

# **DRAPER CITY**

## **Allocation of Incremental Costs to Traverse Ridge Special Service District**

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Finding and Recommendation  
For the Year Ended June 30, 2014

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Report No. 14-TRSD-8L



**OFFICE OF THE  
UTAH STATE AUDITOR**

# **DRAPER CITY**

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Finding and Recommendation  
For the Year Ended June 30, 2014

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Report No. 14-TRSD-8L

**AUDIT LEADERSHIP:**

Van Christensen, CPA, Audit Director  
Ryan Roberts, CPA, Audit Supervisor  
Jenifer Vallejos, CPA, Audit Supervisor



OFFICE OF THE  
UTAH STATE AUDITOR

**REPORT NO. 14-TRSD-8L**

April 16, 2015

Mayor Troy Walker and Draper City Council  
Draper City Hall  
1020 East Pioneer Road  
Draper, UT 84020

Dear Mayor and the City Council members:

The Office of the Utah State Auditor has investigated a complaint that Draper City (City) did not fairly charge expenses to Traverse Ridge Special Service District (District). We performed this investigation as a result of allegations received through our hotline. The results of our investigation are included in the attached findings and recommendations.

Our testwork involved reviewing the methodology used by the City to allocate incremental costs to the District for fiscal year 2014.

Our procedures were more limited than would be necessary to express an opinion on the effectiveness of the City's internal control or any part thereof. Accordingly, we do not express such an opinion. Alternatively, we have identified the procedures we performed and the findings resulting from those procedures. Had we performed additional procedures or had we made an audit of the effectiveness of the City's internal control, other matters might have come to our attention that would have been reported to you.

By its nature, this report focuses on exceptions, weaknesses, and problems. This focus should not be understood to mean there are not also various strengths and accomplishments. We appreciate the courtesy and assistance extended to us by the personnel of the City during the course of the investigation, and we look forward to a continuing professional relationship. If you have any questions, please contact me.

Sincerely,

Van Christensen, CPA  
Audit Director  
801-538-1394  
vchristensen@utah.gov

**DRAPER CITY**  
**Allocation of Incremental Costs to Traverse Ridge Special Service District**

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**DRAPER CITY**  
**Allocation of Incremental Costs to Traverse Ridge Special Service District**

FINDINGS AND RECOMMENDATIONS  
FOR THE FISCAL YEAR ENDED JUNE 30, 2014

**BACKGROUND**

The Traverse Ridge Special Service District (District) was created to pay for costs incurred by Draper City (City) for providing services such as snow removal, street lighting, and street maintenance to residents within the District.

Historically, the City provided services to the District and charged them for certain additional incremental costs. During fiscal year 2015, the City and the District came to an agreement that the District would perform the services and the City would provide funds to the District equivalent to a base level of service. Either method is acceptable; however, it may be more efficient for the City to provide the services.<sup>1</sup>

It is unusual for two local governments to impose a tax and be responsible for providing the same service to the same group of citizens. Usually services provided by a district are unique to the district's boundaries. For example, a mosquito abatement district provides abatement services for an entire area and does not supplement services provided by another government such as a county.

**FINDINGS AND RECOMMENDATIONS**

**1. NO AGREEMENT SPECIFYING COST OR REVENUE SHARING**

When the District was created, some key terms and conditions, such as how revenues or expenditures would be shared, were not clearly defined. Most individuals involved in the creation of the District are no longer serving the City or District as elected officials or

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<sup>1</sup> Without additional information defining significant terms between the City and District, and simply on the basis of fairness and equity, we believe that "incremental costs" should represent the cost of additional services beyond a base level of service rather than the entire increase of services. We base this conclusion on mirroring the principle outlined in the following statute. Regarding a special service district, *Utah Code* 17D-1-202(2)(c) states that:

*A proposed special service district may not include land that will not be benefitted by the service that the special service district is proposed to provide, unless the owner of the nonbenefitted land consents to the inclusion.*

In other words, in order for land within a district to be "benefitted" it must be provided with a basic level of service. "Consent" means a positive acknowledgment from the land owner. From our perspective, the proposition approving the tax for the District did not provide sufficient details to "consent" to forego a basic level of certain city services.

It is one thing for landowners within the District to pay a tax and decline to receive certain services from the City; however, without some type of informed consent by the District residents, it seems inequitable for them to pay a tax for specific services and yet be ineligible to receive all of those services.

