California Department of Resources Recycling and Recovery

California Beverage Container Recycling Fund and Related Accounts
For the Fiscal Year Ended June 30, 2016

17-3970-102
July 2018

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Final reports are available on our website at http://www.dof.ca.gov.

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Transmitted via e-mail

July 17, 2018

Mr. Scott Smithline, Director
California Department of Resources Recycling and Recovery
1001 I Street
Sacramento, CA 95814

Dear Mr. Smithline:

Final Report—California Department of Resources Recycling and Recovery, 2016 Financial Statement Audit of the California Beverage Container Recycling Fund

The California Department of Finance, Office of State Audits and Evaluations, has completed its audit of the California Department of Resources Recycling and Recovery's (CalRecycle) California Beverage Container Recycling Fund and related accounts for the fiscal year ended June 30, 2016.

The enclosed report is for your information and use. CalRecycle's response to the report finding is incorporated into this final report. CalRecycle agreed with our finding. We appreciate their assistance and cooperation during the engagement, and their willingness to implement corrective actions. This report will be placed on our website.

If you have any questions regarding this report, please contact Becky McAllister, Manager, or Mary Camacho, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

Cheryl L. McCormick, CPA
Assistant Chief, Office of State Audits and Evaluations

Enclosure

cc: Mr. Matthew Rodriquez, Secretary, California Environmental Protection Agency
Mr. Ken DaRosa, Chief Deputy Director, California Department of Resources Recycling and Recovery
Mr. Tom Estes, Deputy Director, Administration, Finance, and Information Technology Services, California Department of Resources Recycling and Recovery
Mr. Adam Tauber, Interim Assistant Director, Division of Recycling, California Department of Resources Recycling and Recovery
Ms. Sarah Keck, Chief Financial Officer, Fiscal Services Branch, California Department of Resources Recycling and Recovery
Ms. Josephine Urban, Branch Chief, Audits Office, California Department of Resources Recycling and Recovery
Ms. Jane Hayes, Chief Accounting Officer, Accounting Section, California Department of Resources Recycling and Recovery

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Executive Summary

The California Department of Finance, Office of State Audits and Evaluations, performed an audit of the California Beverage Container Recycling Fund (Fund) and related accounts, administered by the California Department of Resources Recycling and Recovery, in accordance with Public Resources Code 14537. The objectives of our audit were to:

- Express an opinion on the *Balance Sheet* and *Statement of Revenue, Expenditures, and Changes in Fund Balance* of the Fund and related accounts for the fiscal year ended June 30, 2016.

- Verify that the financial statements were prepared on the basis of accounting prescribed by the California State Administrative Manual, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

- Report on internal control and compliance weaknesses, and provide recommendations for improving controls over operations of the Fund and related accounts.

Audit Results

- The aforementioned financial statements are fairly presented for the fiscal year ended June 30, 2016 in accordance with a statutory basis of accounting.

- A significant deficiency was identified in the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of the Financial Statements Performed in Accordance with *Government Auditing Standards*, which is included in this report.

This report is intended solely for the information and use of the Fund's and related accounts' management, and is not intended to be, and should not be, used by anyone other than the specified parties. However, this report is a matter of public record and its distribution is not limited.

INDEPENDENT AUDITOR'S REPORT

Mr. Scott Smithline, Director
California Department of Resources Recycling and Recovery
1001 I Street
Sacramento, CA 95814

We have audited the accompanying financial statements (statutory basis) of the governmental activities of the California Beverage Container Recycling Fund (Fund) and related accounts as administered by the California Department of Resources Recycling and Recovery (CalRecycle). The financial statements comprise the Balance Sheet (statutory basis) as of June 30, 2016, the related Statement of Revenue, Expenditures, and Changes in Fund Balance for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with a statutory basis of accounting described in Note 1B. This includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

The California Department of Finance (Finance) and CalRecycle are both part of the State of California's Executive Branch. As required by various statues within the California Government Code, Finance performs certain management and accounting functions.

Under *Government Auditing Standards*, performance of these activities creates an organizational impairment with respect to independence. However, Finance has developed and implemented sufficient safeguards to mitigate the organizational impairment so reliance can be placed on the work performed.

We believe that the audit evidence we obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities of the Fund and related accounts as of June 30, 2016, and the respective changes in financial position for the year then ended, in accordance with a statutory basis of accounting described in Note 1B.

