

The San Francisco Public Utilities Commission Must Strengthen Its Controls to Ensure Accurate Reporting of Bond Expenditures

San Francisco Public Utilities Commission (SFPUC)



Why It Matters

SFPUC has deficiencies in its controls in the assignment and reporting of bond expenditures, resulting in inaccurate and incomplete reporting of millions of dollars in revenue bond spending. SFPUC partially concurs with the report's 3 recommendations, stating that its processes for completely and accurately reporting bond proceeds and related expenditures and for assigning bond expenditures are adequate and that the reporting issue identified by the audit was corrected through existing controls.



Prepared by

**OFFICE OF THE CONTROLLER
CITY SERVICES AUDITOR**

March 19, 2026



About the Controller's Office

The Controller is the chief financial officer and auditor of the City and County of San Francisco (City). We produce regular reports on the City's financial condition, economic condition, and the performance of city government. We strive to be a model for good government and to make the City a better place to live and work.

About the Audits Division

The City Services Auditor (CSA) was created in the Controller's Office through an amendment to the San Francisco Charter that voters approved in 2003. Within CSA, the Audits Division ensures the City's financial integrity and promotes efficient, effective, and accountable government by:

- Conducting performance audits of city departments, contractors, and functions to assess efficiency and effectiveness of service delivery and business processes.
- Investigating reports received through its whistleblower hotline of fraud, waste, and abuse of city resources.
- Providing actionable recommendations to city leaders to promote and enhance accountability and improve the overall performance and efficiency of city government.

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AUDIT AUTHORITY

This audit was conducted under the authority of the San Francisco Charter, Section 3.105 and Appendix F, which requires that CSA conduct periodic, comprehensive financial and performance audits of city departments, services, and activities.

STATEMENT OF AUDITING STANDARDS

We conducted this performance audit in accordance with generally accepted government auditing standards (GAGAS). 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 the findings and conclusions based on our audit objectives. The Audits Division is independent per GAGAS requirements for internal auditors.



OFFICE OF THE CONTROLLER
CITY AND COUNTY OF SAN FRANCISCO

Greg Wagner
Controller

ChiaYu Ma
Deputy Controller

March 19, 2026

San Francisco Public Utilities Commission
525 Golden Gate Avenue, 2nd Floor
San Francisco, CA 94102

Dennis Herrera
General Manager
San Francisco Public Utilities Commission
525 Golden Gate Avenue, 13th Floor
San Francisco, CA 94102

Dear Commissioners and General Manager Herrera:

The Office of the Controller, City Services Auditor (CSA), Audits Division, presents its report of the revenue bond program administered by the San Francisco Public Utilities Commission (SFPUC). The Public Utilities Revenue Bond Oversight Committee (RBOC) engaged CSA, which, in turn, engaged HKA Global, Inc. (HKA) and, as its subcontractor, Yano Accountancy Corporation (YAC), to conduct the audit.¹ The audit had as its objectives to determine whether revenue bond funds were spent in accordance with the stated purposes and permissible use of such bonds.

The audit concluded that SFPUC did not accurately assign \$106.5 million in expenditures related to wastewater revenue bonds and did not accurately report some bond expenditures.

The report includes 3 recommendations for SFPUC to strengthen its controls over assigning expenditures to bond series and reporting bond expenditures. The department's response is attached as an appendix. Although SFPUC partially concurred with the objectives of the recommendations, the department indicated that no revisions or corrective actions were necessary. The auditor's comments on SFPUC's response are provided in Appendix B.

CSA, HKA, and YAC appreciate the assistance and cooperation of all staff involved in this audit. For questions about the report, please contact me at mark.p.delarosa@sfgov.org or 628-652-9924.

Respectfully,

Mark de la Rosa
Director of Audits

cc: Board of Supervisors
Budget Analyst
Citizens Audit Review Board
City Attorney
Civil Grand Jury
Mayor
Public Library

¹ RBOC dissolved on January 1, 2025, pursuant to the San Francisco Administrative Code, Section 5A.36.



REVENUE BOND OVERSIGHT COMMITTEE

San Francisco Public Utilities Commission

PERFORMANCE AUDIT OF SELECTED REVENUE BOND EXPENDITURES

PHASE III

JANUARY 28, 2026

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1. EXECUTIVE SUMMARY

1.1 Introduction

The San Francisco Public Utilities Commission (“SFPUC”), a department of the City and County of San Francisco (“City”), has embarked on multiple construction programs in its Water, Wastewater, and Power enterprises. The San Francisco voters approved Propositions A and E in November 2002. Proposition A, among other things, authorized SFPUC to issue revenue bonds and/or other forms of revenue financing in a principal amount not to exceed \$1.628 billion to finance the acquisition and construction of improvements to SFPUC’s water system, without any further approvals. Proposition E, among other things, enabled SFPUC to issue additional revenue bonds to finance water and clean water facilities and services when authorized by a two-thirds vote of the Board of Supervisors.

In June 2018 San Francisco voters also approved Proposition A to authorize SFPUC to, among other things, issue revenue bonds to build or improve clean energy facilities, when authorized by a two-thirds vote of the Board of Supervisors. Proposition A also prohibits SFPUC from using such proceeds to finance power plants that generate electricity from fossil fuels or nuclear power. Power bonds issued before June 5, 2018, required voter approval.

SFPUC’s enterprises have forecasted expenditures of approximately \$17 billion. Actual program expenditures through June 30, 2022, are \$9.6 billion. SFPUC’s reported funding of these expenditures through June 30, 2023, includes \$8.2 billion in bond proceeds from bond issuances authorized by voter-approved Proposition A in 2018 and propositions A and E in 2002. The remaining \$1.4 billion is funded by a combination of investment earnings on unexpended proceeds, federal and state loans and grants, commercial paper, and SFPUC revenues.

In November 2002 San Francisco voters also passed Proposition P, which created Section 5A.30-5A.36 of the San Francisco Administrative Code (Administrative Code), authorizing the establishment of the Public Utilities Revenue Bond Oversight Committee (“RBOC”). RBOC’s authorities under the Administrative Code, Section 5A.31(b)(6), include the *“...independent review and evaluation of the disbursement and expenditure of the proceeds of such revenue bonds by accessing any funds set aside for this purpose...to retain outside auditors, inspectors and necessary experts to conduct such independent review...”*

RBOC had oversight over the use of all proceeds from bonds issued under the provisions of voter-approved Propositions A and E in 2002 and voter-approved Proposition A in 2018. RBOC retained the Office of the Controller’s (Controller’s) City Services Auditor (“CSA”) to conduct a performance audit of bond-funded expenditures to determine whether expenditures were allowable under bond resolutions, properly supported, and assigned or allocated to the correct project(s) within bond series, and to evaluate the effectiveness of internal control over the allowability, and assignment of expenditures.

RBOC dissolved on January 1, 2025, in accordance with the sunset provisions of the Administrative Code, Section 5A.36. In October 2024 SFPUC reported that its Audit Bureau would assume RBOC’s mission and objectives for oversight of the use of bond proceeds upon RBOC’s dissolution.

CSA engaged HKA Global, Inc. (“HKA”) and Yano Accountancy Corporation (“YAC”) collectively referred to as the “Audit Team”) to conduct a performance audit of eighteen SFPUC bond series subject to RBOC oversight over three phases. This report includes the results of our procedures for the third of the three phases.

1.2 Overall Conclusion, and Summary of Findings and Recommendations

We concluded that SFPUC’s restated reporting of expenditures Wastewater 2018 Series B bond proceeds by project has misstatements of \$106.5 million expenditures, or 53% of total expenditures of \$201 million, should have been assigned to proceeds from other funding sources and therefore questioned as unallowable uses of bond proceeds. These questioned costs include \$81.1 million of expenditures not subject to RBOC oversight.

