State of California
DEPARTMENT OF TRANSPORTATION

California State Transportation Agency

Memorandum

Serious drought.
Help Save Water!

To: RIHUI ZHANG
Chief
Division of Local Assistance

Date: June 30, 2016

File: P1590-0475

From: MARSUE MORRILL, CPA MarSue
Chief, External Audits – Local Governments
Audits & Investigations

Subject: **INDIRECT COST RATE PROPOSAL AUDIT – CITY OF VISALIA, COMMUNITY DEVELOPMENT DEPARTMENT, ENGINEERING DIVISION AND ADMINISTRATIVE SERVICES DEPARTMENT, TRANSIT DIVISION**

At the request of Caltrans Audits and Investigations, the State Controller's Office (SCO) conducted an audit of the City of Visalia, Community Development Department, Engineering Division and Administrative Services Department, Transit Division's (City) Indirect Cost Rate Proposals (ICRPs) for fiscal year (FY) 2012/13.

The purpose of the audit was to determine whether the ICRPs were presented in accordance with Title 2 Code of Federal Regulations Part 225, and Caltrans Local Assistance Procedures Manual, Chapter 5.

The FY 2012/13 rates did not require adjustment. The approved rates of Engineering Division and Transit Division are 45.64 percent and 62.80 percent, respectively. The rates are based on direct salaries and wage plus fringe benefits. Based on the SCO audit, there is one finding. The City is required to contact Caltrans to correct the $79,045 in overpayment it received.

Please provide our office with a corrective action plan addressing the recommendation in the report, including time lines, by August 15, 2016.

If you have any questions, please contact Yung Jo Ryoo, Auditor, at (916) 323-7950, or me, at (916) 323-7105.

Attachment

c: Renee Nagel, Finance Director, City of Visalia
Janice Richard, Director, Financial Services, Federal Highway Administration
Jack Lord, Planning and Air Quality Team Leader, Federal Highway Administration
Veneshia Smith, Financial Program Manager, Federal Highway Administration
Kara Magdaleno, Administrative Program Assistant Planning and Finance, Federal Highway Administration
John Hoole, Chief, Project Implementation South, Division of Local Assistance, Caltrans
Winton Emmett, Chief, Project Implementation North, Division of Local Assistance, Caltrans
Jim Perrault, Chief, Office of Local Assistance, Division of Planning and Local Assistance, District 6, Caltrans
David Saia, LAPM/LAPG Coordinator, Division of Local Assistance, Caltrans
Lai Huynh, Audits and Federal Performance Measures Analyst, Division of Local Assistance, Caltrans
MarSue Morrill, CPA, Chief, External Audits - Local Governments, Audits & Investigations, Caltrans
Office Chron

CITY OF VISALIA COMMUNITY DEVELOPMENT DEPARTMENT, ENGINEERING DIVISION AND ADMINISTRATIVE SERVICES DEPARTMENT, TRANSIT DIVISION

Audit Report

INDIRECT COST RATE PROPOSAL AUDIT OF CALTRANS CONTRACT NO. 77A0034 (Audit Request No. P1590-0475)

July 1, 2012, through June 30, 2013

BETTY T. YEE

California State Controller

June 2016

BETTY T. YEE
California State Controller

June 24, 2016

MarSue Morrill, Chief
External Audits – Local Government
Department of Transportation
Audits & Investigations
P.O. Box 942874
Sacramento, CA 94274-0001

Dear Ms. Morrill:

The State Controller's Office audited the indirect cost rate proposals (ICRPs) of the City of Visalia, Community Development Department, Engineering Division and Administrative Services Department, Transit Division. The audit period included ICRPs for fiscal year 2012-13. The audit was performed at the request of the California Department of Transportation (Caltrans) Audits and Investigations.

The Community Development Department, Engineering Division, proposed an indirect cost rate of 45.64% by dividing indirect and direct costs of $949,751 and $2,081,000. The Administrative Services Department, Transit Division, also proposed an indirect cost rate of 62.80% by dividing indirect and direct costs of $354,069 and $563,800, respectively.

The purpose of the audit was to determine whether the ICRPs were presented in accordance with Title 2, *Code of Federal Regulations*, Part 225, Appendices A–F, and the Caltrans Local Programs Procedures 04-10. The city's management is responsible for fair presentation of the ICRPs.

