Alameda Corridor-East Construction Authority

Indirect Cost Rate Proposal

Fiscal Years 2017-18 and 2018-19

Report No. 19-2660-010

June 2019

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Transmitted via e-mail

June 19, 2019

Ms. MarSue Morrill, Chief, Planning and Modal Office
Independent Office of Audits and Investigations
California Department of Transportation
1304 O Street, Suite 200
Sacramento, CA 95814

Dear Ms. Morrill:

Final Report—Alameda Corridor-East Construction Authority, Indirect Cost Rate Proposal Audit

The California Department of Finance, Office of State Audits and Evaluations, has completed its audit of the Alameda Corridor-East Construction Authority's (ACE) Indirect Cost Rate Proposal for fiscal years 2017-18 and 2018-19.

The enclosed report is for your information and use. ACE's response to the report findings is incorporated into this final report. We appreciate their assistance and cooperation during the engagement, and willingness to implement corrective actions.

If you have any questions regarding this report, please contact Rick Cervantes, Manager, or Jeremy Jackson, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

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

cc: Ms. Luisa Ruvalcaba, Audit Manager, Planning and Modal Office, Independent Office of Audits and Investigations, California Department of Transportation

BACKGROUND, SCOPE, AND METHODOLOGY

BACKGROUND

The California Department of Transportation's (Caltrans) Local Assistance Program oversees more than $1 billion dollars annually available to over 600 cities, counties, and regional agencies for the purpose of improving their transportation infrastructure or providing transportation services. This funding comes from various Federal and State programs specifically designed to assist the transportation needs of local agencies.[1]

The San Gabriel Valley Council of Governments, a joint powers authority comprised of 31 cities and Los Angeles County, created the Alameda Corridor-East Construction Authority (ACE) in 1998 to provide direction and oversight of the ACE Project to mitigate the impacts of significant increases in freight rail traffic over 70 miles of mainline railroad in the San Gabriel Valley. The ACE Project consists of a comprehensive program of safety improvements and mobility upgrades at 39 railroad crossings and 19 roadway-railroad crossing grade separation projects.[2]

At the discretion of local governmental agencies (LGA), indirect costs may be recovered when seeking reimbursement for federal-aid transportation projects and state funded projects. To recover indirect costs, LGAs submit an Indirect Cost Rate Proposal (ICRP), which may also include a fringe benefit rate to Caltrans' Independent Office of Audits and Investigations (IOAI). IOAI reviews the documentation supporting the rate(s) and issues an acceptance letter allowing the LGAs to bill Caltrans and seek reimbursement of indirect costs, which IOAI may audit for compliance with Title 2 Code of Federal Regulations Part 200 (2 CFR 200) and Caltrans' Local Assistance Procedures Manual Chapter 5 (LAPM).

SCOPE

At the request of IOAI, the California Department of Finance, Office of State Audits and Evaluations, audited ACE's ICRPs for fiscal years 2017-18 and 2018-19.

The audit objectives were to:

1. Determine if the 2017-18 and 2018-19 ICRPs, including fringe benefit rates, were in compliance with 2 CFR 200 and the LAPM.

2. Recalculate the proposed ICRP rate if unallowable costs impacting the rate by 1 percent or greater are identified.

The 2017-18 and 2018-19 ICRPs and fringe benefit rates include transactions related to actual costs incurred and billed to Caltrans in 2015-16 and 2016-17.

ACE is responsible for preparing its ICRP in accordance with state and federal requirements, which includes implementing internal controls and maintaining an adequate financial management system to accumulate and segregate reasonable, allowable, and allocable costs.

[1] Caltrans, Division of Local Assistance website http://www.dot.ca.gov/localassistance/index.html
[2] Excerpts obtained from Alameda Corridor-East Construction Authority website http://www.theaceproject.org/

METHODOLOGY

In planning the audit, we gained an understanding of ACE's operations, and identified relevant ICRP requirements by reviewing 2 CFR 200, the LAPM, and applicable ACE policies and procedures, and interviewing IOAI and ACE personnel.