The original reported totals to RBOC of Wastewater proceeds and related expenditures by project for each bond series had a minimum of \$98.9 million of misstatements. SFPUC prepared restated reports of Wastewater proceeds and related expenditures by project for each bond series. These restated reports include the \$106.5 million of misstatements identified above.

Professional standards promulgate that misstatements may result from error or fraud and that misstatements need not be present for deficiencies in internal control significant to the audit objectives to exist. Because of the amounts questioned as not assigned to the correct bond series, we concluded that deficiencies in internal control significant to the audit objectives exist over the reliability of reporting Wastewater proceeds and related expenditures by project for each bond series.

We also concluded that the reports of Wastewater proceeds and related expenditures by bond series should not be relied on until SFPUC re-evaluates the assignment of expenditures to bond series.

Summary of Our Findings and Recommendations

The following summarizes quantifiable questioned expenditures for the bond series in which we questioned costs as unallowable uses of bond proceeds:

Wastewater	2018 Series B
Expenditures Not Assigned to the Correct Funding Source	\$ (106.5)

Expenditures of \$106.5 Million Were Not Assigned to the Correct Funding Sources	SFPUC’s restated reports of proceeds available and related expenditures by project for each bond series include a total of \$106.5 million funded by other funding sources, including \$81.1 million of expenditures not subject to RBOC oversight. Accordingly, these expenditures were questioned for lack of adequate support.
Original Reports Included a Minimum of \$98.9 Million of Misstatements	<p>SFPUC’s original reporting of Wastewater proceeds available for expenditure, expenditures of bond proceeds and unexpended bond proceeds were improperly stated by \$98.9 million, which represented 55.0% of Wastewater 2023 Series B expenditures, and 94.6% of Wastewater 2010 Series A and B expenditures.</p> <p>SFPUC submitted restated reports, which include the \$106.5 million of total questioned expenditures, including \$81.1 million of expenditures not subject to RBOC oversight, identified above.</p>

1.3 Restriction on Use

The purpose of this performance audit is solely to evaluate SFPUC's compliance with and internal control over the allowability of expenditures under bond provisions, support for expenditures, assignment, or allocation of expenditures to correct bond series and projects within bond series. Accordingly, this performance audit is not suitable for any other purpose.

2. PARTIES INVOLVED WITH THE PERFORMANCE AUDIT

In addition to SFPUC as auditee, RBOC, CSA, and the team of HKA and YAC (referred to as the “Audit Team”) all have significant roles and responsibilities in the performance audit.

2.1 Revenue Bond Oversight Committee

In November 2002 San Francisco voters passed Proposition P, which created Section 5A.30-5A.36 of the Administrative Code, authorizing the establishment of RBOC. Under the Administrative Code, Section 5A.31(b)(6), RBOC’s authorities include the “...*independent review and evaluation of the disbursement and expenditure of the proceeds of such revenue bonds by accessing any funds set aside for this purpose...to retain outside auditors, inspectors and necessary experts to conduct such independent review....*”

RBOC had oversight over the use of all proceeds from bonds issued under the provisions of voter-approved Proposition A of June 2018 and propositions A and E of November 2002. RBOC’s work was funded by 1/20th of 1% of the gross bond proceeds of new money revenue bond issuances or sales to the extent permitted by law. RBOC used a portion of its funding to engage CSA to oversee the performance audit to determine whether SFPUC expenditures of bond proceeds were in accordance with bond provisions, adequately supported, and properly assigned or allocated to project(s) within a bond series and evaluate internal control over these expenditures.

RBOC dissolved on January 1, 2025, in accordance with the sunset provisions of the Administrative Code, Section 5A.36. In October 2024 SFPUC reported that its Audit Bureau would assume RBOC’s mission and objectives for oversight of the use of bond proceeds upon RBOC’s dissolution.

2.2 City Services Auditor

CSA is the City’s internal auditor, providing performance, financial, and compliance auditing and managing the City’s Whistleblower Program. CSA produces a wide range of audit reports and performance reports relating to the City’s revenue, spending, service delivery, and outcomes. RBOC has contracted CSA to oversee this performance audit, and CSA, in turn, has contracted HKA, with YAC as a subcontractor, to conduct the Revenue Bond Performance Audit.

2.3 The Audit Team

HKA is a global consultancy company with over 40 years of experience and has completed numerous performance audits on some of the largest and most complex programs/projects in the world. YAC is a regional CPA and consulting firm and has worked directly with the City and County of San Francisco and the San Francisco Public Utilities Commission for over 28 years, performing audits per GAGAS and other relevant auditing and assurance standards. The principals from HKA and YAC, ultimately responsible for the quality of the performance audit, worked together for several years at one of the “Big Four” audit and consulting firms.

3. THE PERFORMANCE AUDIT

3.1 Scope and Objectives

The Audit Team conducted a performance audit of capital expenditures funded by proceeds from public utility revenue bonds. Forty revenue bonds subject to RBOC oversight have funded expenditures through June 30, 2023.

The objectives of this performance audit were to determine whether expenditures from project funds were:

- Allowable under the bond resolutions, laws, and regulations,
- Properly supported,
- Assigned or allocated to the correct bond series and project(s) within a bond series, and
- Subjected to appropriate cost control measures.

Statement of Compliance With Generally Accepted Government Auditing Standards

We conducted this performance audit under 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 we have obtained sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions.

Information Not Subject to Any Performance Audit Procedures

We were not engaged to perform, and did not perform, any performance audit procedures on any budgeted or forecasted information in this report. Such information is identified as unaudited. Accordingly, our audit conclusions do not extend to such information. This is not a scope limitation of the performance audit of the six bond series identified in this report.

This Report Does Not Extend to Other Bond Series Under RBOC Oversight

This report includes our findings, recommendations and conclusions on six bond series subjected to performance audit procedures, and to any other bond series that are affected directly by our audit procedures. We were not engaged to conduct performance audit procedures on all bond series subject to RBOC oversight. Accordingly, our findings, recommendations and conclusions do not extend to all bond series. This is not a scope limitation of the performance audit of the six bond series identified in this report.

3.2 Overall Methodology

The Audit Team approached the audit in three separate stages, enabling us to develop our findings and recommendations to RBOC. These three stages encompass a high-level evaluation of each of the audit planning and survey, fieldwork, and reporting stages.

Stage 1 – Audit Planning and Survey Phase

Upon receiving notice to proceed for Phase 3, the Audit Team conducted an entrance meeting with RBOC and CSA to initiate the audit engagement. From this meeting, we established the audit objectives, methodology, information needs, and engagement timeline.

Next, the Audit Team performed a preliminary assessment on all revenue bonds subject to RBOC oversight. This assessment included an analysis of capital project expenditures funded by the various bond proceeds for the

Wastewater, Water, and Power enterprises. The Audit Team used this information to identify six bonds to include within the Phase 3 audit scope.

The Audit Team presented the preliminary bond assessment to CSA, including the six bonds selected that address the performance audit's scope and objectives.

Stage 2 – Audit Fieldwork

The Audit Team developed an audit plan using information obtained during the audit planning and survey stage. This plan served as our framework and approach for completing the audit fieldwork. The Audit Team engaged multiple SFPUC Infrastructure and SFPUC Financial Services departments to request bond documentation, capital project files, and other related documentation. Additionally, we held discussions with SFPUC department relevant to our scope and objectives.

The Audit Team's fieldwork yielded the audit evidence used to formulate our findings, conclusions, and ultimately our recommendations to RBOC.

The following summarizes the audit procedures performed to accomplish the objectives of the performance audit.

Reporting of Expenditures by Project and Bond Series

The Audit Team:

- Obtained and evaluated relevant commission resolutions, and city and SFPUC policies, procedures and practices on the assignment of project expenditures to bond series;
- Tested the mathematical accuracy of reporting expenditures by project and bond series;
- Compared total expenditures by enterprise and project as reported in SFPUC's books and records to total reported expenditures by project and bond series; and
- Compared total expenditures by project assigned to the six bond series as recorded in SFPUC's general ledger by fiscal year to reported expenditures by project by bond series.