We found that the city miscalculated certain billable rates submitted to Caltrans for project expenditures reimbursement purposes. The accounting impact is $79,045 for the period under audit.

If you have any questions, please contact Andrew Finlayson, Chief, State Agency Audits Bureau, at (916) 324-6310.

Sincerely,

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/as

cc: Alice M. Lee, Audit Manager
California Department of Transportation

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Audit Report

Summary

The State Controller's Office (SCO) audited the indirect cost rate proposals (ICRPs) of the City of Visalia, Community Development Department's Engineering Division and Administrative Services Department's Transit Division. The audit period included ICRPs for fiscal year (FY) 2012-13.

The Community Development Department, Engineering Division, proposed an indirect cost rate of 45.64% by dividing indirect and direct costs of $949,751 and $2,081,000. The Administrative Services Department, Transit Division, also proposed an indirect cost rate of 62.80% by dividing indirect and direct costs of $354,069 and $563,800, respectively.

The purpose of the audit was to determine whether the ICRPs were presented in accordance with Title 2, *Code of Federal Regulations*, Part 225 (2 CFR 225), Appendices A–F, and the California Department of Transportation's (Caltrans) Local Programs Procedures (LPPs) 04-10. The city's management is responsible for fair presentation of the ICRPs.

Our audit found that the city miscalculated certain billable rates submitted to Caltrans for project expenditures reimbursement purposes. The accounting impact is $79,045 for the period under audit.

Background

The City of Visalia's Engineering Division provides customer service and a safe work environment for residents, contractors, and city employees. The Transit Division applies new technology and innovative solutions toward future progress in improving the value, efficiency, and effectiveness of its projects and the economic vitality of the community.

This audit was performed by the SCO on behalf of Caltrans (Audit Request No. P1590-0475). The authority to conduct this audit is given by:

- Interagency Agreement No. 77A0034, dated March 31, 2010, between the SCO and Caltrans, which provides that the SCO will perform audits of proposed ICRPs submitted to Caltrans from local government agencies to ensure compliance with 2 CFR 225 (formerly Office of Management and Budget Circular A-87) and LPPs 04-10.

- Government Code section 12410, which states, "The Controller shall superintend the fiscal concerns of the state. The Controller shall audit all claims against the state and may audit the disbursement of any money, for correctness, legality, and for sufficient provisions of law for payment."

Objectives, Scope, and Methodology

The scope of the audit was limited to the select financial and compliance activities. The audit consisted of recalculating the ICRPs and making inquiries of department personnel. The audit also included tests of individual accounts in the general ledger and supporting documentation to assess allowability, allocability, and reasonableness of costs and an assessment of the internal control system related to the ICRPs for FY 2012-13. Changes to the financial management system subsequent to FY 2012-13 were not tested and, accordingly, our conclusion does not pertain to changes arising after that fiscal year.

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.

Our audit was conducted to determine whether (1) the city's ICRPs were presented in compliance with the cost principles prescribed in 2 CFR 225; (2) the ICRPs were in compliance with the requirements for ICRP preparation and application identified in the Caltrans LPPs 04-10; (3) and the city's financial management system is accumulating and segregating reasonable, allowable, and allocable costs.

To achieve our audit objectives, we performed the following audit procedures:

- Reviewed the city's prior audit reports;
- Reviewed the city's written policies and procedures relating to accounting systems, procurement, and project/contract management;
- Interviewed employees, completed an internal control questionnaire, and performed a system walk-through in order to gain an understanding of the city's internal controls, accounting systems, timekeeping and payroll systems, and procurement and billing processes;
- Performed a limited test of controls on a judgmental sample of transactions to confirm and validate existing documented processes and procedures;
- Recalculated and/or tested the mathematical accuracy of the ICRPs and supporting worksheets; and
- Tested selected individual accounts and transactions, including supporting documentation.

We did not audit the city's financial statements. We limited our audit scope to planning and performing audit procedures necessary to obtain reasonable assurance that the proposed ICRPs were in accordance with the 2 CFR 225 and LPPs 04-10. In addition to developing appropriate auditing procedures, our review of internal control was limited to gaining an understanding of the transaction flow, accounting system, and applicable controls to determine the department's ability to accumulate and segregate reasonable, allowable, and allocable indirect and direct costs.