Emphasis of Matter

As described in Note 1B, these financial statements were prepared on the basis of accounting prescribed by the California State Administrative Manual (SAM), which is a basis of accounting other than accounting principles generally accepted in the United States of America, to meet the requirements of Public Resources Code section 14537, and to present financial information for the Fund and related accounts only. Also as discussed in Note 1B, the financial statements are not intended to present the financial position of CalRecycle or the State of California as of June 30, 2016, or the results of operations or changes in their financial position for the year then ended.

Our opinion is not modified with respect to these matters.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 19, 2018, on our consideration of CalRecycle's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering CalRecycle's internal control over financial reporting and compliance.

Restriction on Use

Our report is intended solely for the information and use of the Fund's and related accounts' management, and is not intended to be, and should not be, used by anyone other than the specified parties. However, this report is a matter of public record and its distribution is not limited.

Original signed by:

Cheryl L. McCormick, CPA
Assistant Chief, Office of State Audits and Evaluations

April 19, 2018

California Department of Resources Recycling and Recovery
California Beverage Container Recycling Fund and Related Accounts
As of June 30, 2016

	California Beverage Container Recycling Fund (0133)	Glass Processing Fee Account (0269)	Penalty Account (0276)	Bimetal Processing Fee Account (0277)	PET[1] Processing Fee Account (0278)
Assets					
Cash and Pooled Investments	$200,224,596	$11,358,294	$5,223,609	$18,615,957	$13,728,964
Receivables	191,995,433	1,586,332	383,363	385,713	1,210,606
Due From Other Funds or Appropriations	26,546,064	20,512	65,154	24,768	20,670
Expense Advances	45,252	-	-	-	-
Prepayments to Other Funds or Appropriations	79,861	-	-	-	-
Total Assets	**$418,891,206**	**$12,965,138**	**$5,672,126**	**$19,026,438**	**$14,960,240**
Liabilities					
Accounts Payable	$121,865,415		-	-	
Due to Other Funds or Appropriations	2,878,451	$5,109,563	$116,851	$60,881	$3,685,068
Due to Local Government	14,193,214	-	-	-	-
Due to Other Government Entities	192,584	-	-	-	-
Uncleared Collections	7,006,064	-	-	-	-
Total Liabilities	**146,135,728**	**5,109,563**	**116,851**	**60,881**	**3,685,068**
Fund Balance					
Deferred Payroll	2,304,499	-	58,031	-	-
Reserved for Encumbrances	11,549,617	-	3,014	-	-
Contingency Reserve for Economic Uncertainties	258,901,362	7,855,575	5,494,230	18,965,557	11,275,172
Total Fund Balance	**272,755,478**	**7,855,575**	**5,555,275**	**18,965,557**	**11,275,172**
Total Liabilities and Fund Balance	**$418,891,206**	**$12,965,138**	**$5,672,126**	**$19,026,438**	**$14,960,240**

The accompanying notes are an integral part of this statement.

[1] Polyethylene Terephthalate (PET)

STATEMENT OF REVENUE, EXPENDITURES, AND CHANGES IN FUND BALANCE—STATUTORY BASIS

California Department of Resources Recycling and Recovery
California Beverage Container Recycling Fund and Related Accounts
For the Fiscal Year Ended June 30, 2016