Compliance With Procurement Policies and Procedures

The Audit Team, for selected contracts, obtained and evaluated the following:

- Relevant procurement-related policies and procedures;
- Relevant documents to communicate contract scope and timing;
- Bids and/or proposals, as applicable, submitted by contractors and/or consultants; and
- SFPUC's documentation of bid and/or proposal evaluation.

Non-Labor Expenditures

The Audit Team selected construction, consultant and other non-labor project and overhead expenditures recorded in SFPUC's general ledger and:

- Obtained payment application packages and/or other invoices supporting the expenditure recorded in the general ledger.
- Tested the mathematical accuracy of the support for the expenditure.
- Evaluated the appropriateness of the approvals for the expenditure.

Labor Expenditures

The Audit Team, for selected labor expenditures:

- Obtained the labor detail report in electronic format, which includes hours and dollars charged to projects and overhead by pay period, person, project and account;
- Summarized the labor detail report information and compared the totals to amounts recorded in the general ledger;
- Tested labor rates for selected job classifications to the applicable Salary Ordinance provisions; and
- Analyzed labor hours and dollars by job classification, project, fiscal year and person.

Reasonableness of Overhead Rates

The Audit Team:

- Summarized overhead dollars charged to selected projects by year and city department, including SFPUC, SFPW, SFMTA and all other departments; and
- Evaluated the overall reasonableness of the overhead rates charged to projects by each department.

Stage 3 - Reporting

Based on the information collected during our fieldwork, the Audit Team developed a preliminary list of observations and distributed this information for SFPUC comment. We revised our initial observations and held follow-up meetings with each department to confirm our understanding of the information further provided to us.

The Audit Team's periodically met with CSA to provide progress updates and coordinate audit fieldwork. Also, the Audit Team provided updates to RBOC during their monthly public meetings. The culmination of our audit fieldwork is represented throughout this performance audit report, including the Audit Team's findings and recommendations to RBOC.

3.3 Risk Assessment

SFPUC Finance provided the Audit Team with schedules for the Water, Wastewater, and Power enterprises, showing expenditures by bond series. The Audit Team used these schedules, along with SFPUC's general ledger, to summarize all debt-funded expenditures by project for Water and Wastewater. The Audit Team then analyzed this information to identify bonds that fit within RBOC's scope and objectives.

Attributes	
Revenue Bonds	<ul style="list-style-type: none"> • Large net proceeds available for capital expenditures • Funds used to defease commercial paper • Bonds associated with historically high-risk projects • Large spend across many projects • Significant spend on two or three projects
Capital Programs and Projects	<ul style="list-style-type: none"> • Inherent project complexities (for example, heavy civil construction and non-typical projects) • Projects with forecasted costs exceeding baseline budgets • Projects with numerous construction schedule delays • Projects managed by other city agencies

3.4 Bond Series Selected for the Performance Audit

The Audit Team selected six bond series for our performance audit from the 40 bond series subject to RBOC oversight as of June 30, 2023: three from the Wastewater Enterprise, two from the Water Enterprise, and one from the Power Enterprise.

*Table 3.1
Bonds Selected for Phase II of the Performance Audit*

Wastewater	Power	Water
2018 Series B	2021 Series A	2017 Series A
2023 Series A	2021 Series B	
2023 Series B		

We originally expected to perform audit procedures on commercial paper defeasances of Wastewater 2023 Series A and B bonds. However, since substantially all proceeds from these two bond series were expended as of June 30, 2023, our performance audit procedures were extended to include all applicable bond proceeds.

The Official Statement for each bond series identifies the amounts deposited to SFPUC’s capital projects fund and the refunding of commercial paper issued to fund capital expenditures until such time that such temporary financing is replaced with long-term bonds. Amounts in the Official Statement are adjusted for investment earnings on unexpended proceeds and other adjustments (typically adjustments to bond issuance and underwriter’s fees, commercial paper interest paid directly from the commercial paper debt service fund, and transfers to RBOC) to determine total available proceeds.

Available Proceeds, Expenditures and Unexpended Bond Proceeds

The Controller’s Accounting Policies & Procedures (“AP&P”), which apply to all city departments, state that “...issuing department periodically generates reports for the Oversight Committee...”² They also require departments receiving debt funding “...to track, in PeopleSoft or off-line, project sources and uses against actuals by fund and by project...”³ Reports required by the AP&P are prepared under the implicit assumption that all relevant AP&P policies and procedures are followed in the generation of information for these reports. We note that SFPUC prepared these required reports for RBOC only after implementing a recommendation from Phase 1 of our performance audit.

² City and County of San Francisco – Office of the City Controller, *Accounting Policies and Procedures*, September 2017, §11.7.5.2.1

³*Ibid*, §11.7.6

The following table summarizes the total available proceeds, expenditures, and unexpended proceeds by bond series for the Wastewater bond series subject to the performance audit.

Table 3.2
Available Proceeds, Expenditures
and Unexpended Proceeds by Wastewater Bond Series
(\$000)

Wastewater	2018 Series B	2023 Series A*	2023 Series B*	Total
Proceeds from Official Statements				
Capital projects fund	\$ 201,047	\$ 164,374	\$ 52,781	\$ 418,202
Commercial paper defeased	-	400,918	156,927	557,845
Subtotal proceeds from Official Statements	201,047	565,292	209,708	976,047
Post-issuance adjustments				
Investment earnings				-
Other adjustments	335	364	(20,620)	(19,921)
Subtotal post-issuance adjustments	335	364	(20,620)	(19,921)
TOTAL AVAILABLE PROCEEDS	201,382	565,656	189,088	956,126
EXPENDITURES	(201,382)	(565,656)	(179,909)	(946,947)
UNEXPENDED PROCEEDS	\$ -	\$ -	\$ 9,179	\$ 9,179

Source: Bond Series Official Statements and SFPUC Summaries of Unexpended Proceeds and Proceeds Available

The following table summarizes the total available proceeds, expenditures, and unexpended proceeds by bond series for the Power bond series subject to the performance audit.

Table 3.3
Available Proceeds, Expenditures
and Unexpended Bond Proceeds by Power Bond Series
(\$000)

Power	2021 Series A	2021 Series B	Total
Proceeds from Official Statements			
Capital projects fund	\$ -	\$ -	\$ -
Commercial paper defeased	82,710	55,005	137,715
Subtotal proceeds from Official Statements	82,710	55,005	137,715
Post-issuance adjustments			
Investment earnings			-
Other adjustments	(1,030)	(685)	(1,715)
Subtotal post-issuance adjustments	(1,030)	(685)	(1,715)
TOTAL AVAILABLE PROCEEDS	81,680	54,320	136,000
EXPENDITURES	(81,680)	(54,320)	(136,000)
UNEXPENDED PROCEEDS	\$ -	\$ -	\$ -

Source: Bond Series Official Statements and SFPUC Summaries of Unexpended Bond Proceeds

The following table summarizes the total available proceeds, expenditures, and unexpended proceeds by bond series for the Water bond series subject to the performance audit.

*Table 3.4
Available Proceeds, Expenditures
and Unexpended Bond Proceeds by Water Bond Series
(\$000)*

Water	2017 Series A
Proceeds from Official Statements	
Capital projects fund	\$ 65,500
Commercial paper defeased	60,875
Subtotal proceeds from Official Statements	126,375
Post-issuance adjustments	
Investment earnings	(117)
Subtotal post-issuance adjustments	(117)
TOTAL AVAILABLE PROCEEDS	126,258
EXPENDITURES	(126,258)
UNEXPENDED PROCEEDS	\$ 0

Source: Bond Series Official Statement and SFPUC Summaries of Unexpended Proceeds and Proceeds Available

Project Expenditures by Bond Series

The following table summarizes expenditures by project and bond series for the Wastewater bond series subject to the performance audit.