We conducted a risk assessment, including evaluating whether key internal controls relevant to our audit objectives such as reviews and approvals, separation of duties, reconciliations, knowledge of tasks, and separation of indirect and direct costs were properly designed, implemented, and operating effectively. Our assessment included observing processes and testing transactions related to accounts payable, time keeping/payroll, billing, and cash disbursements for effectiveness of existing documented processes and procedures. Deficiencies in internal controls that were identified during our audit and determined to be significant within the context of our audit objectives are included in this report.

Additionally we assessed the reliability of data from ACE's financial management system, Microsoft Dynamics GP, and ACE's electronic time reporting system, Unanet. Our assessment included reviewing information process flows, testing transactions for completeness and accuracy, and determining if costs were separately categorized by tracing to the accounting records. We determined the data were sufficiently reliable for the purpose of this audit.

Based on the results of our planning, we developed specific methods for gathering evidence to obtain reasonable assurance to address the audit objectives. Our methods are detailed in the Table of Methodologies on the following page.

Table of Methodologies

Audit Objective	Methods

Objective 1:
Determine whether the 2017-18 and 2018-19 ICRPs, including the fringe benefit rates, are in compliance with 2 CFR 200 and the LAPM.
	• Selected significant and high-risk cost categories to verify compliance with 2 CFR 200 and the LAPM. Specifically, costs were selected from direct and indirect salaries and wages, fringe benefits, and the indirect costs pool.
	    o Selected items for direct and indirect salaries and wages was based on quantitative factors such as total hours charged; and qualitative factors such as the type (i.e. description) of costs.
	    o The most quantitatively significant fringe benefit costs were selected for testing.
	    o Selected items for indirect costs pool were based on quantitative factors such as costs with a potential impact to the ICRP rate by 1 percent or greater; and qualitative factors such as the timing and type (i.e. description) of costs.
	• Determined if direct and indirect salaries and wages were allowable, supported, segregated, and allocated, by tracing amounts and task coding to accounting and time reporting records, reviewing timesheets and payroll records, interviewing staff, and reviewing project description codes in the Unanet time reporting system.
	• Determined if fringe benefit costs were allowable, supported, segregated, and allocated by interviewing staff, tracing amounts to accounting records, payroll records and electronic fund transfers, and reviewing retirement contracts and the California Public Employees Retirement System (CalPERS) pension plan actuarial valuation reports.
	• Determined if indirect costs pool were allowable, supported, segregated, and allocated, by interviewing staff, reviewing invoices for descriptions and accurate coding, reviewing vendor lease agreements and contracts, reviewing depreciation schedules, and agreeing costs to cleared checks.
	• Verified the actual indirect costs recovered by ACE were billed at the IOAI approved indirect cost rate by reviewing invoices, verifying support for direct labor hours, and recalculating the indirect cost billed to Caltrans.
	• Verified the actual fringe benefit costs recovered by ACE were billed at the IOAI approved fringe benefit cost rate by reviewing invoices, verifying support for direct labor hours, and recalculating the fringe benefit costs billed to Caltrans.

Objective 2: Recalculate the proposed ICRP rate if unallowable costs impacting the ICRP rate by 1 percent or greater are identified.	• Recalculated the proposed ICRP rates as a result of indirect costs pool audit adjustments greater than 1 percent. o Removed ineligible excess unfunded liability costs from the indirect costs pool. • Recalculated the carry forward adjustments based on fiscal year 2015-16 and 2016-17 audited actual amounts.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

CONCLUSION

Based on the procedures performed and evidence gathered, we determined ACE's 2017-18 and 2018-19 ICRPs are not in compliance with 2 CFR 200 and the LAPM. We identified weaknesses in ACE's review process when preparing the ICRPs as noted in Finding 1. Additionally, as described in Finding 2, we identified unallowable costs that impacted the 2017-18 and 2018-19 ICRP rates and recommend a rate change decrease of 52.4 percent and 130.8 percent as identified in Table 1 below. No change to the fringe benefit rates were identified.

