

Proposition H

Police and Fire Public Safety Oil Production Act

*Generated nearly \$3 million in additional
revenue for public safety in FY 2020*



Independence you can rely on

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Table of Contents

Audit Results 1

 Conclusion 1: Prop H revenues received during FY 2020 were substantively calculated properly based on oil producers’ reports remitted to the City.....1

 Conclusion 2: FY 2020 expenditures of Prop H funds complied with the approved uses set forth in the City’s Municipal Code.2

 Conclusion 3: The amount of unspent Prop H monies at the end of FY 2020 that were carried over into the current fiscal year is \$201,389.....3

 Conclusion 4: The anticipated projects and programs funded by Prop H revenue in FY 2021 comply with the approved uses set forth in the City’s Municipal Code.4

Background..... 5

Objective, Scope & Methodology 10

Management Comments 12

Audit Results

Objective 1: Identify Prop H revenues received during FY 2020 and determine if funds remitted by the oil producers were properly calculated based on oil producers' reports remitted to the City.

Conclusion 1: Prop H revenues received during FY 2020 were substantively calculated properly based on oil producers' reports remitted to the City.

The City of Long Beach (City) received a total of \$2,980,540 of Proposition H (Prop H) oil tax revenue, including penalties and interest, during fiscal year (FY) 2020, as depicted in Table 1 below. This is a revenue decrease of 9% from the prior year. The oil tax revenue received was based on FY 2020 production reports totaling 9,181,310 barrels of oil in Fiscal Year 2020 excluding the month of April 2020¹.

Table 1
Total Tax Revenues Received
FY 2020

Oil Tax Revenue	Penalties and Interest	Total
\$ 2,961,873	\$ 18,667	\$ 2,980,540

We tested 97% of the special tax revenues received in FY 2020 through confirmations with the top oil producers and determined that funds remitted by oil producers were substantively calculated properly based on the reports presented to the City. Not all penalties were assessed on late payments when appropriate, however, they are not a substantial portion of total revenue.

In FY 2020, the special tax revenues and penalties received were substantively deposited correctly into Fund 2100, the Fire Public Safety Oil Production Tax Special Revenue Fund, and Fund 2150, the Police Public Safety Oil Production Tax Special Revenue Fund, as required by §3.80.225 of the Municipal Code. The revenues were divided equally between the funds.

¹ Per the Municipal Code, Prop H revenue will be suspended for any month in which the average WTI oil index price is below \$20.00 per barrel. The average monthly price of oil in April 2020 was \$16.52.

Objective 2: Identify FY 2020 expenditures of Prop H funds and analyze whether such expenditures complied with the approved uses set forth in the Long Beach Municipal Code.

Conclusion 2: FY 2020 expenditures of Prop H funds complied with the approved uses set forth in the City's Municipal Code.

Prop H expenditures during FY 2020 totaled \$2,959,804 and were made for eligible costs as defined in the City's Municipal Code.

Police Department

In FY 2020, Prop H expenses for the Police Department totaled \$1,481,094. In FY 2020, \$1,483,067 (100.1% of department expenses²), was spent on salaries and benefits for Police Department employees. This \$1,483,067 was spent on partially funding seven employees assigned to the Police Department's Mental Health Evaluation Team. These expenditures increased from FY 2019 largely due to the addition of a Police Sergeant to the Mental Health Evaluation Team. The remaining Prop H department expenses were spent on interfund service expenses.

In total, we reviewed \$1,475,081 (99%) of Prop H Police Department expenditures and found that they complied with the approved uses as set forth in the City's Municipal Code.

Fire Department

The Fire Department's FY 2020 Prop H expenditures totaled \$1,478,710. Most of the expenditures, \$1,469,481 (99% of department expenditures), were for salaries and benefits for nine positions to staff Fire Truck 17. The remaining Prop H department expenses included additional smaller charges for benefits and salaries (0.2%) and costs for interfund service expenses (0.4% of department expenses). Due to the increasing operating costs, Prop H funds were not used to fund Fire Academy training costs as the Fire Department had anticipated doing in FY 2020.