*Table 3.5
Wastewater Expenditures by Project and Bond Series
\$(000)*

Wastewater Projects	2018 Series A	2023 Series A	2023 Series B	Total
Biosolids Digester	\$ -	\$ 281,436	\$ 36,283	\$ 317,719
Repair and Replace Collection System	132,078	-	21,427	153,505
Southeast Community Center Improvement	22,667	-	84,564	107,231
Wastewater Treatment Plant Improvements	-	84,743	-	84,743
Wastewater Treatment Plant Improvements	-	64,622	-	64,622
Collection System Improvement	-	64,526	-	64,526
Stormwater Management	-	34,827	-	34,827
Collection Division Consolidation	11,752	-	945	12,697
Ocean Beach	8,730	-	14,730	23,460
Treasure Island Capital Improvements	4,000	-	9,573	13,573
Islais Creek Outfall	10,267	-	266	10,533
Sewer Improvements - Small Diameter	-	-	3,320	3,320
Outfall Assessment and Rehabilitation	-	-	1,721	1,721
Flood Resilience – Hydraulic	-	8,626	-	8,626
Program Wide Management	-	26,834	-	26,834
Commercial Paper Expenditures	11,876	-	6,264	18,140
Other Projects	13	42	817	872
TOTAL	\$ 201,383	\$ 565,656	\$ 179,910	\$ 946,949

Source: SFPUC Summary of Revenue Bond Expenditures

The following table summarizes expenditures by project and bond series for the Power bond series subject to the performance audit.

*Table 3.6
Power Expenditures by Project and Bond Series
(\$000)*

Power Projects	2021 Series A	2021 Series B	Total
Hetchy Water - Power Infrastructure	\$ 25,984	\$ 18,016	\$ 44,000
Distribution Services – Retail	43,985	27,299	71,284
Hetchy Water - Joint Project	11,711	8,303	20,014
All Other Projects		702	702
TOTAL	\$ 81,680	\$ 54,320	\$ 136,000

Source: SFPUC Summary of Revenue Bond Expenditures

The following table summarizes expenditures by project and bond series for the Water bond series subject to the performance audit.

*Table 3.7
Water Expenditures by Project and Bond Series
(\$000)*

Water Projects	2017 Series A
Calaveras Dam Replacement	\$ 73,966
HTWTP Long-Term Improvements	18,158
New Irvington Tunnel	4,793
Seismic Upgrade of BDPL at Hayward Fault Phase 2	4,345
Regional Ground Water Storage and Recovery	11,839
Habitat Reserve Program	2,350
All Other Projects	10,807
TOTAL	\$ 126,258

Source: SFPUC Summary of Revenue Bond Expenditures

Bond Expenditure Categories and Assignment to Bonds

AP&P §3.1 states in part:

“...The encumbrance of funds is an important and usually last step in any ordering or contracting process. Encumbrance is a formal commitment of funds, recorded against a department’s budget in the financial system. An encumbrance is required before an order or contract is issued, and there are very, very few exceptions...”⁴

Implementation of the encumbrance system requires the assignment of each encumbrance to one or more specific funding sources. Numerous SFPUC construction projects, to include all enterprise funds, have multiple funding sources – including those subject to RBOC oversight, and could have funding sources not subject to RBOC oversight. Because of multiple funding sources and the limitations of the City’s accounting system in place through June 30, 2017, SFPUC determined that it was impracticable to assign each encumbrance to one or more specific funding sources. Therefore, SFPUC used a first-in, first-out (“FIFO”) framework to assign encumbrances and related expenditures to funding sources and represented to us that it had obtained approvals to use the FIFO framework to assign expenditures to bond series.

The general FIFO framework is commercial paper proceeds ultimately refunded by RBOC bonds and “new money” proceeds from bond issuances are assigned to expenditures on a FIFO basis. Under this alternative practice, commercial paper proceeds refunded by later bond series would be expended earlier than new money deposited at a later date. There are exceptions, such as certain Water bond series designated to fund only specific projects.

Separate expenditure pools are established for Water, Power and Wastewater. These pools were further split into “green” and “non-green” subpools upon issuance of green and non-green bond series in 2016.

⁴ *Ibid*, §3.1

Finally, SFPUC was able find other funding source(s) for expenditures originally funded by RBOC bonds, particularly government awards. When such expenditures are identified and their funding is transferred to the other funding source(s), the deposit date of the original RBOC funding is the FIFO date for funds made available by such funding transfers.

Since SFPUC determined that strict compliance with the City’s encumbrance policies to be impracticable, we therefore considered SFPUC’s FIFO funding framework as the *de-facto* standard for evaluating the propriety of assigning project expenditures to funding sources. We did not consider funds to be available until they were received.

SFPUC informed us that it did not assign Wastewater expenditures from FY 2006-07 through FY 2018-19 to specific bond series until FY2018-19, at which time it accumulated all expenditures by project and bond series back to Wastewater 2010 Series A and B.

Bond-Funded Expenditures

As part of the audit risk analysis procedures, we summarized bond-funded expenditures by cost category identified and described below:

*Table 3.8
Project Cost Categories*

Expenditure Category	Description
Labor-related	Labor and benefits charged by CCSF employees, and related overhead on labor.
Consultants	Expenditures to consultants such as program management, project management, construction management, environmental services, specialty inspection services, systems consulting, other management consulting services.
Construction contracts	Expenditures to contractors for construction labor and materials.
Land acquisition	Expenditures for additional land.
Fees, licenses, and permits	Expenditures to federal, state, and local government agencies to comply with regulatory and other requirements.
Construction materials	Construction materials purchased directly by SFPUC.
Other allocations	Allocations from within SFPUC that are not based on labor expenditures.
Legal and related	Expenditures under the control of the Office of the City Attorney.
Commercial paper-related	Expenditures for commercial paper fees and interest.
Intra-city charges	Expenditures to other departments other than labor, benefits and related overhead, and expenditures to the Office of the City Attorney.
Transfers	Expenditures for land and buildings from other departments for use on SFPUC projects.
All other	All other non-labor expenditures not classified above.

SFPUC informed us that it started to assign Wastewater project expenditures to specific bond series in fiscal year 2018-19, including the assignment of such project expenditures incurred in all prior years. We were provided with assignments of Wastewater project costs to funding sources only at the project level, but not at the account level. These assignments are documented on spreadsheets and not in SFPUC’s general ledger. All expenditures in fiscal years 2009-10 through 2020-21 were summarized by authority (consisting of multiple projects) and the general ledger sub-fund in which they were recorded. Expenditures through June 30, 2017, were not summarized by fiscal year; summarization by fiscal year started as of July 1, 2017. All bond proceeds from all Wastewater revenue bond series used to defease commercial paper are included as a separate funding source and not assigned to the applicable bond series. Wastewater’s accounting for defeased commercial paper differs from Water’s, which assigned expenditures funded by defeased commercial paper to the applicable bond series.

The following table summarizes estimated expenditures for Wastewater 2023 Series A and B bonds, which were issued at the same time. The Biosolids Digester Project was funded with both bond series, which is allowable under the bond indenture. Accordingly, the table summarizes expenditures funded only by 2023 Series A bonds, funded only by 2023 Series B bonds, and (the Biosolids Digester Project) funded by both 2023 Series A and B bonds.

