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# Financial slips hurt Desert Hot Springs

**Audit cites mismanagement, planning miscues led to money woes**



The entrance to Desert Hot Springs City Hall located at 65-950 Pierson Blvd. in Desert Hot Springs is shown on June 5, 2009. / Desert Sun file photo

**DESERT HOT SPRINGS** — Unrealistic projections for future revenue and management decisions that overrode financial controls contributed to the fiscal crisis in Desert Hot Springs, according to an ongoing audit of the city's budget.

The city's financial condition has deteriorated to a level that there is ongoing concern about the city's ability to continue, Kenneth Pun, of Pun & McGeady, said in a report to city leaders Tuesday.

The auditor said the city's finance department was not sufficiently involved in the budgeting process and that funds were moved from restricted accounts, such as capital or grant funds, to cover gaps in the general fund.

"It was like robbing Peter to pay Paul," said Mayor Pro Tem Russell Betts.

Pun, hired to audit the city's 2012-2013 budget, advised council members to establish a whistleblower policy and other internal controls so that rank-and-file city employees are protected if they report potential misconduct or mismanagement.

Betts and Desert Hot Springs Mayor Adam Sanchez, a council member at the time, often quarreled with former city manager Rick Daniels and then-Mayor Yvonne Parks. Betts and Sanchez claimed Daniels excluded them from key policy and financial deliberations. Daniels claimed the pair harassed him and asked for a formal investigation.

But after nine months, an outside investigator found "insufficient evidence" of workplace harassment.

Pun's analysis, Betts said, supports his contention that Daniels often overstepped his role as city manager by interfering with proper accounting processes.

Still, city officials are fairly certain that nothing illegal occurred, said Interim City Manager Bob Adams.

When reached by phone Thursday, Daniels, who left Desert Hot Springs to take the city manager job in Needles, refused to comment on anything related to Desert Hot Springs' financial situation.

One of Daniels' signature projects was the \$17.5 million construction of the city's Health and Wellness Center — a facility with a grand pool, clinical services and after-school programs — but little ongoing revenue was had to support operations and maintenance.

“The due diligence process and cash projections were not even completed before you decided to put this project on the agenda,” Pun told the council.

Adams called the decision to open the Health and Wellness Center shortsighted.

“There was no plan on how that money would come in,” he said. “There were some verbal agreements made, but they were unable to fulfill those agreements.”

There needed to be a joint-venture agreement formed with the Palm Springs Unified School District and the Coachella Valley Boys & Girls Club to help pay for the center but that never happened, Adams said.

“We were left holding the bag” and paying more than \$900,000 in yearly upkeep, which included funding the building’s use by the Boys & Girls Club, Adams said.

## **Tapping reserved funds**

Desert Hot Springs is not the only city in economic trouble that used money in restricted accounts to fill its general fund. The city of Azusa’s credit rating was downgraded in 2012 by Moody’s Investor Services and subsequently given a negative outlook by Standard & Poor’s. This occurred after a 2011 audit found that Azusa’s general fund balance was almost completely made up of funds from restricted land assets.

Desert Hot Springs Councilman Joe McKee said it is not uncommon for cities to use reserve funds in a very short-term fashion, but “the money should have been moved back rapidly.”

“There were procedures but they were overruled,” McKee said.

Pun’s audit report showed the city had a more than \$900,000 general fund deficit by July 2013.

The city’s general cash fund, which covers short-term payable responsibilities such as city employee salaries and payments to vendors, was short by more than \$560,000, Pun said.

“The city was not in compliance with its own investment policy,” Pun explained to the council.

Many of these shortages have been addressed in the current fiscal year, Adams said, and city staff is working to set up mechanisms to educate council members about their fiduciary responsibilities in making sure the city’s finances are properly managed.

The city began cost-cutting in December when city leaders, facing a more than \$6 million operational deficit and under the threat of bankruptcy, declared a fiscal emergency. City leaders hoped this legal maneuver would give them more legroom when negotiating with the city's employee unions.

Since entering a fiscal emergency, the city council has approved several cost-cutting measures, such as cutting employee salaries, including police, by more than 22 percent and reducing vendor contracts.

Various department heads also reduced spending in the 2013-2014 fiscal year, but a balanced budget has yet to be adopted for next year, said Desert Hot Springs Finance Director Amy Aguer.

Aguer previously told The Desert Sun that "optimistic speculations" led to an overestimate of revenue for the current fiscal year.

The lurching U.S. economy and a downturn in the real estate market were contributing factors, Adams explained.

"The facts speak for themselves," Adams said. "The big drop in property tax values, and subsequent loss of revenue from that circumstance, coupled with the loss of redevelopment by the governor's swipe of a pen, were significant signs of rough financial water. We lost \$3 million in annual revenues and continued operating as if nothing had happened."

According to recent estimates for the 2013-2014 fiscal year, Desert Hot Springs is projected to spend about \$16.6 million on city services while only collecting \$14.1 million in revenues. Public safety spending takes up the largest share.

Adding to the challenges that the struggling municipality faces are mounting pension liabilities that will peak in 2015 and a more than \$1 million lawsuit filed by the police union last week for back wages.

If the union wins its lawsuit, McKee said, the city will be ruined.

"This is about survival now," he said.