State of California
DEPARTMENT OF TRANSPORTATION

California State Transportation Agency

Memorandum

Serious drought.
Help Save Water!

To: RIHUI ZHANG
Division Chief
Local Assistance

Date: August 17, 2015

File: P1590-0245
P1590-0246

From: MARSUE MORRILL, CPA
Chief, External Audits-Local Governments
Audits and Investigations

Subject: **AUDIT REPORT – COUNTY NAPA, DEPARTMENT OF PUBLIC WORKS, DIVISION OF ENGINEERING**

At the request of the Caltrans, Audits and Investigations, the State Controller's Office (SCO) conducted an audit of the County of Napa, Department of Public Works, Division of Engineering's (County) indirect cost rate proposals (ICRPs) for fiscal years (FY) 2007/08, and 2008/09 to determine whether the ICRPs are presented in accordance with Title 2 Code of Federal Regulations (CFR) Part 225. The audit report is attached.

Based on audit work performed by the SCO, we determined the County's ICRPs are presented in accordance with Title 2 CFR Part 225. **The approved indirect cost rates are 40.29 percent and 54.30 percent of total direct salaries and fringe benefits for FYs 2007/08 and 2008/09 respectively**.

The audit identified $138,769 and $109,434 in engineering indirect labor costs for FY 2007/08 and FY 2008/09 respectively that were misallocated to a division outside the Department of Public Works, the Division of Flood Control and Water Resources. This misallocation resulted in the indirect cost rates to be understated by 4.47 percent for FY 2007/08 and by 3.21 percent for FY 2008/09.

Since the audited indirect rates are higher than the FY 2007/08 and FY 2008/09 rates of 35.82 percent and 52.76 percent respectively that were previously accepted on April 23, 2012, the County may use the higher audited rate to reconcile prior reimbursement claims.

If you have any questions, contact Alice Lee, Audit Manager, at (916) 323-7953.

Attachment

c: Steve Lederer, Director, Department of Public Works, County of Napa
Janice Richard, Director, Financial Services, Federal Highway Administration
Jack Lord, Director, Planning and Air Quality, Federal Highway Administration
Kara Magdaleno, Administrative Program Assistant, Planning and Finance, Federal Highway Administration
C. Edward Philpot, Jr., Branch Chief, Grants/Public Engagement, Office of Community Planning, California Department of Transportation
Andrew Finlayson, Chief, State Agency Audit Bureau, California State Controller's Office
James Ogbonna, Chief, Rural Transit and Intercity Bus Branch, Division of Mass Transportation, California Department of Transportation
Sylvia Fung, DLAE, Chief, Office of Local Assistance, District 4, Division of Transportation Planning, California Department of Transportation
Ezequiel Castro, Chief, Associate Transportation Planner, Division of Mass Transportation, California Department of Transportation
Erin Thompson, Senior Environmental Planner, Division of Transportation Planning, California Department of Transportation
Michael Mock, Audit Manager, State Agency Audit Bureau, State Controller's Office
Sean Tsao, Audit Manager, State Agency Audit Bureau, State Controller's Office
Karen Hunter, Rail Transportation Associate, Division of Rail, California Department of Transportation
Lisa Gore, Associate Accounting Analyst, Division of Accounting, California Department of Transportation
Annette Goudeau, Acting Audits & Federal Performance Measures Analyst, Division of Local Assistance, California Department of Transportation
David Saia, LAPM/LAPG Coordinator, Division of Local Assistance, California Department of Transportation

NAPA COUNTY

Audit Report

INDIRECT COST RATE PROPOSAL (ICRP) AUDIT OF CALTRANS CONTRACT NO. 77A0034 (Audit Request No. P1590-0245, 0246, 0247, and 0248)

July 1, 2007, through June 30, 2009

BETTY T. YEE

California State Controller

July 2015

BETTY T. YEE
California State Controller

July 13, 2015

MarSue Morrill, Chief
External Audits-Local Governments
Audits and Investigations, MS 2
California Department of Transportation
1304 O Street, Suite 200, MS 2
Sacramento, CA 95814

Dear Ms. Morrill:

The State Controller's Office audited the indirect cost rate proposal (ICRP) of the Napa County, Department of Public Works, Engineering Division for fiscal year (FY) 2007-08 and FY 2008-09. The County proposed indirect cost rates of 35.82% and 51.09%, respectively.

The purpose of the audit was to determine whether (1) proposed rates were in compliance with the cost principles prescribed in Title 2, *Code of Federal Regulations*, Part 225; (2) ICRPs were in compliance with Caltrans Local Program Procedures Manual 04-10; and (3) the Department's cost accounting system was accumulating and segregating reasonable, allowable, and allocable costs.