Conclusion

We determined that the city's ICRPs were prepared in accordance with 2 CFR 225, and that the project billings generally appear to be in compliance with the Local Assistance Procedures Manual, Chapter 5, except that the city miscalculated certain billable rates submitted to Caltrans for project expenditures reimbursement purposes. The accounting impact is $79,045 for the period under audit.

We also determined that the city has an adequate financial management system to accumulate and segregate allowable and allocable direct and indirect costs, and that the city is in compliance with applicable state and/or federal procurement policies and procedures.

Views of Responsible Officials

We conducted a telephone exit conference. Renee Nagel, Finance Director; and Jason Serpa, Financial Analyst, agreed with the audit results. Ms. Nagel and Mr. Serpa declined a draft audit report and agreed that we could issue the audit report as final.

We provided the city with a copy of the audit finding. Renee Nagel, Finance Director, responded by a letter through email, agreeing with the audit results.

Restricted Use

This report is solely for the information and use of the City of Visalia, the California Department of Transportation; and the SCO. It is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this report, which is a matter of public record.

Jeffrey V. Brownfield

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

June 24, 2016

Schedule 1—
Summary of ICRP Costs
Engineering Division, Community Development Department
July 1, 2012, through June 30, 2013

	Proposed Amounts	Audit Adjustments	Audited Amounts
Direct costs			
Salaries and benefits			
Salaries	$ 1,501,700	-	$ 1,501,700
Benefits	579,300	-	579,300
Total salaries and benefits	$ 2,081,000	-	$ 2,081,000
Indirect costs			
Salaries and benefits			
Salaries	-	-	-
Benefits	-	-	-
Total salaries and benefits	-	-	-
Services and supplies			
New employee expenses	$ 1,000	-	$ 1,000
Recruitment costs	500	-	500
Clothing and personal expense	900	-	900
Membership-organization	2,800	-	2,800
Membership-employee	2,300	-	2,300
Business meetings	600	-	600
Conferences/seminars	500	-	500
Training	2,100	-	2,100
Office supplies	2,500	-	2,500
Paper/forms supplies	2,000	-	2,000
Postage	700	-	700
Publications/subscriptions	300	-	300
Special departmental supply	5,500	-	5,500
Paint supplies	300	-	300
Misc. other expenses	-	-	-
Equipment supply and maintenance	11,200	-	11,200
Small tools	800	-	800
Traffic signs	-	-	-
Professional and specialized services	1,700	-	1,700
Contracts-landscape maintenance	1,400	-	1,400
Contracts-mall service	-	-	-
Contracts-copier leases	2,900	-	2,900
Advertising	200	-	200
Duplicating services	100	-	100
Telephone	2,000	-	2,000
Telephone-computer line	3,100	-	3,100
Telephone-wireless communication	1,800	-	1,800
Telephone-cellular	8,900	-	8,900
Software	-	-	-
Allocation P/W fleet fuel	13,800	-	13,800
Total services and supplies	$ 69,900	-	$ 69,900
A-87	879,851	-	879,851
Total indirect costs	$ 949,751	-	$ 949,751
Total direct costs	2,081,000	-	2,081,000
Indirect Cost Rate [1]	**45.64%**		**45.64%**

[1] The indirect cost rate is calculated by dividing the total indirect costs by the indirect cost calculation base (total estimated direct salaries and wages plus fringe benefits).

Schedule 2—
Summary of ICRP Costs
Transit Division, Administrative Services Department
July 1, 2012, through June 30, 2013