*Table 3.9
Wastewater Bond-Funded Expenditures by Expenditure Classification
(\$000)*

Expenditure Classification	2023 Series A Only	2023 Series B Only	2023 Series A or B	Total
Labor-related and consultants				
Labor-related	\$ 49,245	\$ 19,462	\$ 12,150	\$ 80,857
Consultants	47,609	15,294	29,902	92,805
Subtotal Labor-related and consultants	96,854	34,756	42,052	173,662
Construction contracts	187,204	95,428	290,297	572,929
Subtotal labor-related, consultants, and construction contracts	284,058	130,184	332,349	746,591
Other expenditures				
Fees, licenses, and permits	219	6,148	4	6,371
Construction materials	895	3	-	898
Legal and related	131	-	165	296
Intra-CCSF charges	54	455	12	521
Fund transfers	129	450	3,500	4,079
All other	2,446	3,740	2,794	8,980
Subtotal other expenditures	3,874	10,796	6,475	21,145
TOTAL EXPENDITURES	\$ 287,932	\$ 140,980	\$ 338,824	\$ 767,736

Source: SFPUC General Ledger

The \$767.8 million of total expenditures shown is \$22.2 million greater than the \$745.6 million bond-funded expenditures in Table 3.2, because of funding source changes that occur during the middle of a month. The \$22.2 million difference includes \$21.1 million due to mid-month funding changes in the Biosolids Digester Project.

The negative net transfer of program management costs reflects SFPUC's success in obtaining Government Awards and transferring the funding of expenditures from revenue bonds subject to RBOC oversight to other funding sources.

We did not summarize expenditures by classification for 2018 Series B bonds, since we found that more than 50% of the expenditures were not properly supported.

The following table summarizes Wastewater bond-funded expenditures by expenditure classification as a percentage of total expenditures (also known as "common size"):

Table 3.10
Wastewater Bond-Funded Expenditures by Expenditure Classification
as a Percentage of Total Expenditures
(\$000)

Expenditure Classification	2023 Series A Only	2023 Series B Only	2023 Series A or B	Total
Labor-related and consultants				
Labor-related	17.10%	13.80%	3.59%	10.53%
Consultants	16.53%	10.85%	8.83%	12.09%
Subtotal Labor-related and consultants	33.63%	24.65%	12.42%	22.62%
Construction contracts	65.02%	67.69%	85.68%	74.63%
Subtotal labor-related, consultants, and construction contracts	98.65%	92.34%	98.10%	97.25%
Other expenditures				
Fees, licenses, and permits	0.08%	4.36%	0.00%	0.83%
Construction materials	0.31%	0.00%	0.00%	0.12%
Legal and related	0.05%	0.00%	0.05%	0.04%
Intra-CCSF charges	0.02%	0.32%	0.00%	0.07%
Fund transfers	0.04%	0.32%	1.03%	0.53%
All other	0.85%	2.65%	0.82%	1.17%
Subtotal other expenditures	1.35%	7.66%	1.91%	2.75%
TOTAL EXPENDITURES	100.00%	100.00%	100.00%	100.00%

Source: SFPUC General Ledger

Overall construction cost percentages continue to be lower than the comparable construction cost percentages for both Power and Water Enterprise construction cost percentages due to the Water Enterprise Construction Program, and particularly WISP, being close to completion.

Table 3.11
Power Bond-Funded Expenditures by Expenditure Classification

Expenditure Classification	2021 Series A and Series B (\$000)	% Of Total
Labor-related and consultants		
Labor-related	\$ 15,857	11.56%
Consultants	33,826	24.67%
Subtotal Labor-related and consultants	49,683	36.23%
Construction contracts	68,073	49.66%
Subtotal labor-related, consultants, and construction contracts	117,756	85.89%
Other expenditures		
Fees, licenses, and permits	17	0.01%
Construction materials	3,524	2.57%
Utilities	13,850	10.10%
Legal and related	377	0.27%
Commercial paper related	706	0.51%
Intra-CCSF charges	39	0.03%
All other	844	0.62%
Subtotal other expenditures	19,357	14.11%
TOTAL EXPENDITURES	\$ 137,113	100.00%

Source: SFPUC General Ledger

Total expenditures in Table 3.11 are \$1.1 million higher than total bond-funded expenditures, as SFPUC did not specifically allocate the related project expenditures to bonds in the general ledger, and the \$1.1 million reflects mid-month cut-off between bond series, which is normal.

We note that labor-related, consultant, and construction expenditures were almost 86% of total bond-funded expenditures. The relatively high percentage of labor-related and consultant expenditures to total expenditures reflects the early phases of the Power bond-funded projects.

The following table summarizes the journal entries to transfer expenditures from the Water expenditure pool to reflect amounts funded by Water bonds subject to the performance audit:

Table 3.12
Water Bond-Funded Expenditures by Expenditure Classification

Expenditure Classification	2017 Series A	
	\$(000)	% of Total
Labor-related and consultants		
Labor-related	\$ 9,709	7.69%
Consultants	11,583	9.17%
Subtotal Labor-related and consultants	21,292	16.86%
Construction contracts		
	101,692	80.55%
Subtotal labor-related, consultants, and construction contracts	122,984	97.41%
Other expenditures		
All other	3,274	2.59%
Subtotal other expenditures	3,274	2.59%
TOTAL EXPENDITURES	\$ 126,258	100.00%

Source: SFPUC General Ledger

The high percentage of construction contract costs funded by Water 2017 Series A bonds reflects that such expenditures were made during the latter stages of the WSIP.

Identification and Evaluation of Internal Control Significant to the Audit Objectives

GAGAS requires the identification and evaluation of internal controls that are significant to the audit objectives.

AP&P states that the City uses the COSO Internal Control Integrated Framework as its internal control framework. AP&P §1.7 requires all City departments to “...maintain effective internal control systems as an integral part of their management practices...” and “...establish and maintain policies and procedures with department-specific details supplementing the framework described here... SFPUC is also required to comply with Citywide policies established by certain city offices, including but not limited to, Contract Administration, City Attorney, and Labor Standards Enforcement.

We identified the following elements of SFPUC’s system of internal controls to be significant to our audit objectives. We, therefore, evaluated these elements to the extent necessary to meet our performance audit objectives:

- Contractor/consultant/vendor selection, including bid advertisement, acceptance and evaluation, and contract award procedures
- Encumbrances
- Project cost control
- Claims and change order control process
- Allocation of program management costs to projects
- Assignment of project costs to bond series
- Reporting to Oversight Committees

Since the COSO Framework adopted by the City is an acceptable framework under GAGAS for our consideration of internal control,⁵ we evaluated the City’s design and operating effectiveness of relevant internal control against the COSO Framework. The AP&P, as updated from time to time, and the Controller’s Office communication of the AP&P’s contents to City departments and agencies, is a component of internal control. Certain AP&P requirements are identified in various sections of this report.

SFPUC also has multiple specific policies and procedures to supplement the AP&P, particularly related to contracting and project management.

Professional standards promulgate that deficiencies in internal control significant to the audit objectives may exist even though no misstatements were identified during the performance audit.

Consideration of Findings in Prior Audit Reports

GAGAS requires auditors to consider findings from prior audit projects as part of performance audit risk assessment procedures and their effect on planned performance audit procedures.

Other auditors performed the audits of the financial statements of SFPUC’s major funds as of and for the year ended June 30, 2020, in accordance with GAGAS and auditing standards generally accepted in the United States of America. Those auditors issued a report dated February 26, 2021, which identified a material weakness in internal control over financial reporting. This material weakness was a result of a bribery and corruption scheme by SFPUC’s former general manager (GM), who held this position from September 2012 to November 2020, and who was the assistant general manager (AGM) for Infrastructure from March 2003 to September 2012.⁶ The former GM was convicted of bribery and other charges in July 2023 and was sentenced to four years in prison in March 2024.

All contractor, consultant, and vendor selections for contracts subject to RBOC oversight from June 2003 to November 2020 were under the control of this individual as either GM or AGM. Expenditures on such contracts occurred after November 2020. The material weakness identified by the other auditors is also a deficiency in internal control significant to the audit objectives over the allowability of expenditures under bond resolutions and allowability or allocability to project(s) within a bond series.