Table 1 – Accepted and Audited 2017-18 and 2018-19 ICRP and Fringe Benefit Rates[3]

Fiscal Year	Rate Type	Accepted Rate	Audited Rate	Difference
2017-18	ICRP	184.6%	132.2%	(52.4%)
	Fringe Benefit	38.59%	38.59%	0%
2018-19	ICRP	282.2%	151.4%	(130.8%)
	Fringe Benefit	40.02%	40.02%	0%

See Appendix A and Appendix B for the Summary of Accepted and Audited Costs and Rates for the Indirect Cost Rate Proposals and the Fringe Benefit Rates.

FINDINGS AND RECOMMENDATIONS

Finding 1: Carry Forward Calculation Procedures Need Improvement

ACE included the incorrect beginning carry forward cost in its calculation to determine the 2018-19 ICRP rate submitted to IOAI.[4] ACE used $872,051 as the beginning carry forward amount. However, ACE subsequently determined the amount was incorrectly calculated and the correct carry forward amount should be $167,648. We verified the accurate carry forward amount of $167,648 in the 2016-17 IRCP rate submission letter that was accepted by IOAI, and additionally recalculated it. The $704,403 difference overstates the indirect cost rate by 39.4 percent. According to ACE, as of September 17, 2018, it has not billed Caltrans indirect costs for 2018-19. ACE does not have a review process to ensure the accuracy of the ICRP rate calculation. Additionally, ACE does not perform a reconciliation of estimated fringe benefits to actual fringe benefit costs to ensure the difference between actual and estimated costs is recovered in a subsequent period. Although the variance was not significant for 2017-18 or 2018-19, the lack of reconciliation increases the risk of over or under billing fringe benefits.

[3] The ICRPs and Fringe Benefit Rates submitted by ACE were accepted by IOAI on July 18, 2017, and August 21, 2018.

[4] ACE uses a schedule of estimated direct and indirect costs to determine the annual indirect cost rate. These estimates are reconciled to actual costs. The difference between the actual costs and the estimated costs is carried forward and is included in the calculation of a future ICRP rate. This is referred to as the carry forward calculation.

2 CFR 200, Appendix VII to Part 200-States and Local Government and Indian Tribe Indirect Cost Proposals, B. Definitions, 5, states the difference between the estimated costs and the actual, allowable costs of the period covered by the rate is carried forward as an adjustment to the rate computation of a subsequent period."

LAPM section 5.13, Documentation of Proposal, section 1B states subsidiary worksheets should include a schedule showing the calculation of the over/under carry forward provision when a fixed rate is used.

2 CFR 200.411 (a) (2) states negotiated indirect cost rates based on a proposal later found to have included costs that are unallowable because they are not allocable to the Federal award(s), must be adjusted, or a refund must be made, in accordance with the requirements of this section. These adjustments or refunds are designed to correct the proposals used to establish the rates and do not constitute a reopening of the rate negotiation.

Recommendations:

A. Adjust the 2018-19 carry forward adjustment by $704,403 and submit a revised ICRP for 2018-19 to IOAI.

B. Develop review procedures to ensure the ICRP rate calculation is accurate.

C. Implement a reconciliation process to calculate the difference between the estimated direct fringe benefit and actual direct fringe benefit costs. The difference between the actual and the estimated costs should be included in the calculation of subsequent fringe benefit rates.

Finding 2: Unallowable Excess Unfunded Liability Payments

In 2014-15, ACE began making payments in excess of the required payments listed in the CalPERS amortization schedules for its employee retirement plan unfunded liability. The excess payments were from a payment schedule developed by ACE to pay the entire unfunded liability balance over a period of three years. ACE stated the excess payments were made because it estimated all projects would be completed and the agency would close in approximately four years. The excess payments were included in the indirect costs pool for 2015-16 through 2018-19. ACE did not follow the actuarial amortization payment schedule of 20, 25, or 30 years provided in the CalPERS Annual Valuation report as of June 30, 2013. Therefore, the payments made in excess of the amortization schedule are unallowable and should not be included in the indirect cost pool. To calculate the unallowable indirect costs, we used the 20 year CalPERS amortization schedule. The 20 year schedule allows for the largest allowable payment based on the CalPERS actuarial schedule. Table 2 on the following page shows the unallowable costs for each fiscal year.

