the Administrator or funding recipients to anticipate how much or when program funding would be available at any given time. As a result, the SEP Administrator allowed balances to accumulate until sufficient funding was available to purchase buses and to enter into a contract with the service provider to realize economies of scale instead of paying for each retrofit separately. Exhibit 7 shows the timing of School Bus SEP funds received and expended.

**EXHIBIT 7. SCHOOL BUS SEP FUNDS RECEIVED AND ENCUMBERED/ EXPENDED, 2012 THROUGH 2017**

Period Ending	Programmatic Funds Received (93%)	Programmatic Funds Encumbered / Expended	Percent of Available Funds Encumbered/Expended
September 2012	\$32,318	\$0	0.0%
September 2013	\$90,210	\$19,996	22.2%
September 2014	\$601,626	\$75,967	12.6%
December 2015 <sup>1</sup>	\$2,141,489	\$256,267	12.0%
December 2016	\$3,849,321	\$2,178,628	56.6%
December 2017	\$4,354,911	\$3,389,970	77.8%

<sup>1</sup>Program reporting periods were changed in 2015

From 2012 through the end of calendar year 2014, the SEP Administrator built up SEP funds but had only expended or encumbered a small portion. By the end of 2016 and 2017, a significant increase in the percent of funds utilized as the contract for retrofits was executed and work completed. According to the SEP Administrator, remaining funding will be utilized to finish outstanding filter replacements and any additional funding left over will be repurposed with the approval of CARB.

Additionally, according to the SEP Administrator, SEP funds accumulated were held in an interest-bearing account, and generated an additional \$56,847 that was utilized for project funding.

## Small Engine Maintenance & Repair Courses (Small Engine) SEP

The Small Engine Maintenance & Repair Courses (Small Engine) SEP was established in 2014 to fund emissions-controlled maintenance and repair courses at three California community colleges. The purpose of Small Engine SEP was to purchase new equipment and instructional materials and provide student scholarships in vocation training for small off-road engines, such as in power lawn mowers, leaf blowers, chainsaws, generators, and small gas-powered scooters. The SEP Administrator for the Small Engine SEP was the Foundation of California Community Colleges that directly purchased program-related equipment and training materials on behalf of the three recipient colleges and also entered into reimbursement-based contracts with the colleges to pay for instructor time and college facility use.

Overall, our analysis of documentation provided revealed CARB and the Small Engine SEP Administrator provided records that agreed on the level of funding disbursed and received. While expenditure information reviewed suggests program funding was largely spent on costs related to the program's intent and expenses were adequately supported, administrative and personnel-related costs were higher than amounts incurred by the other two SEPs. Additionally, the timeliness of utilizing Small Engine SEP funding after receipt appears reasonable.

### Amounts Designated to Small Engine SEP and Payments Received Per SEP Administrator Records Agreed

Between January 2014 and December 2017, four CARB settlement agreements reflecting total penalties of \$1,844,372 designated \$433,593 (23.5 percent) of the penalties to the Small Engine SEP. The SEP Administrator provided records reflecting that it received \$433,593.

### 30 Percent of Small Engine SEP Funding was Spent on Administrative and Personnel Costs

The administrators of each of the three SEPs reviewed as part of this audit were allowed an administrative fee of between 5 and 7 percent—the Small Engine SEP administrative fee was set at 7 percent. However, we found that in addition to the 7 percent spent on administrative costs, and additional 23 percent of program funding was spent on the SEP Administrator's personnel costs associated with the program. Specifically, we found that about 30 percent of the total \$433,593 SEP funding kept for administrative and personnel costs:

- \$28,366 (about 7 percent) for administrative costs associated with accounting, finance and human resource management, information technology support and other overhead costs as allowed by the contract.
- \$100,469 (23 percent) for the SEP Administrator's personnel costs associated with developing, implementing and administering the new program, securing the participation of colleges, instructors and eligible students.

The amounts spent on administrative and personnel costs appear much higher than the other two SEPs that spent between 5 and 7 percent on administrative costs. It appears that the intent of the Small Engine SEP was to utilize funding to enhance *existing* programs; instead, SEP funds were used in part to implement *new* programs at the colleges, which is likely the reason for the additional personnel costs.