We reviewed \$1,469,481 (99%) of Prop H Fire Department expenditures and found that they complied with the approved uses as set forth in the City's Municipal Code.

² An accrual reversal was credited to the fund in the amount of \$7,985 (-0.5%). As a result, this allowed the department to charge more to Prop H than the total fund expenses listed.

Objective 3: Determine the amount of unspent Prop H monies on deposit at September 30, 2020 that were carried over into the current fiscal year, FY 2021.

Conclusion 3: The amount of unspent Prop H monies at the end of FY 2020 that were carried over into the current fiscal year is \$201,389.

Financial Management has a Prop H reserve policy which establishes a range of \$150,000 to \$400,000 to be available should Prop H oil production revenues decline, or for any one-time needs. Financial Management has stated that this policy is used as a general guideline, and deviations from the policy are not necessarily causes for concern. In addition, they have stated that the Prop H Fund is part of a multi-fund and multi-year budgeting strategy; therefore, decisions regarding reserves are not made based on any one particular year.

During FY 2020, the carryover amount increased 11.48% from the prior fiscal year, from \$180,653 to \$201,389. This amount is within the allowed carryover range established by Financial Management’s carryover policy. The projected carryover for FY 2021 is expected to be \$201,389 which is equal to FY 2020 carryover. See Table 2 below.

**Table 2
Prop H Funds Cash Flow
FY 2019-2021**

	Police	Fire	Total	FY % Change
FY 2019 Carryover	\$ 176,393	\$ 4,260	\$ 180,653	
FY 2020 Actual Revenue	\$ 1,491,337	\$ 1,489,203	\$ 2,980,540	
FY 2020 Actual Expenditures	\$ 1,481,094	\$ 1,478,710	\$ 2,959,804	
FY 2020 Carryover	\$ 186,636	\$ 14,753	\$ 201,389	11%
FY 2021 Budgeted Revenue	\$ 1,659,194	\$ 1,659,194	\$ 3,318,387	
FY 2021 Budgeted Expenditures	\$ 1,659,194	\$ 1,659,194	\$ 3,318,387	
FY 2021 Projected Carryover	\$ 186,636	\$ 14,753	\$ 201,389	0%

Objective 4: Determine the status of any projects and programs funded by Prop H revenue and whether they comply with the approved uses set forth in the City's Municipal Code.

Conclusion 4: The anticipated projects and programs funded by Prop H revenue in FY 2021 comply with the approved uses set forth in the City's Municipal Code.

Anticipated Activities

In FY 2021, the Police Department plans to use all budgeted Prop H funds (\$1,659,194) to help fund its Mental Health Evaluation Team (Team). Funding will cover a portion of the staffing costs for six Police Officers on the Team. The Mental Health Evaluation Team responds to calls for service that involve individuals who may require mental health services. The Team partners with the Los Angeles County's Department of Mental Health when they respond to calls, allowing the Team to offer access to mental health services in an efficient manner.

In FY 2021, the Fire Department intends to use all budgeted Prop H funds (\$1,659,194) to fund salaries and benefits, including workers' compensation charges, for nine positions on Fire Truck 17: three engineers and six firefighters.

The Departments' anticipated activities for Prop H funds, as described above, comply with the approved uses as set forth in the City's Municipal Code.

FY 2021 Budgeted Revenues and Expenditures

For FY 2021, budgeted Prop H revenues and expenditures are \$3,318,387 and \$3,318,387 respectively, as shown in Table 2 on the prior page.

Background

Proposition H

The citizens of Long Beach (City) approved Proposition H (Prop H), the Police and Fire Public Safety Oil Production Act, on May 1, 2007. Prop H amended the City’s Municipal Code to assess an additional 25 cents per barrel special tax on oil producers in Long Beach, with the tax rate to be adjusted annually on June 1 based on the Consumer Price Index (CPI). The special tax became effective on June 1, 2007, and has since been adjusted as follows:

Table 3
Prop H Tax Rates
FY 2007-2020

Effective Date	Adjustment for CPI	Amount of Special Tax
June 1, 2007	-	\$0.25
June 1, 2008	\$0.01	\$0.26
June 1, 2009	\$0.01	\$0.27
June 1, 2010	\$0.00	\$0.27
June 1, 2011	\$0.00	\$0.27
June 1, 2012	\$0.01	\$0.28
June 1, 2013	\$0.00	\$0.28
June 1, 2014	\$0.00	\$0.28
June 1, 2015	\$0.01	\$0.29
June 1, 2016	\$0.00	\$0.29
June 1, 2017	\$0.01	\$0.30
June 1, 2018	\$0.00	\$0.30
June 1, 2019	\$0.02	\$0.32
June 1, 2020	\$0.01	\$0.33

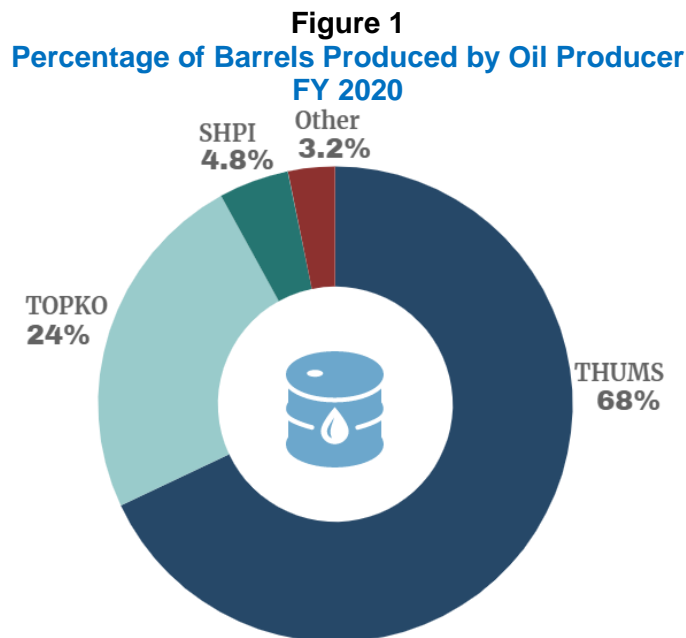
This special tax is in addition to the existing tax of 15 cents per barrel produced and is a legally distinct tax to be used explicitly to fund public safety. Specifically, these tax proceeds may be used only for police officers, firefighters, and related costs, including but not limited to equipment, facilities, and training, to ensure responses to public safety needs.

The special tax is due to the City on or before the last day of the calendar quarter. The payment is based on a production quarter, which ends one month earlier than the calendar quarter. For example, the special tax payment for the production quarter ending August 31, 2020 was due to the City on or before September 30, 2020.

Failure to pay the tax results in a penalty of 25% of the total tax on the first day of the month following the close of the calendar quarter. If the tax remains unpaid for each month thereafter, an additional 10% penalty is assessed, up to a maximum of 100% of the tax amount.

Oil Producers

In fiscal year (FY) 2020, oil operators in Long Beach reported a total of 10,006,240 barrels of oil produced. Due to the monthly price of the WTI crude index dropping below \$20 for the month of April 2020, a total of 9,181,310 barrels of oil produced were taxed for Prop H. THUMS Long Beach Company (THUMS), Tidelands Oil Production Company (TOPKO) and Signal Hill Petroleum, Inc. (SHPI) were the City's top oil producers in FY 2020. As illustrated in Figure 1 below, these three oil operators accounted for approximately 97% of oil produced in FY 2020.