2 CFR 200.431 (g) (6) (ii) and (iii) state that pension plan costs are allowable provided that costs are calculated using an actuarial cost-based method recognized by Generally Accepted Accounting Principles and amounts funded in excess of the actuarially determined amount for a fiscal year may be used as the entity's contribution in future periods.

Table 2 – Unallowable Unfunded Liability Payments

Fiscal Year[5]	Amount Paid/Budgeted (a)	Payment per 20 Year Amortization Schedule (b)	Unallowable Costs (c = a – b)	Audit Adjustment in Appendix A
2015-16	$ 339,392	$ 77,690	$ 261,702	2017-18 Carry Forward
2016-17	900,000	80,021	819,979	2018-19 Carry Forward
2017-18	900,000	82,421	817,579	2017-18 Fringe Benefits
2018-19	900,000	84,894	815,106	2018-19 Fringe Benefits
Total	$ 3,039,392	$ 325,026	$ 2,714,366	

Recommendations:

A. Adjust the 2017-18 indirect costs pool by $817,579 and the 2018-19 indirect costs pool by $815,106 for the unallowable employee retirement payments in excess of the CalPERS amortization schedule and ensure these costs are not included in future indirect costs pools.

B. Adjust the 2015-16 carry forward amount by $261,702 and the 2016-17 carry forward amount by $819,979, as a result of the unallowable indirect costs described above.

C. Reconcile the 2017-18 and 2018-19 billings using the audited rate of 132.2 percent and 151.4 percent, respectively, and reimburse Caltrans any over payments.

[5] ACE began making excess payments in 2014-15; however, those payments were not included in the 2017-18 and 2018-19 ICRP calculations and are outside our audit scope. ACE included excess payments made in 2015-16 through 2018-19 in the ICRP calculations for 2017-18 and 18-19; those payments were included in our audit scope.

APPENDIX A

Summary of Accepted and Audited Costs and Rates
Indirect Cost Rate Proposal
Alameda Corridor-East Construction Authority
2017-18

Description	Accepted Amounts[6]	Audit Adjustments	Audited Amounts	Finding No.
Direct Costs				
Salaries and Wages	$ 1,485,000	$ 0	$ 1,485,000	
Fringe Benefits[7]	573,000	0	573,000	
Total Direct Salaries and Wages plus Fringe Benefits	$ 2,058,000	$ 0	$ 2,058,000	
Indirect Costs Pool				
Salaries and Wages	$ 1,499,700	$ 0	$ 1,499,700	
Fringe Benefits	1,316,000	(817,579)	498,421	2
Legal - Agency Support	25,000	0	25,000	
Auto/Travel	4,700	0	4,700	
Training/Memberships	27,200	0	27,200	
Auditing/Accounting	42,000	0	42,000	
Risk Management	52,000	0	52,000	
Insurance	224,000	0	224,000	
Equipment Expense	119,000	0	119,000	
Office Expense	251,000	0	251,000	
Office Operations	51,000	0	51,000	
Other	7,000	0	7,000	
Total Indirect Costs Pool	$ 3,618,600	$ (817,579)	$ 2,801,021	
Carry Forward (2015-16)	$ 180,870	$ (261,702)	$ (80,832)	
Adjustments to Indirect Costs	0	(817,579)	(817,579)	2
Total Carry Forward Adjustment	$ 180,870	(1,079,281)	$ (898,411)	2
Budgeted Indirect Costs	$ 3,618,600	$ (817,579)	$ 2,801,021	2
Total Indirect Costs*	3,799,470	(1,079,281)	2,720,189	2
Total Direct Salaries and Wages plus Fringe Benefits	2,058,000	0	2,058,000	
Indirect Cost Rate**	184.6%	-52.4%	132.2%	2
Fringe Benefit Rate***	38.59%	0.0%	38.59%	
* Total Indirect Costs is the sum of Total Carry Forward Adjustments and Budgeted Indirect Costs				
** Indirect Cost Rate is the quotient of Total Indirect Costs divided by Total Direct Salaries and Wages plus Fringe Benefits				
*** Fringe Benefit Rate is the quotient of Direct Fringe Benefits divided by Direct Salaries and Wages				

[6] The ICRP and Fringe Benefit Rate submitted by ACE was accepted by IOAI on July 18, 2017.
[7] Fringe benefits include dental insurance, life insurance, short and long term disability, medical insurance, retirement, vision insurance, worker's compensation, and employer taxes.