Our Phase 1 performance audit report includes an observation that SFPUC did not prepare reports of unexpended bond proceeds, available proceeds and expenditures by project and bond series. We have follow-up observations and recommendations on our Phase 1 finding as they relate to bond series subject to our Phase 3 performance audit.

Our Phase 2 audit report includes an observation that SFPUC did not have adequate procedures to ensure that everyone evaluating vendor proposals had signed appropriate conflict of interest statements. SFPUC deemed it impracticable to look at ALL procurements finalized before the issuance of our Phase 2 performance audit report.

We considered all of the above in our risk analysis and determination of our performance audit procedures.

Evaluation of Misstatements

We identified misstatements in the original and corrected financial schedules provided to us. Misstatements could result from either error or fraud. GAGAS defines fraud as “...obtaining something of value through willful

⁵ GAGAS July 2018 Revision, ¶8.130.

⁶ Letter dated February 26, 2021, from KPMG LLP to the Honorable Mayor and Board of Supervisors, which includes SFPUC’s response to the finding.

misrepresentation...”⁷ An individual may obtain value, among other ways, directly through misappropriation of assets, or indirectly from fraudulent financial reporting.

⁷ *Government Auditing Standards*, July 2018 Revision, ¶8.73

4. FINDINGS

We found that SFPUC’s restated submissions of Wastewater bond proceeds available for expenditure, expenditures of bond proceeds and unexpended bond proceeds had a total of \$106.5 million of expenditures that were not assigned to the correct funding sources, including \$81.1 million of expenditures not subject to RBOC oversight. We questioned these expenditures as not having adequate support since they were not assigned to the correct funding source.

SFPUC also reported to us that its Wastewater reporting in Phases 1 and 2 excludes \$98.9 million of expenditures that should have been included. Its original Wastewater reporting, as of June 30, 2023, of the corrected amounts did not reflect the \$98.9 million of expenditures. Rather, these are included as reductions of bond proceeds. SFPUC submitted restated reports, which include the \$106.5 million of total questioned costs, and \$81.1 million of expenditures not subject to RBOC oversight.

Finding No. 1: SFPUC Restated Reports Did Not Assign \$106.5 Million of Expenditures to the Correct Funding Sources, Including \$81.1 Million of Expenditures Not Subject to RBOC Oversight

<p>Summary</p>	<p>SFPUC did not assign \$106.5 million of expenditures to the correct funding sources, including \$81.1 million of expenditures that are not subject to RBOC oversight. Since one of the audit objectives was to evaluate whether expenditures and exclusions were assigned to the correct bond series, these expenditures are not proper support for claimed expenditures.</p> <p>SFPUC asserts that it was able to use Wastewater Series 2018B proceeds to refinance expenditures made before the issuance of the bonds. We agree that SFPUC has the authority to use bond proceeds to refund previously issued commercial paper.</p> <p>However, the information provided by SFPUC to support its assertion that Wastewater 2018 Series B proceeds were used to refund commercial paper was actually support for the commercial paper ultimately being refunded by proceeds from other funding sources.</p> <p>The combination of internal control deficiencies over the preparation of reports expenditures by project for each bond series is a deficiency in internal control significant to the audit objectives. SFPUC’s internal control over financial reporting cannot be relied on to provide complete, accurate and usable Wastewater reports by bond series of expenditures of proceeds by project.</p>
<p>Criteria</p>	<p>Controller Accounting Policies & Procedures §11.7.5.2.1 requires SFPUC to provide periodic reporting to oversight committees. Controller Accounting Policies & Procedures §11.7.6.2 requires SFPUC to track bond funded sources and expenditures by project and fund.</p> <p>Controller Accounting Policies & Procedures §3.1 requires the use of encumbrance accounting in which each encumbrance must be assigned to one or more (as applicable) specific funding sources. SFPUC represented to us that strict compliance with this policy would be impracticable, so obtained approval to implement a system in which project expenditures were assigned on a first-in, first-out basis. Part of the implementation of the first-in, first-out assignment of expenditures was that commercial paper proceeds would be assigned to the funding source(s) that ultimately refunded the applicable commercial paper proceeds.</p>

	<p>The Administrative Code, Section 5A.31(b), states in part that RBOC “...shall provide oversight to ensure that: (1) The proceeds from revenue bonds authorized by the Board and/or the voters of the City are expended in accordance with the authorizing bond resolution and applicable law; (2) Bond proceeds are expended solely for uses, purposes and projects authorized in the bond resolution; and (3) Revenue bond funds are appropriately expended for authorized capital improvements so that an uninterrupted supply of water and power continues to flow to the City and to the PUC's customers...”</p> <p>The Administrative Code, Section 5A.31(c)(6), empowers RBOC to “...independent review and evaluation of the disbursement and expenditure of the proceeds of such revenue bonds by accessing any funds set aside for this purpose under Subsection (d) of this section to retain outside auditors, inspectors and necessary experts to conduct such independent review...” One of our performance audit objectives is to evaluate whether expenditures are assigned to the correct bond series and project within each bond series.</p> <p>RBOC cannot provide the oversight required by the Administrative Code, Section 5A.31(b), unless it is given complete, accurate and usable information about the reporting of bond-funded expenditures, and the assignment of expenditures to bond proceeds.</p>
<p>Observations</p>	<p>SFPUC reported expenditures of \$106.5 million of Wastewater 2018 Series B proceeds as funded by commercial paper proceeds and ultimately repaid with these bond proceeds. SFPUC asserts that it was able to use Wastewater Series 2018B proceeds to refinance expenditures made before the issuance of the bonds. We agree that SFPUC has the authority to use bond proceeds to refund previously issued commercial paper and other money used to finance capital expenditures.</p> <p>However, the documentary evidence provided by SFPUC to support the \$106.5 million of commercial paper refunded by Wastewater 2018 Series B proceeds actually provided evidence that \$81.1 million was specifically refunded by Government Awards proceeds not subject to RBOC oversight and that \$25.4 million was specifically refunded by Wastewater 2021 Series B proceeds.</p> <p>Limited Procedures on Expenditures and Reductions</p> <p>We performed only limited procedures to evaluate the expenditures and reductions to determine whether they were otherwise allowable. The performance of such limited procedures is not a scope limitation because of the adequacy of other evidence to support our observations that \$106.5 million was not assigned to the correct funding source. We did not have any further observations resulting from these limited procedures.</p>
<p>Effect</p>	<p>SFPUC’s restated reporting of Wastewater 2018 Series B expenditures had \$106.5 million of expenditures funded by other sources, so is deemed to be unallowable uses of 2018 Series B proceeds. Since these expenditures were funded by other sources, expenditures by project of the other sources also have unsupported expenditures totaling \$106.5 million. We question a minimum of \$106.5 million of expenditures as unallowable uses of proceeds. The questioned expenditures include \$81.1 million of expenditures not subject to RBOC oversight.</p> <p>It was beyond the scope of the performance audit to determine the correct assignment to bond series of these \$106.5 million of expenditures, as this would have involved the evaluation of almost \$3 billion of expenditures, and multiple bond series outside the scope of the performance audit.</p>

Cause	SFPUC did not have adequate internal controls to assign expenditures to the correct bond proceeds, a deficiency in internal control significant to the audit objectives.
Recommendations	<ol style="list-style-type: none"> 1. SFPUC should ensure it has adequate internal controls for complete and accurate of reporting expenditures by project within each bond series. 2. SFPUC should re-evaluate its assignment of expenditures to bond series and revise the assignment as applicable.