	California Beverage Container Recycling Fund (0133)	Glass Processing Fee Account (0269)	Penalty Account (0276)	Bimetal Processing Fee Account (0277)	PET Processing Fee Account (0278)
Revenue					
Fees	$1,280,482,730	$6,921,493	-	$1,352,398	$6,389,644
Interest	457,029	54,324	$22,750	75,196	34,667
Miscellaneous Revenue	3,472,256	28	-	774	
Penalties	32,374	-	453,331	-	-
Total Revenue	**1,284,444,389**	**6,975,845**	**476,081**	**1,428,368**	**6,424,311**
Expenditures					
Payments to Recyclers, Processors, and Manufacturers	1,080,245,181	61,435,420	-	95,879	39,827,240
Handling Fee Payments	51,296,978	-	-	-	-
Local Conservation Corps Grants	9,021,020	-	-	-	-
Beverage Container Recycling Grants	836,236	-	-	-	-
Curbside Program Payments	14,892,457	-	-	-	-
Payments to Cities and Counties	10,499,728	-	-	-	-
Quality Incentive Payments	10,253,464	-	-	-	-
Plastic Market Development Payments	9,997,047				
Other Grants	52,396	-	-	-	-
Administrative Support	43,096,226	2,011	742,316	2,011	2,011
Total Expenditures	**1,230,190,733**	**61,437,431**	**742,316**	**97,890**	**39,829,251**
Revenues Over(Under) Expenditures	**54,253,656**	**(54,461,586)**	**(266,235)**	**1,330,478**	**(33,404,940)**
Other Financing Sources (Uses)					
Operating Transfers In	-	51,500,368	-	-	42,693,586
Refunds to Reverted Appropriations	80,584				
Operating Transfers Out	(94,193,954)	-	-	-	-
Total Other Financing Sources (Uses)	(94,113,370)	51,500,368	-	-	42,693,586
Fund Balance July 1, 2015	**312,615,192**	**10,816,793**	**5,821,510**	**17,635,079**	**1,986,526**
Net Change in Fund Balance	(39,859,714)	(2,961,218)	(266,235)	**1,330,478**	9,288,646
Prior-Period Adjustments	-	-	-	-	-
Fund Balance June 30, 2016	**$272,755,478**	**$7,855,575**	**$5,555,275**	**$18,965,557**	**$11,275,172**

The accompanying notes are an integral part of this statement.

California Department of Resources Recycling and Recovery
California Beverage Container Recycling Fund and Related Accounts
For the Fiscal Year Ended June 30, 2016

NOTE 1 Definition of Reporting Entity and Summary of Significant Accounting Policies

A. Definition of Reporting Entity

CalRecycle brings together the state's recycling and waste management programs. Through landmark initiatives, such as the Integrated Waste Management Act and the Beverage Container Recycling and Litter Reduction Act, California works toward a society that uses less, recycles more, and takes resource conservation to higher levels.

The California Beverage Container Recycling Program (Program) is comprised of the Fund and related accounts. The Program was created with the passage of the California Beverage Container Recycling and Litter Reduction Act of 1986 (Act), Chapter 21, Statutes of 2009 (Senate Bill 63), and places the administration of the Act with CalRecycle.

Pursuant to the Act, the legislative intent is to:

- Reach a statewide recycling goal of 80 percent for each container type.
- Reduce the beverage container component of litter in the state.
- Make redemption and recycling convenient to consumers.
- Create and maintain a marketplace where it is profitable to establish sufficient recycling centers and locations to provide consumers with convenient recycling opportunities.

The Act requires beverage distributors to make redemption payments and beverage manufacturers to pay processing fees based on the number of beverage containers sold in the state. Redemption payment revenues are used to pay processor claims for the refund value of the beverage containers purchased from recyclers in the state and the related administrative support costs and Program activities as identified in the Act as follows:

- Handling fee payments to supermarket site recycling centers
- Curbside program payments to curbside recycling program operators
- Litter abatement and recycling activity grants
- Payments to cities and counties for beverage container recycling and litter abatement activities
- Recycling and litter reduction program payments in the form of grants

- Quality incentive payments for empty beverage containers
- Market development grants
- Recycling incentive payments
- Market development payments for empty plastic beverage containers

Processing fee revenues are used to pay recyclers as “processing payments” to cover their recycling costs.

B. Basis of Presentation—Fund Financial Statements

The Fund and related accounts are classified as Other Governmental Cost Funds, which are used to account for revenues restricted by law for specified purposes.

The Program’s activities are accounted for in five separate special funds in the California State Treasury:

1. California Beverage Container Recycling Fund (Fund 0133)
2. Glass Processing Fee Account, Beverage Container Recycling Fund (Fund 0269)
3. Penalty Account, Beverage Container Recycling Fund (Fund 0276)
4. Bimetal Processing Fee Account, Beverage Container Recycling Fund (Fund 0277)
5. PET Processing Fee Account, Beverage Container Recycling Fund (Fund 0278)

The financial statements present information of the financial activities of the Program funds only, and do not represent all of the financial activities of CalRecycle or the State of California as of June 30, 2016.