Our audit identified direct and indirect costs that were incorrectly recorded and or excluded, causing the indirect cost rate to be understated by 4.47% for FY 2007-08 and understated by 3.21% for FY 2008-09. We reclassified these labor costs and determined an indirect cost rate of 40.29% and 54.30%, respectively.

Except for these costs, we determined that the proposed rates were in accordance with the above requirements and that the County's cost accounting system is accumulating and segregating reasonable, allocable, and allowable costs.

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

Sincerely,

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

JVB/as

cc: Steven E. Lederer, Director
Department of Public Works, Napa County

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Audit Report

Summary

The State Controller's Office (SCO) audited the indirect cost rate proposal (ICRP) of the Napa County, Department of Public Works, Engineering Division for fiscal year (FY) 2007-08 and FY 2008-09. The County proposed indirect cost rates of 35.82% and 51.09%, respectively.

The purpose of the audit was to determine whether (1) proposed rates were in compliance with the cost principles prescribed in Title 2, *Code of Federal Regulations*, Part 225 (2 CFR 225); (2) ICRPs were in compliance with California Department of Transportation (Caltrans) Local Program Procedures Manual (LPP) 04-10; and (3) the Department's cost accounting system was accumulating and segregating reasonable, allowable, and allocable costs.

Our audit identified direct and indirect costs that were incorrectly recorded and or excluded, causing the indirect cost rate to be understated by 4.47% for FY 2007-08 and understated by 3.21% for FY 2008-09. We reclassified these labor costs and determined an indirect cost rate of 40.29% and 54.30%, respectively.

Except for these costs, we determined that the proposed rates were in accordance with the above requirements and that the County's cost accounting system is accumulating and segregating reasonable, allocable, and allowable costs.

Background

Napa County, situated in California's wine country, was formed in February 1850. The County is governed by a five-member Board of Supervisors, each of whom is elected to a four-year term; the Chair position is rotated each year among the members.

The Department of Public Works constructs, maintains, and improves facilities and infrastructure within the unincorporated areas of Napa County, which is home to 450 miles of public roads, 79 bridges, and 50 major drainage structures.

The Construction and Design Engineering Departments provide design and/or oversight for all contracted professional services and contract administration.

The proposed indirect cost rate allows the County to recover Federal Highway Administration and Caltrans-funded project-related indirect costs.

The audit was performed by the SCO on behalf of Caltrans (Audit Request No. P150-0137). 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 LPP 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

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

The scope of the audit was limited to the select financial and compliance activities. The audit consisted of recalculating the ICRP 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 ICRP for FY 2007-08 and FY 2008-09. Changes to the financial management system subsequent to FY 2008-09 were not tested and, accordingly, our conclusion does not pertain to changes arising after this fiscal year.

We did not audit Napa County's financial statements. We limited our audit scope to planning and performing audit procedures necessary to obtain reasonable assurance that the proposed ICRP was in accordance with the 2 CFR 225 and LLP 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.

We conducted this performance audit in accordance with the 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

We audited the indirect cost rate proposal of the Napa County, Department of Public Works, Engineering Division for FY 2007-08 and FY 2008-09. The County proposed an indirect cost rate of 35.82% and 51.09%, respectively. Our audit determined an indirect cost rate of 40.29%, a difference of 4.47% for FY 2007-08 and an indirect cost rate of 54.30%, a difference of 3.21% for FY 2008-09. The proposed rates were understated because the County inadvertently misclassified direct and indirect costs. We reclassified these costs and determined indirect cost rate of 40.29% for FY 2007-08 and 54.30% for FY 2008-09.

Except for these misclassified costs, we determined that the proposed rates were in accordance with the above requirements and that the County's cost accounting system is accumulating and segregation reasonable, allocable, and allowable costs.

Views of Responsible Officials

We conducted an exit conference on March 13, 2014, and discussed our audit results with Kim Henderson, Staff Services Manager; Jason Campbell, Deputy Director; and Sophie Johnson, Supervising Staff Services Analyst of the Napa County Department of Public Works. They agreed with the audit results and understood that the final report will be issued to Caltrans.