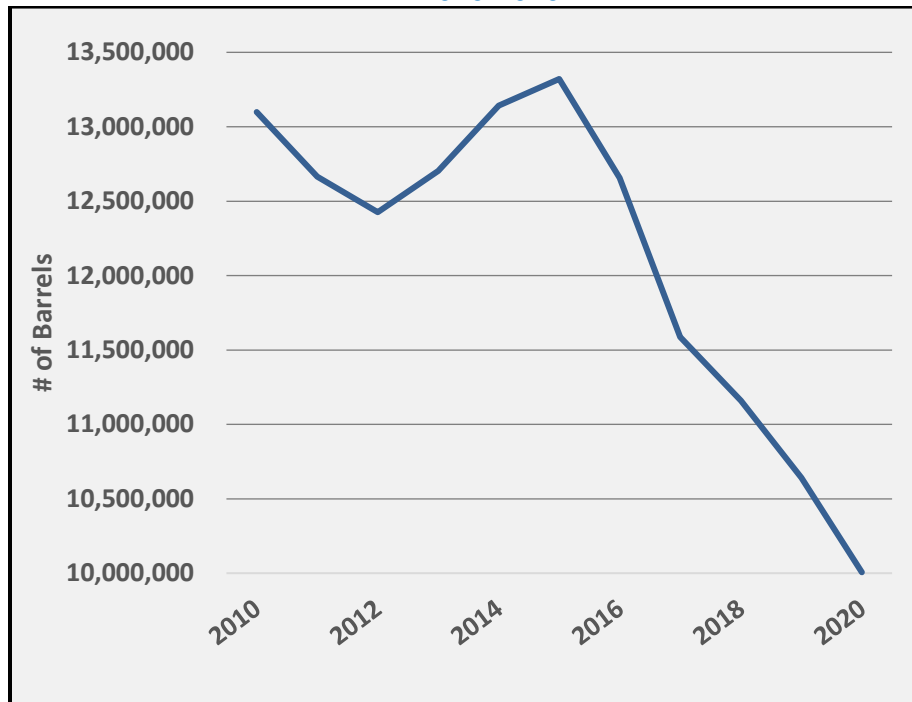


Most of the oil is produced in the Wilmington Oil Field. The Wilmington Oil Field was discovered in Long Beach in 1932 and is 13 miles long, extending from San Pedro to Seal Beach. The field is divided into two sections: West and East. TOPKO serves as the field contractor for the western section of the oil field, and THUMS serves as the field contractor for the eastern section. In FY 2020, THUMS produced 6,806,697 barrels of oil, while TOPKO produced 2,405,242 barrels of oil.

SHPI, the third largest oil producer in Long Beach, is the operator for the Signal Hill West Unit, Signal Hill East Unit, Signal Hill Bryant Lease, Signal Hill H&L Lease, Signal Hill B-302, Signal Hill LBA-1, Signal Hill Graner Lease Oil Fields, and for Well TC-1 on the Long Beach Oil Field. These oil fields are located in both Long Beach and Signal Hill. In FY 2020, SHPI produced a total of 477,183 barrels of oil in Long Beach.

Since the inception of Prop H through September 30, 2020, annual oil production in Long Beach has fluctuated. Production steadily declined from FY 2010 to FY 2012, and then experienced a growth period from FY 2013 to FY 2015 but has declined by 25% since then. In FY 2020, there was a decline of 6% from the prior year. See Figure 2 below for additional details on the fluctuation in annual oil production.

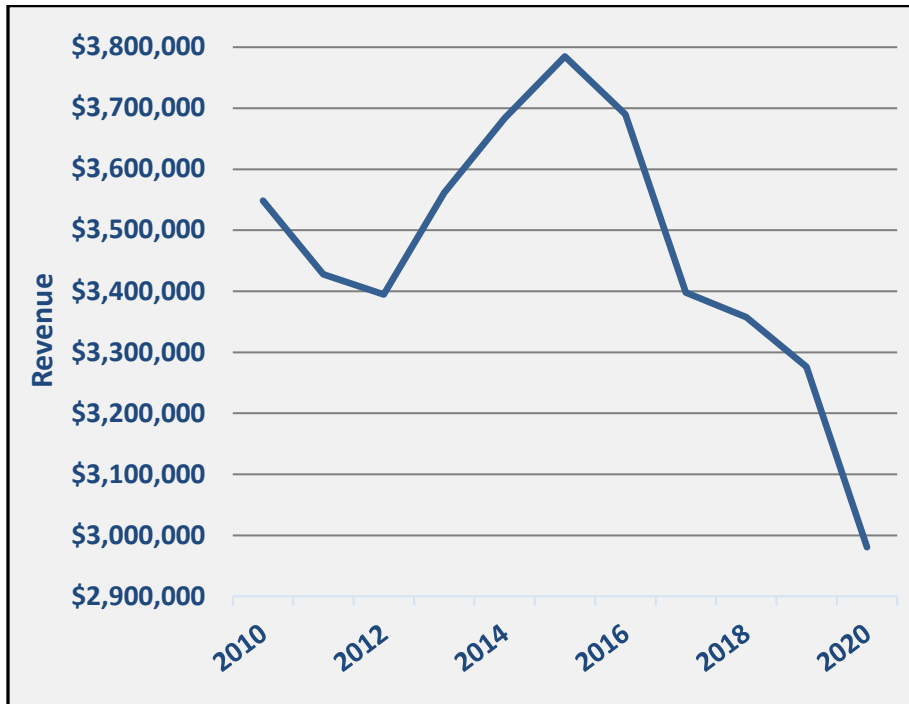
Figure 2
Annual Oil Production
FY 2010-2020