C. Measurement Focus and Basis of Accounting—Statutory Basis

The Fund and related accounts financial statements are prepared using a current financial resources measurement focus. This measurement focus concentrates on transactions that increase or decrease resources available for spending in the near future. Accordingly, non-current or long-term assets and liabilities are not presented in the accompanying financial statements; instead, these items are presented in the notes when applicable.

The Fund and related accounts financial statements are presented using the modified accrual basis of accounting (statutory basis). The statutory basis of accounting is presented in accordance with state laws and state accounting procedures prescribed by SAM, which is a basis of accounting other than generally accepted accounting principles (GAAP). The significant differences from GAAP are as follows:

- *Accounts Payable* – The Fund acts as the main fund for CalRecycle and includes Accounts Payable that belong to other funds and appropriations, which are offset with Due To Other Funds or Appropriations in the related accounts, as detailed in Note 4. This is to ensure the fund balance for the

Fund is not overstated on the balance sheet because of the related account transactions. Under GAAP, liabilities that will consume current financial resources of the fund responsible for payment are presented in that fund's balance sheet.

- *Fund Balance Categorization* – The Fund Balance in the financial statements are presented in "reserve" categories according to their specified purposes. Under GAAP, the fund balance of the Fund would be classified as "restricted" due to enabling legislation.

- *Deferred Payroll* – Control section 12.45 of the Budget Act deferred the June 2016 payroll expense to July 2016. Under GAAP, payroll expenses are recognized in the period in which the government receives the employee services.

- *Encumbrances* – Encumbrances at year-end are excluded from liabilities and expenditures and are established as *Reserved for Encumbrances* in the fund balance. Under GAAP, encumbrances are also excluded from liabilities and expenditures, but are not established as a separate reserve in the fund balance.

- *Compensated Absences* – Vacation, annual, sick and other leave are expensed as personal services cost when used. Under GAAP, compensated absences for other than sick leave should be recognized as expenditures when the benefits are earned by the employees.

D. Budget and Budgetary Control

The accounting policies of CalRecycle conform to SAM and are based on the state's budgetary provisions. Program funds not related to administrative support are continuously appropriated without regard to fiscal year. These program funds include payments to recyclers, processors, and manufacturers; handling fees; local conservation corps grants; beverage container recycling grants; curbside program payments; payments to cities and counties; quality incentive payments; plastic market development payments; and other grants. Management is responsible for exercising budgetary control to ensure available amounts are not overspent. In addition, the State Controller's Office (SCO) is responsible for statewide appropriation control and does not allow expenditures in excess of authorized appropriations.

E. Investment Basis and Allocation of Investment Income

Investments consist of cash in excess of current needs on deposit in the Surplus Money Investment Fund (SMIF). The Fund and related accounts participate in the State of California's Pooled Money Investment Program, whereby cash on deposit in the State Treasury determined to be in excess of immediate needs are transferred to the SMIF for investment purposes. All earnings from investments are apportioned to the contributing fund as provided in Government Code. Participant's shares are valued on an amortized cost basis, which approximates fair value. Because the differences between amortized cost and fair value are not material, no adjustment for this has been made in the financial statements.

Deposits in SMIF are recorded in the accounting records as overseen by SCO. CalRecycle made the appropriate entries to record the ending balances of

Deposits in SMIF to be in agreement with SCO per the reconciliation requirements in SAM. Therefore, the Cash and Pooled Investments line item includes the following balances of Deposits in SMIF as recorded in the SCO Fund Reconciliation Report dated June 30, 2016:

FUND	JUNE 30, 2016
0133	$156,995,000
0269	11,138,000
0276	5,221,000
0277	18,605,000
0278	13,694,000

F. Accounts Receivable

Receivables for the funds primarily consist of year-end estimated beverage container redemption fees and processing fees to be collected in the following year. Other receivable balances include, but are not limited to, penalties and interest.

G. Accounts Payable

Payables include, but are not limited to, year-end estimated refund values, processing fees, administrative fees and handling fees to vendors, various grants and incentive payments, and administrative costs to be paid in the following fiscal year. It also includes accruals related to program expenses claimed, but not yet paid at fiscal year-end.