Finding No. 2: Original Reports Did Not Include \$98.9 Million of Proceeds and Expenditures

Summary	<p>SFPUC’s original reporting of expenditures by project for each Wastewater bond series was inaccurate. SFPUC submitted restated reports of expenditures by project for each bond series, which resulted in changes in the underlying support of expenditures by project for each bond series.</p> <p>Our evaluation of the restated reports identified misstatements and related questioned costs identified in previous findings. The combination of internal control deficiencies over the preparation of reports of proceeds available and related expenditures by project for each bond series is a deficiency in internal control significant to the audit objectives.</p>
Criteria	<p>The Administrative Code, Section 5A.31(b), states in part that RBOC “...shall provide oversight to ensure that: (1) The proceeds from revenue bonds authorized by the Board and/or the voters of the City are expended in accordance with the authorizing bond resolution and applicable law; (2) Bond proceeds are expended solely for uses, purposes and projects authorized in the bond resolution; and (3) Revenue bond funds are appropriately expended for authorized capital improvements so that an uninterrupted supply of water and power continues to flow to the City and to the PUC’s customers...”</p> <p>The Administrative Code, Section 5A.31(c)(6), empowers RBOC to “...independent review and evaluation of the disbursement and expenditure of the proceeds of such revenue bonds by accessing any funds set aside for this purpose under Subsection (d) of this Section to retain outside auditors, inspectors and necessary experts to conduct such independent review...”</p> <p>Controller Accounting Policies & Procedures §11.7.5.2.1 requires SFPUC to provide periodic reporting to oversight committees. Controller Accounting Policies & Procedures §11.7.6.2 requires SFPUC to track bond funded sources and uses by project and fund. RBOC cannot provide the oversight required by the Administrative Code, Section 5A.31(b), unless it is given complete, accurate and usable information about the reporting of bond-funded expenditures, and the assignment of expenditures to bond proceeds.</p>
Observations	<p>SFPUC’s reports of Wastewater bond-funded expenditures as of June 30, 2023, and all prior periods excluded \$8.9 and \$90.0 million of bond proceeds from Wastewater 2023 Series A and 2023 Series B bonds, respectively. SFPUC also excluded \$106.5 million of expenditures, which agreed to bond proceeds excluded. These expenditures were partially funded by \$50.0 million and \$54.5 million of proceeds from 2010 Series A and 2010 Series B bonds, respectively, as well as other bond series.</p>

	<p>Our observations on misstatements of expenditures of 2010 Series A and B bond proceeds are within the scope of this performance audit because they are directly associated with the misstatements of 2023 Series B proceeds available.</p> <p>SFPUC disagreed with our evaluation because the explanation for the \$98.9 million reduction of Wastewater 2023 bond proceeds is included in the footnotes of the schedule of expenditures by project and bond series. SFPUC's treatment of expenditures funded by 2010 Series A and B proceeds as reductions of 2023 Series A and B proceeds results in multiple misstatements, as explained below in the effects. The explanation of the \$98.9 million as a reduction of Wastewater 2023 Series A and B proceeds only caused misstatements of proceeds and expenditures of these two bond series and did not correct any of the misstatements in the reporting of expenditures by project and bond series of multiple prior bond series.</p> <p>SFPUC submitted restated reports of proceeds available and related expenditures by project for each bond series. We note that even though the Audit Team recommended the revision and resubmission of the Wastewater reporting, SFPUC is responsible for the completeness and accuracy of all reports, including any decision to restate any reports.</p> <p>SFPUC also reported to us that it did not assign Wastewater expenditures by project to bond series until fiscal year 2018-19. Such expenditures were incurred as far back as fiscal year 2007-08.</p> <p>The restated reports include the \$106.5 million of questioned costs identified in Finding No. 1, including \$81.1 million of expenditures not subject to RBOC oversight.</p>
<p>Effect</p>	<p>After corrections made by SFPUC, we questioned a total of \$106.5 million of expenditures assigned to the incorrect funding sources, and therefore were unallowable uses of proceeds, as more fully described in Finding No. 1. Total questioned expenditures include \$81.1 million of expenditures not subject to RBOC oversight.</p> <p>Before corrections made by SFPUC:</p> <ul style="list-style-type: none"> • \$8.9 and \$90.0 million of bond proceeds from Wastewater 2023 Series A and 2023 Series B bonds, respectively, are deemed to have been used for unallowable purposes because the expenditures supporting the total \$104.5 million of expenditures were funded by 2010 Series A and 2010 Series B bond proceeds. Total expenditures of Wastewater 2023 Series A and B bonds were also understated by \$8.9 and \$90.0 million, respectively, to match the corresponding understatement of available proceeds that were actually expended. • \$98.9 million of expenditures of Wastewater 2010 Series A and 2010 Series B bonds are deemed to be used for unallowable purposes because the expenditures supporting these amounts were funded by other bond series. Since Series 2010A and Series 2010B proceeds are deemed to be “fungible” and therefore interchangeable with each other, the misstatement was not allocated between the two series. The expenditures to support the total \$98.9 million of these expenditures were excluded from the reports of bond proceeds available for expenditure and related bond-funded expenditures. • Reporting of all other Wastewater expenditures by project for each bond series was misstated because of the improper exclusion of expenditures funded by 2010 Series A and 2010 Series B proceeds, which affected the assignment of expenditures to all subsequent bond series. Proceeds from

	<p>all Wastewater bond proceeds required reassignment to projects after the missing expenditures were included in the restated reports.</p>
<p>Cause</p>	<p>SFPUC did not have adequate internal controls to:</p> <ul style="list-style-type: none"> • Identify all expenditures subject to RBOC oversight; • Account for all bond proceeds; • Match expenditures to available proceeds; and • Prepare complete, accurate and usable reports. <p>The combination of these internal control deficiencies is a deficiency in internal control significant to the audit objectives.</p> <p>SFPUC asserted to us that it could not identify the \$98.9 million of expenditures until after the completion of Phase 2 of our performance audit and could not assert as to whether the misclassification of expenditures was due to error or fraudulent financial reporting. Accordingly, we did not determine whether the misstatement was an error or fraudulent financial reporting.</p> <p>As discussed previously, SFPUC reported in October 2024 that its Audit Bureau would assume RBOC’s mission and objectives regarding the oversight of revenue bond expenditures after RBOC’s term expired.</p>
<p>Recommendation</p>	<p>3. SFPUC should ensure it has adequate internal controls to account for all bond proceeds, and for completeness, accuracy and consistency of reporting bond proceeds and related expenditures by project by bond series.</p>

5. CONCLUSION

We met our audit objectives for the Phase 3 performance audit of capital expenditures funded by proceeds from public utility revenue bonds subject to RBOC oversight.

We found that, as of the beginning of Phase 3 of our performance audit, SFPUC did not have adequate controls over the complete and accurate reporting of proceeds available for expenditure, expenditures of bond proceeds and unexpended bond proceeds. This was evidenced by SFPUC's submission of restated reports to the Audit Team.

Even after submission of restated reports, we concluded that SFPUC had inadequate controls to assign Wastewater expenditures to the correct funding source.

Finally, we conclude that reports of Wastewater proceeds and related expenditures by bond series should not be relied upon until SFPUC re-examines its assignment of expenditures to bond proceeds.

6. APPENDIX A: DEPARTMENT RESPONSE



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January 26, 2026

Mark de la Rosa, CSA Director of Audits
City Hall, Room 476
1 Dr. Carlton B. Goodlett Place
San Francisco, CA 94102

Subject: San Francisco Public Utilities Commission (SFPUC) Response to
Phase 3 of the Revenue Bond Oversight Committee Audit

Dear Mr. de la Rosa,

We appreciate the opportunity to review and respond to the Phase 3 performance audit conducted on behalf of the Revenue Bond Oversight Committee (RBOC). SFPUC values independent oversight and remains committed to transparency, accountability, and continuous improvement in the stewardship of voter-approved revenue bond proceeds.