Prop H Revenues

Based on the level of production shown above, Prop H revenue received by the City shows the similar general fluctuations: overall decline from FY 2010 to FY 2012, increase from FY 2013 to FY 2015, and a decline in revenue of 21% between FY 2015 and FY 2020. In FY 2020, Prop H experienced a 9% decline from the revenue received the previous fiscal year. See Figure 3 on the next page.

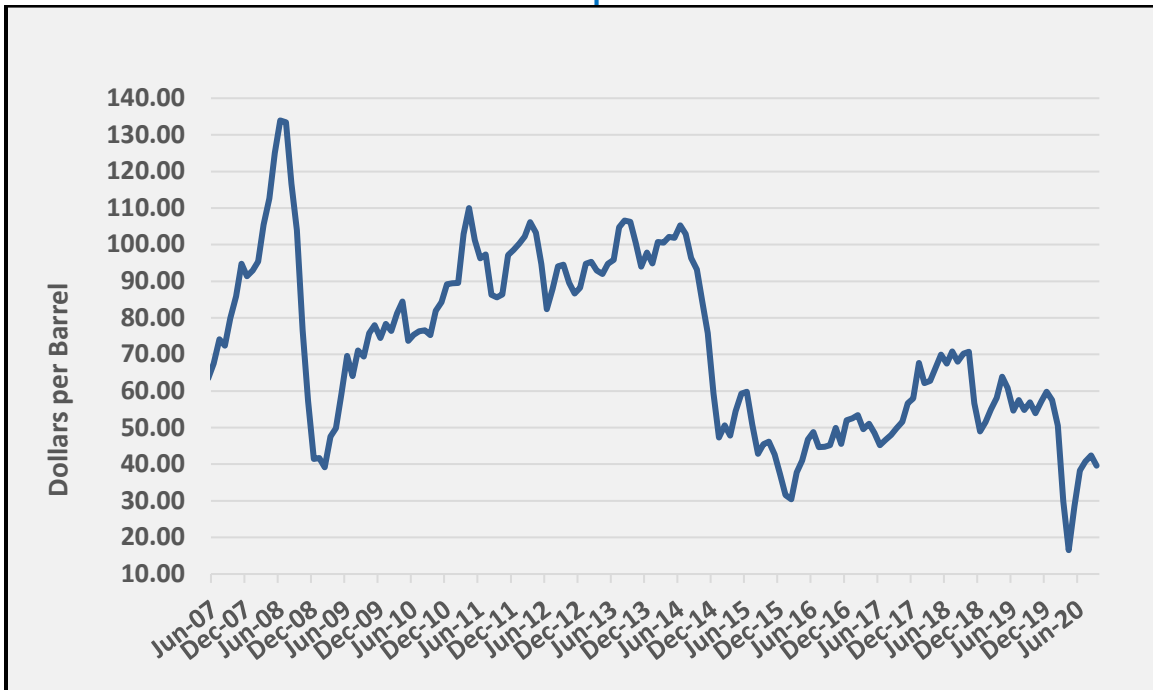
Figure 3
Prop H Annual Revenue
FY 2010-2020



Price of Oil

As shown in Figure 4 on the next page, when the special oil tax became effective in June 2007, the monthly average price of oil, based on the West Texas Intermediate (WTI) crude index, was steadily rising. In June 2008, the monthly WTI average reached a high of \$133.93 per barrel. The price of crude oil declined significantly shortly thereafter with the average monthly WTI price falling to \$39.15 per barrel in February 2009, but it increased steadily thereafter. For a four-year period, between October 2010 and September 2014, the WTI monthly average price was higher than \$80.00 per barrel, averaging \$95.81 per barrel.