H. Fund Balance

The Fund Balance is the excess of a fund's assets over its liabilities. The Fund Balance increases during a fiscal period when receipts exceed disbursements. Conversely, the Fund Balance decreases during a fiscal period when disbursements exceed receipts. Part or all of the Fund Balance may be reserved as a result of law or statutory basis of accounting. Reserves represent those portions of the Fund Balance that are legally segregated for specific uses. The Fund Balance as of June 30 for each year has been categorized as follows:

- *Deferred Payroll* - Represents the amount of June 2016 payroll expenditures recognized in July 2016 per Control Section 12.45 of the Budget Act.
- *Reserved for Encumbrances* - Represents a portion of Fund Balance segregated for expected expenditures.
- *Contingency Reserve for Economic Uncertainties* - Represents the unappropriated balances of the Fund and related accounts as of June 30, 2016 that is available for appropriation the following fiscal year.

I. Revenue

Revenue consists of redemption payments and processing fees imposed on the sale or transfer of California Redemption Value (CRV) eligible beverage containers, other than a refillable beverage container in the state or imported into the state, interest income earned on funds deposited in SMIF, penalties, and unclaimed checks escheated to the issuing fund. Revenues are recorded when they become measurable and available to finance expenditures of the current period. Accrual of revenue occurs for transactions that transpired as of the last day of the fiscal year, and the due date for the revenue is within 12 months of the end of the fiscal year.

J. Expenditures

Expenditures are recorded when the related liability is incurred. Expenditures include the following components:

- *Payments to Recyclers, Processors, and Manufacturers* – Includes reimbursements to recycling centers of CRV paid to consumers when they return empty beverage containers to certified recycling centers.
- *Handling Fee Payments* – Subsidies from CalRecycle to convenience zone recyclers to promote a wider geographical dispersal than would be possible if unassisted.
- *Local Conservation Corps Payments* – Payments to certified community conservation corps that are designated by a city or county to perform litter abatement or recycling activities.
- *Curbside Program Payments* – Payments to curbside programs to expend on recycling efforts.
- *Payments to Cities and Counties* – Payments for beverage container recycling and litter clean-up activities.
- *Quality Incentive Payments* – Payments to improve the quality of glass material going to processors.
- *Plastic Market Development Payments* – Payments to improve the quality of plastic material from a processor to an end user manufacturer producing product in California.
- Other various expenditures including administrative support costs.

K. Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported in the assets and liabilities, disclosure of the contingent assets and liabilities, and the reported amounts of revenue and expenses during the reporting period.

NOTE 2 Investments

For disclosures related to investment policy and related investment risk categories, see the State of California Comprehensive Annual Financial Report.

NOTE 3 Accounts Receivable

A summary of receivables at June 30, 2016 by fund and type is provided in Table 1:

Table 1: Accounts Receivable, June 30, 2016	
Fund 0133:	
Beverage Container Redemption Fees - CRV	$ 190,964,597
Abatements	1,030,836
Total Fund 0133 Receivables	$ 191,995,433
Fund 0269:	
Beverage Container Redemption Fees – Processing Fees	$ 1,586,332
Total Fund 0269 Receivables	$ 1,586,332
Fund 0276:	
Penalty Assessments	$ 383,363
Total Fund 0276 Receivables	$ 383,363
Fund 0277:	
Beverage Container Redemption Fees – Processing Fees	$ 385,713
Total Fund 0277 Receivables	$ 385,713
Fund 0278:	
Beverage Container Redemption Fees – Processing Fees	$ 1,210,606
Total Fund 0278 Receivables	$ 1,210,606

NOTE 4 Due From/To Other Funds or Appropriations

SCO requires departments to identify the intergovernmental receivable and payable balances that represent amounts due from other state funds or appropriations to the Fund and related accounts and amounts due from the Fund and related accounts to other state funds.