Restricted Use

This report is solely for the information and use of Napa County Department of Public Works; 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, CPA
Chief, Division of Audits

July 13, 2015

Schedule 1—
Summary of Proposed, Audited, and Adjusted Direct Costs, Indirect Costs, and Indirect Cost Rate
FY 2007-08 through FY 2008-09

Description of Costs	Proposed Amount FY 2007-08	Audited Amount FY 2007-08	Adjustments	Proposed Amount FY 2008-09	Audited Amount FY 2008-09	Adjustments
Direct Costs						
Salaries and benefits	$ 3,104,101	$ 3,080,294	$ (23,807)	$ 3,152,636	$ 3,167,550	$ 14,914 [1]
Indirect Costs			–			–
Salaries and benefits	321,505	460,274	138,769	418,282	527,716	109,434 [1]
Other Indirect Costs						
Services, supplies, and other			–			–
Communications	4,251	4,251	–	4,262	4,262	–
Insurance	191,030	191,030	–	310,873	310,873	–
Equipment Maintenance	3,978	3,978	–	4,010	4,010	–
Memberships	3,160	3,160	–	3,224	3,224	–
Office Expense	21,437	21,437	–	18,925	18,925	–
Computer Services	166,179	166,179	–	169,430	169,430	–
Publications/legal notices	9,738	–	(9,738) [2]	5,808	5,808	–
Equipment Leases/Rent	3,088	3,088	–	3,097	3,097	–
Professional Services	–	–	–	121,115	121,115	–
Software License(autocad)	7,780	7,780	–	8,993	8,993	–
Transportation and travel	7,622	7,622	–	6,275	6,275	–
Mileage	25,589	25,589	–	23,232	23,232	–
Training	6,055	6,055	–	8,794	8,794	–
A-87 Costs FY 07/08 Proposed	285,246	285,246	–	415,427	415,427	–
A-87 Costs FY 05/06 Roll Forward	55,244	55,244	–	88,811	88,811	–
Subtotal	790,397	780,659	–	1,192,276	1,192,276	–
Total Indirect Costs	1,111,902	1,240,933	–	1,610,558	1,719,992	–
Divide by Direct Salaries and Benefits	3,104,101	3,080,294	–	3,152,636	3,167,550	–
Indirect Cost Rate	35.82%	40.29%	4.47%	51.09%	54.30%	3.21%

[1] See Finding 1
[2] See Finding 2

Findings and Recommendations

FINDING 1—Misclassified Labor Costs

The County misclassified $(23,807) of direct labor costs and $138,769 of indirect labor costs for fiscal year (FY) 2007-08 and; $14,914 of direct and $109,434 of indirect labor costs for FY 2008-09. As a result, for FY 2007-08, direct salaries were overstated while indirect salaries were understated, and for FY 2008-09, both direct and indirect salaries were understated. The Department of Public Works' (DPW) administration staff also works on Flood Division Projects. In an attempt to exclude the administrative salaries of employees working on flood-related projects, the DPW estimated the time each administrative staff member spends working on flood projects and used the percentage result to apply to its total salaries; this dollar amount became the unallowable flood-project salaries. However, in this methodology, the wrong salary amount was excluded.

Our audit identified instances in which administrative staff works on projects for the Flood Division. The staff can use charge codes that would segregate work such as flood indirect time. Therefore, when compiling indirect salary costs for the Indirect Cost Rate Proposal (ICRP), the DPW should use only the Engineering indirect salary and exclude such salary codes as flood-project indirect salaries.

Title 2, *Code of Federal Regulations*, Part 225 (2 CFR 225), Appendix A. F.1. states in part that:

> Indirect costs are those: Incurred for a common or joint purpose benefiting more than one cost objective, and not readily assignable to the cost objective specifically benefitted, without effort disproportionate to the results achieved. The term "indirect costs," as used herein, applies to costs of this type originating in the grantee department, as well as those incurred by other departments in supplying goods, services, and facilities. . . . Indirect cost pools should be distributed to benefitted cost objectives on bases that will produce an equitable result in consideration of relative benefits derived.

Recommendation

We recommend that Caltrans request that the County revise and resubmit the ICRP excluding those salaries that are flood-related. Doing so will allow the county to properly classify these direct and indirect salaries. The County should also implement policies and procedures to ensure that only reasonable, allowable, and allocable costs are included in the indirect cost pool.

FINDING 2—Unallowable Indirect Costs

Napa County DPW included $9,738 of unallowable indirect publications costs. In order for publications costs to be an allowable charge, they must be for the benefit of federal projects. The costs included by the County were for private residents who were requesting information on their lot lines; these costs were not for the benefit of federal projects.

2 CFR 225, Appendix B. 1.c (1-4) states:

c. The only allowable advertising costs are those which are solely for:

(1) The recruitment of personnel required for the performance by the governmental unit of obligations arising under federal award;

(2) The procurement of good and services for the performance of a federal award;

(3) The disposal of scrap or surplus materials acquired in the performance of a federal award except when governmental units are reimbursed for disposal costs at a predetermined amount; or

(4) Other specific purposes necessary to meet the requirements of the federal award.

Recommendation

We recommend that Caltrans request that the County revise and resubmit the ICRP excluding unallowable indirect publication costs. The County should ensure that these costs are not included in the indirect cost pool.

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