	Proposed Amounts	Audit Adjustments	Audited Amounts
Direct costs			
Salaries and benefits			
Salaries	$ 390,300	-	$ 390,300
Benefits	173,500	-	173,500
Total salaries and benefits	$ 563,800	-	$ 563,800
Indirect costs			
Salaries and benefits			
Salaries	-	-	-
Benefits	-	-	-
Total salaries and benefits	-	-	-
Services and supplies			
New employee expenses	$ 300	-	$ 300
Recruitment costs	-	-	-
Education assistance	-	-	-
Membership-employee	15,400	-	15,400
Business meetings	500	-	500
Conferences/seminars	3,700	-	3,700
Training	2,100	-	2,100
Oranization development	-	-	-
General community support	500	-	500
Office supplies	5,800	-	5,800
Paper/forms supplies	100	-	100
Postage	1,100	-	1,100
Publications/subscriptions	200	-	200
Janitorial supplies	900	-	900
Misc. other expenses	100	-	100
Pumping equipment repairs	-	-	-
Photo supplies	-	-	-
Rents and leases	-	-	-
Vehicle rental fees	500	-	500
Bank administration fees	-	-	-
Duplicating services	600	-	600
Natural gas	14,800	-	14,800
Water/refuse/sewer	34,400	-	34,400
Telephone	4,800	-	4,800
Telephone-computer line	3,700	-	3,700
Telephone-fax	800	-	800
Telephone-cellular	700	-	700
Telephone-online service	600	-	600
Commission Fee	-	-	-
Total services and supplies	$ 91,600	-	$ 91,600
A-87	262,469	-	262,469
Total indirect costs	$ 354,069	-	$ 354,069
Total direct costs	563,800	-	563,800
Indirect Cost Rate [1]	**62.80%**		**62.80%**

[1] The indirect cost rate is calculated by dividing the total indirect costs by the indirect cost calculation base (total estimated direct salaries and wages plus fringe benefits).

Finding and Recommendation

FINDING — City employees' billable rates were miscalculated

The city bills California Department of Transportation (Caltrans) for direct and indirect project costs including the city's personnel services costs for employees who work on Caltrans-funded projects. In reviewing of the billable rate calculations provided by the city, we noted that the city incorrectly included employee benefit costs more than once in the calculations worksheet for part of the period under audit. The accounting impact is at least $79,045.

The city uses weighted rates to bill Caltrans for the city staff time. The weighted rates include both a base hourly rate and employee benefit costs such as paid time off, health, and dental plans. Because the employees' benefit costs are factors in calculating the billable rates for requesting reimbursements from Caltrans, the incorrect calculation does not represent actual expenditures of the city. We noted that the city also has overbilled indirect costs due to the incorrect weighted rates for employees.

Title 2, of the *Code of Federal Regulations* (CFR), Part 225, Appendix A, section C.2.b states that:

> A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost. The question of reasonableness is particularly important when governmental units or components are predominately federally-funded. In determining reasonableness of a given cost, consideration shall be given to: The restraints or requirements imposed by such factors as: Sound business practices; arm's-length bargaining; Federal, State and other laws and regulations; and, terms and conditions of the Federal award.

Recommendation

The city should ensure that personnel services expenditures, including fringe benefits submitted to Caltrans for reimbursement, represent actual reimbursable costs that are adequately calculated in accordance with 2 CRF 225. The city should ensure that all employee benefit costs are correctly calculated. Additionally, the city should review prior invoices that were reimbursed by Caltrans to ensure that direct and indirect expenses were not overbilled, and the city should reimburse Caltrans for any overbilled amounts.

City's Response

> The City of Visalia has reviewed the ICRP audit recommendations and findings submitted for the fiscal year ending July 1, 2012 through June 30, 2013. The city concurs with the findings and has implemented controls to mitigate incorrect charges in the future.
>
> The city will also be in contact with Caltrans to correct the $79,045 in overpayment the city received.
>
> The city of Visalia is committed to providing excellent financial service and thanks the SCO for their dedication in the field.

SCO's Comment

The city agreed with the finding and recommendation.

City of Visalia

707 West Acequia Ave.
Visalia, CA 93291

Finance Division

Renee Nagel
Tel.:(559) 713-4375
Fax: (559) 713-4801

July 30, 2015

Laurentiu Pele
State Controller's Office
Division of Audits – ICAP

Dear Mr. Pele:

Regarding City of Visalia ICRP Audit:

The city of Visalia has reviewed the ICRP audit recommendations and findings submitted for the fiscal year ending July 1, 2012 through June 30, 2013. The city concurs with the findings and has implemented controls to mitigate incorrect charges in the future.

The city will also be in contact with Caltrans to correct the $79,045 in overpayment the city received.

The city of Visalia is committed to providing excellent financial service and thanks the SCO for their dedication in the field.

Renee Nagel

Renee Nagel – Finance Director
City of Visalia - Finance Dept.
(559) 713-4375 / Fax (559) 713-4801