The ending balances of Due From/To Other Funds or Appropriations accounts are displayed in Tables 2 and 3 on the following page:

Table 2: Due From Other Funds or Appropriations, June 30, 2016	
Fund 0133:	
Deferred Payroll	$ 2,304,499
Tire Recycling Management Fund (0226)	5,780,950
Glass Processing Fee Account (0269)	5,109,563
PET Processing Fee Account (0278)	3,685,068
Integrated Waste Management Fund (0387)	5,295,270
Various Other Funds or Appropriations	4,370,714
Total Due From Other Funds or Appropriations	$ 26,546,064
Fund 0269:	
California Beverage Container Recycling Fund (0133)	$ 1,588
Surplus Money Investment Fund	18,924
Total Due From Other Funds or Appropriations	$ 20,512
Fund 0276:	
Deferred Payroll	$ 58,031
Surplus Money Investment Fund	7,123
Total Due From Other Funds or Appropriations	$ 65,154
Fund 0277:	
Surplus Money Investment Fund	$ 24,768
Total Due From Other Funds or Appropriations	$ 24,768
Fund 0278:	
California Beverage Container Recycling Fund (0133)	$ 1,200
Surplus Money Investment Fund	19,470
Total Due From Other Funds or Appropriations	$ 20,670

Table 3: Due To Other Funds or Appropriations, June 30, 2016	
Fund 0133:	
General Fund (0001)	$ 898,287
Glass Processing Fee Account (0269)	1,588
PET Processing Fee Account (0278)	1,200
Various Other Funds or Appropriations	1,977,376
Total Due To Other Funds or Appropriations	$ 2,878,451
Fund 0269:	
California Beverage Container Recycling Fund (0133)	$ 5,109,563
Total Due To Other Funds or Appropriations	$ 5,109,563
Fund 0276:	
California Beverage Container Recycling Fund (0133)	$ 116,851
Total Due To Other Funds or Appropriations	$ 116,851
Fund 0277:	
California Beverage Container Recycling Fund (0133)	$ 60,881
Total Due To Other Funds or Appropriations	$ 60,881
Fund 0278:	
California Beverage Container Recycling Fund (0133)	$ 3,685,068
Total Due To Other Funds or Appropriations	$ 3,685,068

NOTE 5 Transfers

Legally authorized transfers of money collected by one fund to another fund are reported as Operating Transfers and are accounted for as reductions or increases in Fund Balance.

Operating Transfers Out represents the following items:

- Pursuant to Public Resources Code (PRC), Section 14581 (c)(5)(A), CalRecycle shall expend the amount necessary to pay the processing payment established pursuant to PRC Section 14575.
    - Transfers Out of Fund 0133 to the Glass Processing Fee Account (Fund 0269) amounted to $51.5 million.
    - Transfers Out of Fund 0133 to the PET Processing Fee Account (Fund 0278) amounted to $42.7 million.

NOTE 6 Significant Effects of Subsequent Events

The following are significant contingencies in Fund 133 that will not be recognized in its financial statements until actually realized:

On August 26, 2016, a final audit found Wal-Mart Stores, Inc. (Wal-Mart) underpaid CalRecycle $7.3 million in unpaid CRV, processing fees, and interest for the period of April 1, 2011 through March 31, 2014. Wal-Mart accepted the audit findings and reached an agreement with CalRecycle to pay in part, through an offset on refunds due to Wal-Mart. In September 2016, Wal-Mart paid the difference between the finding amount and offset amount to CalRecycle, with the offset completed in December 2016.

During the fiscal year ending June 30, 2016, an administrative accusation for restitution and penalties was pending against Mission Fiber Group, et. al. (the respondents). A final administrative decision was issued in June 2014 ordering the respondents to pay CalRecycle $32.7 million in restitution and $18.7 million in civil penalties. Several of the respondents have filed a civil action to overturn the decision, which is currently pending. A hearing was held on October 27, 2016 on CalRecycle's Demurrer to the third amended petition. CalRecycle's motion was granted and the Administrative Decision is now final. The matter has been referred to the Attorney General's Office for collection.

On April 28, 2016, an administrative accusation for restitution and penalties was filed against California Waste Solutions for $12.4 million for payments made between April 1, 2011 and April 30, 2014 that were based upon falsified information and $311,000 in civil penalties. No hearing date has been set.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Mr. Scott Smithline, Director
California Department of Resources Recycling and Recovery
1001 I Street
Sacramento, CA 95814

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements (statutory basis) of the governmental activities of the California Beverage Container Recycling Fund (Fund) and related accounts as of and for the year ended June 30, 2016 and the related notes to the financial statements, which collectively comprise the Fund's and related accounts' financial statements and have issued our report thereon dated April 19, 2018.