### Expenditures Appear Related to Program Intent and were Adequately Supported, but Certain Purchasing Best Practices were not Followed

While formal agreements were not in place that described required processes related to receiving and expending SEP funding, our review of the expenditure information provided by the SEP Administrator found that the SEP funding appeared to be generally spent on programmatic items related to the program's intent, such as student internships, curriculum and instruction, and purchasing equipment and tools necessary to diagnose and repair small engines. In total, the Small Engine SEP Administrator utilized \$301,290, or about 70 percent of the funding, on programmatic costs in the following major categories:

- Instructors—\$122,963
- Student Internships—\$98,950
- Supplies—\$29,986
- Equipment—\$28,680
- Rent—\$19,300
- Travel—\$1,412

Of the \$301,290 spent on programmatic costs and the \$100,469 spent on the SEP Administrator's personnel costs, we performed a detail review of 16 expenditure items totaling \$60,394. We found that all of the expenditure items reviewed appeared reasonably related to the Small Engine SEP.

However, CARB did not provide detailed guidance to the SEP Administrator for purchasing requirements related to SEP funding and the SEP Administrator did not appear to have internal policies related to purchasing and procurement methods. Our detailed review of the 16 expenditure items looked for reasonable purchasing activities and found the following:

- Most of the items were reasonably supported by an invoice, quote, or timesheets. However, four of the 16 items reviewed totaling \$20,820 did not have sufficient support. In one example totaling \$10,578 related to contracted-instructor fees, the SEP Administrator was unable to provide sufficient support documenting work logs and timesheets for time spent even though contracts between the SEP Administrator and the instructors stated that hours worked must be logged. For three items, which totaled \$10,242 related to SEP Administrator personnel costs, timesheet documentation was not provided. Additionally, for all of the SEP Administrator personnel costs reviewed, a reasonable and consistent methodology to allocate a portion of the Administrator's total personnel costs to the SEP program was not provided. According to the SEP Administrator, the amounts allocated were conservative estimates.
- Of the 16 expenditure items, we reviewed four related to the purchase of goods and travel and the SEP Administrator was able to provide reasonable approval documentation for one of the items. For example, one expenditure totaling \$4,965 for tools, lawn mower parts, and equipment was only signed by the individual requesting the purchase and lacked a second authorizing signature. Best

practices require that an independent reviewer approve such purchases and the requisition form reviewed appeared to require a secondary signature. Additionally, the expenditure totaling \$596 for air travel had evidence of review however, the travel claim did not include a signature for approval. Further, the expenditure for a software license itemized a portion of the total \$157 for the SEP program and also did not have approval documentation.

- Of the 16 items tested, a few items were above \$5,000; however, those items related to acquiring consultant services of instructors employed by the three recipient colleges to provide the instructional services and SEP Administrator personnel costs, and thus, reasonably would not be applicable to competitive procurement processes.

Our testing suggests that expenditures reviewed were related to the intent of the Small Engine SEP and were generally reasonably supported with just a few exceptions.

Timeliness of Utilizing Small Engine SEP Funding Appears Reasonable

Unlike the CCDET or School Bus SEPs, the Small Engine SEP funding was predictable as the program involved receiving only four payments associated with settlement agreements. During the first year of receiving SEP funding (June 1, 2014 to June 30, 2015), efforts were focused on the start-up including program planning and contract negotiation, consequently operational expenditures were minimal. During the first full year of running the program (July 2015 to June 2016), the majority of programmatic funds were expended, as shown in Exhibit 8.

**Exhibit 8. Small Engine SEP Funds Received and Encumbered/Expended, 2014 through 2018**

Period	Programmatic Funds Received (70%)	Programmatic Funds Expended	Percent of Available Funds Expended
June 1, 2014, through June 30, 2015	\$257,775	\$4,796	1.9%
July 1, 2015, through June 30, 2016	\$303,515	\$246,352	81.2%
July 1, 2016, through January 31, 2018	\$303,515	\$301,023	99.2%

Additionally, according to the SEP Administrator, Small Engine SEP funds were not held in an interest-bearing account and all funds had been expended as of June 30, 2018.

In conclusion, a general lack of sufficient processes, criteria, and data hampered efforts to fully evaluate the receipt and use of SEP funding, but as discussed throughout Finding 2, our analysis of documentation provided revealed the records of CARB and program participants did not always agree related to the amounts of SEP funding disbursed and received, likely due to the lack of complete records as well as a combination

of timing issues and some misapplications of payments. Additionally, testing of available information found that expenses appeared generally related to the intent of the SEPs and were reasonably supported. Lastly, the timeliness of utilizing SEP funding after receipt appeared reasonable. To improve reported SEP funding discrepancies and ensure all funds are received as expected, CARB should implement a consistent and coordinated process to track amounts designated to SEPs, amounts paid by responsible parties, amounts paid to SEP Administrators, and amounts received by program recipients. Although the three SEPs assessed as part of this audit have since been completed or are nearing completion, CARB should ensure all future SEPs have formal purchasing requirements and guidance to ensure SEP funds are utilized for appropriate purposes and follow leading purchasing practices, such as checking for duplicate payments, ensuring appropriate support and approvals are provided, and utilizing competitive purchasing methods. These types of controls are meant to eliminate personal conflicts of interests for those involved in the procurement process and to promote the efficient use of funding to achieve program goals and objectives.