## DRAPER CITY

### **Allocation of Incremental Costs to Traverse Ridge Special Service District**

#### FINDINGS AND RECOMMENDATIONS FOR THE FISCAL YEAR ENDED JUNE 30, 2014

employees. However, we were able to review various documents establishing the District or tax rate. These documents use terms such as “full cost” or “incremental cost” but do not specifically define whether the full cost or incremental cost of providing services would be charged to the District or what incremental cost means. Incremental cost could mean the cost of additional services beyond a base level of service within the District or it could be interpreted as the entire increase of City services provided within the District.

The following documents indicate which services the District will provide and how revenues or expenditures are shared with the District.

- *Resolution* – The District was created in 1999 with the adoption of a resolution by the City Council. The resolution authorized the District to provide, “...transportation, including snow removal, street lighting services, repairing and maintaining roads, and sweeping and disposal services.”
- *Proposition* – In 2001, an election was held adopting a proposition authorizing a tax levy and restricting the use of the revenue generated to, “...providing transportation, including snow removal, street lighting services, repairing and maintaining roads, sweeping and disposal services and facilities within the boundaries of the [District].”
- *Voter Information Sheet* – A voter information sheet providing notice of a special election to establish a tax twice states that the District was established to recognize the **incremental costs** of providing basic municipal services to the development within the District. The information sheet also states that, “...the District may annually impose fees and charges **to pay for all or a part** of the services to be provided by the District. (emphasis added)
- *Meeting Minutes* – Minutes from a City Council meeting held on January 31, 2012 state the services the District is authorized to provide and then state, “It has nothing to do with the differential for provision of services...In the Master Development Agreement, the city agreed to pay standard municipal services, including fire protection. Because the developer wanted to provide a higher level of service, creation of a special service was provided for.”

Because available documents regarding the creation of the District and how revenues or expenditures would be shared are vague, the concepts to be applied to a cost allocation methodology have been unclear. At the creation of this type of district, the participating entities should ensure that an agreement is in place which clearly defines significant terms.

#### **Recommendation:**

**We recommend that whenever the City creates a district or enters into an interlocal agreement the City ensures that an agreement is in place which clearly defines significant terms and the metrics to be used for revenue or expense sharing.**

## **DRAPER CITY**

### **Allocation of Incremental Costs to Traverse Ridge Special Service District**

#### **FINDINGS AND RECOMMENDATIONS FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

### **2. WEAKNESSES IN COST ALLOCATION METHODOLOGY**

Prior to the fiscal year 2015 agreement between the City and District, the City did not develop and use a reasonable cost allocation methodology that captured and quantified all costs that could be charged to the District. The City tracked and allocated some costs, others costs were tracked but not allocated, and others were not captured or quantified but were used to justify charges in excess of other allocated amounts (see finding No. 3).

Not developing a reasonable methodology combined with undefined terms and conditions has led to confusion over possible overcharging or undercharging of the District. As the service provider and fiscal agent for the District, the City was responsible for preparing and providing an accurate accounting justifying costs charged to the District.

#### **Recommendation:**

**Whenever the City chooses to provide services to the District and charge the District for the associated costs, we recommend:**

- **The City develop a reasonable methodology that accurately tracks direct costs and allocates indirect costs based upon a reasonable rate calculation.**
- **The City and District reconcile end-of-year actual costs to beginning-of-year estimates and true up any differences.**

**Whenever the City chooses to share revenue with the District we recommend:**

- **The City have a reasonable methodology for revenue sharing, such as identifying how revenues are applied across the costs of various services and the metrics used for allocating costs.**

### **3. WEAKNESSES IN COSTS ALLOCATED**

A practice inconsistently applied by the City appeared to indicate the District would be charged an incremental amount above a base level of service comparable to the cost of similar service in other parts of the City. However, we noted variances between City estimated costs and what was actually charged to the District. We include the variances noted below to illustrate discrepancies and identify areas where the District may have been overcharged or undercharged. It is not our objective to recreate an accounting of all potential charges and reasonable allocations; we simply note the deficiencies we found. As noted in finding No. 2, without a reasonable methodology that captures and quantifies relevant costs, we cannot reach a conclusion of whether the District was charged appropriately. The variances are as follows:

## **DRAPER CITY**

### **Allocation of Incremental Costs to Traverse Ridge Special Service District**

#### **FINDINGS AND RECOMMENDATIONS FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

##### ***Possible Improper Direct Charges***

- a. The City charged the District for the annual salaries and benefits of three full-time employees which the City represented was for labor costs associated with snow removal within the District. However, these three employees did not work exclusively within the District, nor was snow removal performed throughout the year. The City maintained records that tracked the hours, location (in-District vs. out-of-District), and labor rates of the snow plow drivers. The City even calculated the excess costs for the removal of snow in the District versus snow in the City using the data and applying a reasonable methodology. However, the City did not use the calculated “excess costs” when charging the District. As such, for fiscal year 2014 there was a variance of approximately \$149,000 between the City’s calculation of incremental costs of approximately \$30,000 and the amount the District was charged.