The California Department of Finance, Office of State Audits and Evaluations (Finance) and the California Department of Resources Recycling and Recovery (CalRecycle) are both part of the State of California's Executive Branch. As required by various statues within the California Government Code, Finance performs certain management and accounting functions. Under *Government Auditing Standards*, performance of these activities creates an organizational impairment with respect to independence. However, Finance has developed and implemented safeguards to mitigate the organizational impairment so reliance can be placed on the work performed.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered CalRecycle's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of CalRecycle's internal control. Accordingly, we do not express an opinion on the effectiveness of CalRecycle's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, we identified one significant deficiency in internal control described below.

Finding 16-01: Year-End Accrual Process Needs Improvement

Condition: Although CalRecycle performed an analysis comparing actual expenditures and revenues to accrual amounts, it did not adjust its financial statements or contact SCO for instructions regarding the material differences it identified subsequent to fiscal year-end. These material differences were corrected in the financial statements referenced in the first paragraph of this report.
Criteria: The California State Administrative Manual (SAM) section 7981, states departments will periodically review their expenditures and income accruals. After issuing its year-end financial statements, if departments determine there are material differences between amounts accrued as of June 30 and subsequent events relating to prior year funds, it will immediately contact SCO for instructions. Materiality is defined, for this purpose, as net changes greater than $100,000.
Cause: CalRecycle's year-end accrual process did not include adjusting its financial statements for material differences between accruals and actual amounts, or contacting SCO for instructions when material differences were identified subsequent to fiscal year-end.

Effect: Comprehensive year-end accruals enable more accurate preparation of annual financial statements. Prior to their correction, the net impacts of this finding were as follows:

Fund	Asset*	Liability*	Revenue*	Expenditure*
133	($17,453,592)	-	($17,453,592)	-
269	($ 434,913)	($ 266,833)	($ 434,913)	($ 266,833)
276	$ 1,136,993	-	$ 1,136,993	-
278	$ 208,651	$ 850,560	$ 208,651	$ 850,560

* Amounts in parenthesis represent understatements.

Recommendation: Develop and implement a methodology for determining whether differences greater than $100,000 exist between amounts accrued and subsequent events. After year-end, CalRecycle should adjust its financial statements if there are material differences between amounts accrued as of June 30 and subsequent events related to the prior year, and contact SCO for further instructions, as required by SAM.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether CalRecycle's financial statements are free of material misstatement, we performed tests of compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Original signed by:

Cheryl L. McCormick, CPA
Assistant Chief, Office of State Audits and Evaluations

April 19, 2018

California Environmental Protection Agency Edmund G. Brown Jr., Governor

CalRecycle

DEPARTMENT OF RESOURCES RECYCLING AND RECOVERY

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July 13, 2018

Ms. Cheryl McCormick
Assistant Chief, Office of State Audits and Evaluations
Department of Finance
915 L Street
Sacramento, CA 95814

Dear Ms. McCormick:

Thank you for the opportunity to review and comment on the June 19, 2018, Financial Statement Draft Audit Report for the California Beverage Container Recycling Fund for the fiscal year ended June 30, 2016. The Department of Resources Recycling and Recovery (CalRecycle) concurs with the results of the audit, and has addressed the following finding:

Finding 16-01: Year-End Accrual Process Needs Improvement

Condition:

Although CalRecycle performed an analysis comparing actual expenditures and revenues to accrual amounts, it did not adjust its financial statements or contact SCO for instructions regarding the material differences it identified subsequent to fiscal year-end. These material differences were corrected in the financial statements referenced in the first paragraph of this report.

Recommendation:

Develop and implement a methodology for determining whether differences greater than $100,000 exist between amounts accrued and subsequent events. After year-end, CalRecycle should adjust its financial statements if there are material differences between amounts accrued as of June 30 and subsequent events related to the prior year, and contact SCO for further instructions, as required by SAM.

CalRecycle Response:

CalRecycle currently has procedures in place to work with accounting staff to ensure the proper process includes adjusting financial statements as necessary if revenue and expenditure accruals differ materially from the actuals.

CalRecycle is committed to continuing the recommendations noted in the audit report and will ensure that processes are periodically evaluated to ensure compliance with applicable requirements. Thank you for the opportunity to respond to the Draft Audit Report. Should you have any questions or concerns regarding our response, please contact Josephine Urban at (916) 322-3472.

Sincerely,

Original signed by Ken DaRosa for:

Scott Smithline
Director