## Chapter 2—Audit Recommendations

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As the three SEPs assessed as part of this audit have since been completed or are nearing completion, we offer recommendations to improve processes related to CARB's overall SEP program and future SEPs. Specifically, to improve CARB's system of controls to ensure responsible parties provide the agreed-upon funding to the SEPs as part of their settlement agreement process and that program monies were spent appropriately and in-line with CARB expectations, we offer the following go-forward recommendations for consideration:

1. Establish within the Enforcement Division (ED) a process to maintain a central and comprehensive universe of settlement agreement information. Specifically, designate a single point of contact where all settlement agreements executed are immediately sent and key information, such as total settlement amounts, amounts designated to SEPs, dates paid, etc., is entered into a tracking mechanism, such as an electronic spreadsheet or database.
2. Reduce the individual handling of SEP payments associated with settlement agreements within CARB by establishing a consistent, coordinated, and centralized process for responsible parties to submit SEP funds, such as requiring all responsible parties to send SEP payments directly to SEP administrators and eliminating the ability for responsible parties to submit some SEP payments (e.g. wire transfers) to ASD for processing, handling, and forwarding.
3. Establish a process for ED to track both SEP and non-SEP payments made by responsible parties associated with all settlement agreements and follow-up on settlement agreements with past due amounts to investigate the responsible party's adherence to the settlement agreement terms to ensure corrective actions have taken place and all required amounts remitted.
4. Move away from funding on-going programs to a merit-based approach that provides funding to applicants for projects with defined scopes, discrete goals, and timelines for implementation.
5. Establish sufficient and formal agreements with SEP administrators or with a single SEP administrator acting as a "clearinghouse" for all other SEPs. Agreements should contain adequate and formally agreed-upon provisions that protect CARB's interests, and ensure compliance with all applicable laws, regulations, rules, and best practices. Provisions should define expectations, compliance criteria, roles, responsibilities, duties, and authorities and describe requirements related to project activities, schedules, funding disbursements, appropriate use rules, recordkeeping, project close-out, performance measuring and regular reporting of program achievements and outcomes. Agreements should also state when SEP Administrators are required to enter into agreements with third-parties, such as when funding is disbursed to colleges or school districts, to ensure all SEP funding recipients adhere to CARB's rules and expectations.
6. Establish a comprehensive set of internal policies and procedures that outline the roles and responsibilities of CARB management and staff involved in SEP processes and activities. A comprehensive set of policies and procedures should include, but is not limited to, tracking SEP amounts owed from and paid by responsible parties and following up on collections or late payments;

communicating funding expectations to recipients, ensuring program expenditures are reviewed for appropriateness; monitoring program performance by formally reviewing and approving regular SEP performance and outcomes reporting and providing feedback to program participants, including additional guidance on program management and administration; and developing formal project-close out processes.

7. Establish comprehensive program guidance for SEP Administrators and funding recipients in regards to receiving, disbursing, transferring, or expending SEP funds, including, but not limited to, general purchasing guidelines, such as requirements for appropriate use of SEP funds, competitive solicitations, thresholds for purchase approval, invoicing and expenditure supporting documentation, and management and disposal of capital assets purchased with SEP funds; timeliness of utilizing program funds and holding program funding in interest bearing accounts; and recordkeeping, performance measurement, project close-out, and regular status reporting of program information, outcomes, and achievements.
8. Establish SEP-specific program goals as well as a framework to measure program outcomes and performance in meeting those goals. Consistent with AB 1071, program goals should provide a connection between a specific SEP project and an environmentally impacted community. To measure program performance, CARB should establish specific performance targets in the agreement and require SEP administrators to periodically report on ongoing progress in meeting those targets.
9. Establish a process to periodically perform site visits to SEP administrators and funding recipients to spot check and inspect SEP activities, including verifying large equipment purchased with SEP funds are adequately secured, stored, and maintained, and to ensure the program activities are consistent with progress reporting.