Because the incremental cost amount was readily available, the City should have known it was overcharging the District in this instance. The City’s management indicated that a comparison of the amounts was not made and that, instead, they followed the methods used since fiscal year 2008. This error may have occurred because the City did not reassess an approximation that at a previous point in time may have been reasonable. Although we did not review prior years, we assume that similar variances occurred because this method of charging the District has been used since fiscal year 2008.

- b. The City charged the District for the entire direct costs for certain materials and supplies, property damage repairs, uniforms, street light repairs, and road striping. Charging the full cost of these direct costs is not consistent with the methodology noted in a. above where an incremental amount above a base level was charged.
- c. The City provided our office with a schedule of road projects completed within the District totaling \$1,596,244 for the period 2007 through 2014. According to documents noted in finding No. 1, the City could have charged the District for some or all of these costs; however, these projects do not appear to have been charged to the District.

##### ***Possible Improper Indirect Charges***

- d. The City did not have a reasonable basis for charging the District for administrative fees based on 15% of the District’s tax revenues. The City represented that it charged the District using the same rate it charged Redevelopment Agencies; however, the City was unable to support that the 15% rate approximated actual incremental administrative charges. For fiscal year 2015, the City and District negotiated a rate of 10% of expenses for administrative costs, which will result in lower administrative costs.

## **DRAPER CITY**

### **Allocation of Incremental Costs to Traverse Ridge Special Service District**

#### **FINDINGS AND RECOMMENDATIONS FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

Allocating costs on the basis of expenses rather than revenues is more reasonable because administrative costs correlate better with expenses.

#### **Recommendation:**

**We recommend that the City:**

- **Provide a transparent accounting to interested parties.**
- **Settle any variances, as considered appropriate.**
- **Improve tracking of direct costs associated with the various services provided.**
- **Capture indirect costs and have a reasonable methodology of allocating these costs.**



April 15, 2015

Van Christensen, CPA  
Office of the Utah State Auditor  
Utah State Capitol Complex  
East Office Building, Suite E310  
Salt Lake City, UT 84114-2310

RE: Draper City's Response to Report No. 14-TRSD-8L

Dear Mr. Christensen:

The Office of the Utah State Auditor conducted an investigation into a complaint alleging Draper City "did not fairly charge expenses to Traverse Ridge Special Service District." We have reviewed the findings and submit the following response to be included in the final findings and recommendation report.

The Traverse Ridge Special Service District (the "District") was formed in 1999 for the "purpose of providing transportation, including snow removal, street lighting services, repairing and maintaining roads, [and] sweeping and disposal services ..." <sup>1</sup> Since then Draper City has provided services to the District and has charged the District for providing those services. At issue is whether Draper City has been fairly charging the District for providing services. As stated in the report, at the time the District was created there was no defined methodology for determining costs. However, the resolution creating the District does not mention anything about incremental costs, or how revenues and expenses would be shared with the City. It simply states that the District is authorized to provide the services. The City agrees that it should enter into an interlocal agreement with the District that clearly defines the terms for providing services, if the City decides it wants to offer the services to the District. The City also agrees that if it chooses to provide services to the District that it adopt a methodology for calculating and tracking direct and indirect costs.

Regarding the *Improper Direct Charges*, it is the City's position is that, while the report outlines in specificity certain charges that exceeded direct costs, the report does not outline in specificity the other direct and indirect charges that were not charged to the District, such as rent for equipment and salt storage, use of City equipment that benefitted the District, etc. As previously stated, the specificity of direct and indirect charges will be identified if the City chooses to offer its' services to the District.

Draper City appreciates the Office of the Utah State Auditor's recommendations in the report and the City may implement some suggestions in the audit as it deems necessary.

Sincerely,

Troy Walker  
Mayor

A handwritten signature in black ink, appearing to read "Troy Walker", is written over a horizontal line.

<sup>1</sup> Resolution No. 99-82 of the Draper City Council