Summary of Accepted and Audited Costs and Rates
Indirect Cost Rate Proposal
Alameda Corridor-East Construction Authority
2018-19

Description	Accepted Amounts[8]	Audit Adjustments	Audited Amounts	Finding No.
Direct Costs				
Salaries and Wages	$ 1,277,000	$ 0	$ 1,277,000	
Fringe Benefits[9]	511,000	0	511,000	
Total Direct Salaries and Wages plus Fringe Benefits	$ 1,788,000	$ 0	$ 1,788,000	
Indirect Costs Pool				
Salaries and Wages	$ 1,539,846	$ 0	$ 1,539,846	
Fringe Benefits	1,327,753	(815,106)	512,647	2
Legal - Agency Support	25,000	0	25,000	
Auto/Travel	6,200	0	6,200	
Training/Memberships	31,700	0	31,700	
Auditing/Accounting	42,345	0	42,345	
Risk Management	65,000	0	65,000	
Insurance	171,000	0	171,000	
Equipment Expense	84,723	0	84,723	
Office Expense	256,038	0	256,038	
Office Operations	47,800	0	47,800	
Other	6,250	0	6,250	
Total Indirect Costs Pool	$ 3,603,655	$ (815,106)	$ 2,788,549	
Carry Forward (2016-17)	$ 1,442,382	$ (1,524,382)	$ (82,000)	1, 2
Adjustments to Indirect Costs	0	(815,106)	(815,106)	2
Total Carry Forward Adjustment	$ 1,442,382	$ (2,339,488)	$ (897,106)	1, 2
Budgeted Indirect Costs	$ 3,603,655	$ (815,106)	$ 2,788,549	2
Total Indirect Costs*	5,046,037	(2,339,488)	2,706,549	1, 2
Total Direct Salaries and Wages plus Fringe Benefits	1,788,000	0	1,788,000	
Indirect Cost Rate**	282.2%	-130.8%	151.4%	1, 2
Fringe Benefit Rate***	40.02%	0.0%	40.02%	

* Total Indirect Costs is the sum of Total Carry Forward Adjustments and Budgeted Indirect Costs

** Indirect Cost Rate is the quotient of Total Indirect Costs divided by Total Direct Salaries and Wages plus Fringe Benefits

*** Fringe Benefit Rate is the quotient of Direct Fringe Benefits divided by Direct Salaries and Wages

[8] The ICRP and Fringe Benefit Rate submitted by ACE was accepted by IOAI on August 21, 2018.

[9] Fringe benefits include dental insurance, life insurance, short and long term disability, medical insurance, retirement, vision insurance, worker's compensation, and employer taxes.

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June 4, 2019

CalTRANS Audit Department

I am responding to your draft audit report of the Alameda Corridor – East Construction Authority's FY 17/18 & 18/19 ICAP Audit. I appreciate your efforts during the audit process to provide timely, constructive advice on how to improve the authority's internal controls and processes for the ICAP preparation.

Management has reviewed the findings noted in the ICAP audit. After discussion with management the findings will be corrected as follows . The overstated ICAP rate for FY 17-18 will be reduced from the FY 19-20 ICAP rate. The overstated ICAP rate for the current year FY 18-19 will be adjusted within this year since the accounting period is still open and the changes can be made prior to the closeout of the books. The calculation issues that were noted with the carry-forward spreadsheet will be resolved by using a new template for completing the new ICAP proposal for FY 19-20. Budget vs actual costs will also be reconciled moving forward as part of the ICAP and closeout process . Implementing these steps will ensure that the noted issues are corrected and a system would be in place to avoid this occurring again.

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I appreciate the continuing professional, cooperative relationship that exists with CalTRANS and the Alameda Corridor – East Construction Authority.

Sincerely,

Original signed by:

Maritza Ramos
Director of Finance