Management agrees that its original reporting in the biannual *Wastewater Unexpended Revenue Bond Proceeds Report* required correction. SFPUC proactively identified the matter, timely notified the audit team, and submitted revised schedules during the audit’s fieldwork. These revisions improved the presentation of bond-funded expenditures and did not identify any new expenditures, unsupported costs, or noncompliance with bond provisions.

SFPUC respectfully disagrees with several conclusions presented in the audit report, as those conclusions are not supported by the factual record, applicable bond provisions, or professional audit standards, and reflect an incomplete application of SFPUC’s debt accounting and capital financing framework.

The audit characterizes certain expenditures and reporting adjustments as “unallowable uses of bond proceeds” based solely on their assignment to a different bond series than originally described at issuance. The audit does not cite any bond provision, indenture requirement, or legal authority that would establish the questioned expenditures as ineligible for bond funding, nor does it demonstrate that the expenditures failed to meet the definition of allowable project costs. Misclassification or reallocation of expenditures between bond series for reporting purposes does not, by itself, render otherwise allowable expenditures as unallowable.

Daniel Lurie
Mayor

Joshua Arca
President

Stephen E. Leveroni
Vice President

Avni Jamdar
Commissioner

Kate H. Stacy
Commissioner

Meghan Thurlow
Commissioner

Dennis J. Herrera
General Manager

OUR MISSION: To provide our customers with high-quality, efficient and reliable water, power and sewer services in a manner that values environmental and community interests and sustains the resources entrusted to our care.



Similarly, the audit's conclusion that certain expenditures were incurred before proceeds became available does not establish noncompliance and reflects an incomplete consideration of SFPUC's capital financing practices. The audit does not address interim financing, reimbursement practices, or other mechanisms permitted by SFPUC's revenue bond covenants, nor does it evaluate eligibility of underlying project costs. Absent this context, such conclusions are not adequately supported.

SFPUC also disagrees with the conclusion that a significant internal control deficiency existed relative to the audit objectives. The audit does not identify a specific control failure or breakdown in control design or operation. To the contrary, SFPUC staff identified the reporting matter, corrected it through established processes, and provided timely and complete documentation supporting the revised reporting. Corrected reporting misstatements identified and resolved through existing controls, absent evidence of a control failure, do not support a conclusion that internal controls are deficient.

SFPUC further disagrees with the assertion that the revised reports should not be relied upon. The revised reports reflect the adjustments discussed with the audit team, are fully supported by documentation provided, and accurately reflect allowable expenditures in accordance with SFPUC's established accounting and capital financing practices, as authorized and overseen by the Controller's Office.

Throughout the audit, management and staff engaged extensively with the audit team, providing supporting documentation and analyses addressing the allowability of expenditures, reporting revisions, and internal controls. SFPUC raised concerns regarding the interpretation of its debt accounting and capital financing practices and provided information to address those concerns; however, the audit report does not reflect that context.

SFPUC remains committed to transparency and accountability in its capital programs and will continue to conduct internal review and assurance activities through its internal Audit Bureau, which is positioned to evaluate capital program financing across the full range of funding sources. SFPUC submits this response to accurately describe the matters addressed and the actions taken.

Sincerely,



Dennis J. Herrera
General Manager

cc: Ronald P. Flynn, Deputy General Manager
Nancy L. Hom, Chief Financial Officer and AGM of Business Services
Christopher Crane, Acting Audit Director

Recommendations and Responses

For each recommendation, the responsible agency should indicate in the column labeled **Agency Response** whether it concurs, does not concur, or partially concurs and provide a brief explanation. If it concurs with the recommendation, it should indicate the expected implementation date and implementation plan. If the responsible agency does not concur or partially concurs, it should provide an explanation and an alternate plan of action to address the identified issue.

Recommendation	Agency Response	CSA Use Only Status Determination*
The San Francisco Public Utilities Commission should:		
1. Ensure it has adequate internal controls to account for all bond proceeds by bond series, and for completeness and accuracy of reporting bond proceeds and related expenditures by project within each bond series.	<input type="checkbox"/> Concur <input type="checkbox"/> Do Not Concur <input checked="" type="checkbox"/> Partially Concur SFPUC partially concurs with the recommendation’s objective. Adequate internal controls to account for bond proceeds by bond series, and for the completeness and accuracy of reporting bond proceeds and related expenditures, are in place and operating effectively. The audit did not identify a control design or operating failure. No additional corrective action is required beyond existing processes.	<input type="checkbox"/> Open <input type="checkbox"/> Closed <input checked="" type="checkbox"/> Contested
2. Re-evaluate its assignment of expenditures to bond series and revise the assignment as applicable.	<input type="checkbox"/> Concur <input type="checkbox"/> Do Not Concur <input checked="" type="checkbox"/> Partially Concur SFPUC partially concurs with the recommendation’s objective. SFPUC’s assignment of expenditures to bond series is governed by long-standing accounting and capital financing practices that have been applied consistently across multiple decades of bond programs. The assignments examined during this audit were evaluated and substantiated through documentation provided, and no revisions are warranted.	<input type="checkbox"/> Open <input type="checkbox"/> Closed <input checked="" type="checkbox"/> Contested

1

2

Recommendation	Agency Response	CSA Use Only Status Determination*
<p>3. Ensure it has adequate internal controls to account for all bond proceeds, and for completeness, accuracy and consistency of reporting bond proceeds and related expenditures.</p>	<p> <input type="checkbox"/> Concur <input type="checkbox"/> Do Not Concur <input checked="" type="checkbox"/> Partially Concur </p> <p>SFPUC partially concurs with the recommendation’s objective. Internal controls supporting the completeness, accuracy, and consistency of bond proceeds reporting are in place and operating effectively. The reporting issue identified by the audit was corrected through existing controls, and no additional corrective action is necessary.</p>	<p> <input type="checkbox"/> Open <input type="checkbox"/> Closed <input checked="" type="checkbox"/> Contested </p>

3

* Status Determination based on audit team’s review of the agency’s response and proposed corrective action.

7. APPENDIX B: AUDITOR COMMENTS TO SFPUC RESPONSE

To provide clarity and perspective, we are commenting on SFPUC's response to our audit report. The boxed number below corresponds with those we have placed in the margin of SFPUC's response.

We appreciate that SFPUC acknowledged the items of concern that the audit team notes in the report. Although SFPUC partially concurs with the objectives of Recommendations 1, 2, and 3, the department effectively contested all 3 recommendations, indicating that no revisions or corrective actions were necessary. However, the auditor's findings and recommendations contained in this report remain valid as discussed in our audit report.

- 1** For Recommendations 1 and 2, as part of its reporting to RBOC, SFPUC did not assign \$106.5 million of expenditures to the correct funding sources, including \$81.1 million of expenditures funded by sources not subject to RBOC oversight. The misassigned bond expenditures were evidenced by SFPUC's submission of restated reports to the audit team. One of the audit objectives was to evaluate whether expenditures and exclusions were appropriately assigned to the correct bond series. The expenditures reviewed were not adequate to support proper expenditures under the respective bond series. A performance audit need not identify one or more specific deficiencies in design or operating effectiveness, only that internal control deficiencies exist. It is SFPUC's responsibility to determine whether the identified internal control deficiencies are design and/or operating effectiveness deficiencies.
- 2**
- 3** For Recommendation 3, we found that SFPUC did not have adequate preparation and review procedures over the complete and accurate reporting of bond expenditures to RBOC. SFPUC's original reporting of expenditures by project for each Wastewater bond series was inaccurate. SFPUC submitted restated expenditures reports by project for each bond series. However, the reports continued to contain incorrect information on the bond series under RBOC's authority. SFPUC's assertion that the "...reporting issue identified by the audit was corrected through existing controls..." is not correct – effective controls would have prevented or detected the misstatements prior to issuance of the original expenditure reports.