Figure 4
Price of Oil
June 2007 – September 2020



However, the oil price began decreasing significantly after October 2014, reaching its previous low of \$30.39 average cost per barrel in February 2016. The average monthly WTI cost per barrel began to rise in March 2016 but began falling again in December 2019. FY 2020 began with the average monthly oil price of \$53.98. The price increased slightly at the beginning of the Fiscal Year but experienced a sharp decline all the way to a low of an average monthly oil price of \$16.52 in April 2020. Per the Municipal Code, Prop H revenue will be suspended for any month in which the average WTI index is below \$20.00 per barrel. As a result, Prop H revenue was suspended for the month of April 2020. The price then increased steadily until the end of the Fiscal Year with a small decrease to end the Fiscal Year. At the end of the Fiscal Year, September 2020, the average monthly oil price was \$39.60.

Objective, Scope & Methodology

Long Beach Municipal Code §3.80.227 requires annual independent financial audits of Prop H revenues and expenditures during each fiscal year. The four primary objectives of this audit were as follows:

1. Identify Prop H revenues received during FY 2020 and determine if funds remitted by the oil producers were properly calculated based on oil producers' reports remitted to the City;
2. Identify FY 2020 expenditures of Prop H funds and analyze whether such expenditures complied with the approved uses set forth in the Long Beach Municipal Code;
3. Determine the amount of unspent Prop H monies on deposit at September 30, 2020 that were carried over into the current fiscal year, FY 2021; and
4. Determine the status of any projects and programs funded by Prop H revenue.

The scope of our audit covers the period October 1, 2019 through September 30, 2020. We performed the following procedures during our audit:

- Obtained an understanding of internal controls surrounding the collection and recording of Prop H funds and calculated the annual change in the special tax rate based on the change in the annual average CPI. The following are the internal control components and underlying principles that are significant to the audit objectives. Management is responsible for all of these activities.
 - Risk Assessment
 - Define objective clearly to enable the identification of risks and define risk tolerances.
 - Identify, analyze, and respond to risks related to achieving the defined objectives.
 - Consider potential fraud when identifying, analyzing, and responding to risks.
 - Identify, analyze, and respond to significant changes that could impact the internal control system.
 - Control Activities
 - Design control activities to achieve objectives and respond to risks.
 - Design the entity's information system and related control activities to achieve objectives and respond to risks.
 - Implement control activities through policies.
 - Information and Communication
 - Use quality information to achieve the entity's objectives.
 - Internally communicate the necessary quality information to achieve objectives.

- Externally communicate the necessary quality information to achieve objectives.
- Monitoring
 - Establish and operate monitoring activities to monitor the internal control system and evaluate the results.
 - Remediate identified internal control deficiencies on a timely basis.
- Obtained the Oil Production Taxes Schedule from the Financial Management Department and recalculated Prop H revenues, evaluated penalties assessed, and traced payments from checks to the City's financial system. Independently confirmed approximately 97% of the reported oil production amounts with the oil producers for FY 2020.
- Identified the Prop H expenditures during FY 2020 and determined whether the expenditures were in accordance with the City's Municipal Code and identified the amount of unspent Prop H monies on deposit at September 30, 2020 that were carried over into the current fiscal year, FY 2021.
- Identified the Police and Fire Departments' plans to use Prop H monies in the future, and determined whether those plans are in accordance with §3.80.224 of the City's Municipal Code.

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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Management Comments

The Police Department, Fire Department, and Department of Financial Management agreed with the information contained in the report and had no further comments.



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