

# Memorandum

*Making Conservation  
a California Way of Life.*

To: RYAN DERMODY  
Acting Chief  
Division of Transportation Planning

Date: May 14, 2019

File: P1580-0028

From: MARSUE MORRILL, CPA *Marsue*  
Chief  
Planning and Modal Office  
Independent Office of Audits and Investigations

Subject: **INDIRECT COST ALLOCATION PLAN AUDIT – SAN JOAQUIN COUNCIL OF GOVERNMENTS**

At the request of the Independent Office of Audits and Investigations, the California Department of Finance, Office of Audits and Evaluations (Finance) completed an audit of the San Joaquin Council of Governments' (SJCOG) Indirect Cost Allocation Plan (ICAP) for fiscal year 2017/18. The purpose of the audit was to determine whether the ICAP was presented in accordance with Title 2 Code of Federal Regulations (CFR) Part 200 and Caltrans Local Assistance Procedures Manual (LAPM) Chapter 5. In addition, the audit was performed to determine whether SJCOG had an adequate financial management system, which includes procurement, in accordance with 2 CFR 200 and LAPM Chapter 10. The complete audit report is attached.

Based on the audit, Finance determined that SJCOG's ICAP was not in compliance with 2 CFR 200. Finance found weaknesses in SJCOG's financial management system and identified unallowable costs that impacted the indirect cost rate. In addition, Finance identified unallowable overpayments to SJCOG in two fiscal years totaling \$535,042. Below is the audited indirect cost rate. SJCOG will need to reconcile their FY 2017/18 billings to the California Department of Transportation (Caltrans) using the audited rate and reimburse Caltrans the difference.

Rate Type	Previously Accepted Rate	Audited Rate
Indirect Cost	168.29%	<b>160.69%</b>

In addition, SJCOG will need to reimburse Caltrans for the overpayments identified above.

Please provide our office with a corrective action plan addressing all the recommendations in the audit report, including time lines, by July 17, 2019.

If you have any questions, contact Luisa Ruvalcaba, Audit Manager, at [luisa.ruvalcaba@dot.ca.gov](mailto:luisa.ruvalcaba@dot.ca.gov)

RYAN DERMODY

May 14, 2019

Page 2 of 2

- c: Andrew T. Chesley, Executive Director, San Joaquin Council of Governments  
Steve Dial, Deputy Executive Director/Chief Financial Officer, San Joaquin Council of Governments  
Rodney Whitfield, Director of Financial Services, Federal Highway Administration  
Tashia Clemons, Director, Planning and Environment, Federal Highway Administration  
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Dan McElhinney, District Director, District 10, Caltrans  
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Luisa Ruvalcaba, Audit Manager, Independent Office of Audits and Investigations, Caltrans  
Lisa Gore, Associate Accounting Analyst, Division of Accounting, Caltrans  
P1580-0028



## San Joaquin Council of Governments

Indirect Cost Allocation Plan

Fiscal Year 2017-18

Report No. 19-2660-015  
April 19, 2019

### **Team Members**

Cheryl L. McCormick, CPA, Chief  
Sherry Ma, CRP, Manager  
Kylie Oltmann, CPA, Supervisor  
Zuber Tejani, Lead  
Muang Saeteurn

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

You can contact our office at:

California Department of Finance  
Office of State Audits and Evaluations  
915 L Street, 6<sup>th</sup> Floor  
Sacramento, CA 95814  
(916) 322-2985

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Transmitted via e-mail

April 24, 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— San Joaquin Council of Governments, Indirect Cost Allocation Plan Audit**

The California Department of Finance, Office of State Audits and Evaluations, has completed its audit of the San Joaquin Council of Governments' (SJCOG) Indirect Cost Allocation Plan for fiscal year 2017-18.

The enclosed report is for your information and use. SJCOG's response to the report findings and our evaluation of the response are incorporated into the final report. This report will be placed on our website.

If you have any questions regarding this report, please contact Sherry Ma, Manager, or Kylie Oltmann, Supervisor, at (916) 322-2985.

Sincerely,

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

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## BACKGROUND

The California Department of Transportation's (Caltrans) Division of Transportation Planning (Division) articulates a long-term vision for California's transportation system and implements statewide transportation policy through partnerships with state, regional, and local agencies. The Division provides quality planning products, services, and information to support and guide transportation investment decisions.<sup>1</sup>

The San Joaquin Council of Governments (SJCOG) created in 1968, is a joint-powers authority comprised of the County of San Joaquin and the cities of Stockton, Lodi, Manteca, Tracy, Ripon, Escalon, and Lathrop. SJCOG is governed by a 12-voting member Board of Directors. SJCOG fosters intergovernmental coordination within San Joaquin County and neighboring jurisdictions; other regional agencies in the San Joaquin Valley; the State of California; and various Federal agencies.

SJCOG is both a Metropolitan Planning Organization (MPO) and a Regional Transportation Planning Agency (RTPA). As a MPO, SJCOG is responsible for carrying out federal guidelines and statutes for planning and coordination as well as approving and programming federal transportation funds on transit and street and road projects. As a RTPA, SJCOG is responsible for administering and allocating Transportation Development Act funds for public transit and possible road and street projects as well as adopting a Regional Transportation Plan for the region's boundaries, which include planning and coordination responsibilities over most federal and state funding programs for transportation administered by the State of California.<sup>2</sup>

At the discretion of local governmental agencies (LGA), including MPOs, indirect costs may be recovered when seeking reimbursement for federal-aid transportation projects and state funded projects. To recover indirect costs, LGAs and MPOs annually submit an Indirect Cost Allocation Plan (ICAP), 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 and MPOs to bill Caltrans and seek reimbursement of costs, which IOAI may audit for compliance with Title 2 Code of Federal Regulations (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 SJCOG's ICAP for fiscal year 2017-18.

The audit objective was to determine if the 2017-18 ICAP, including the fringe benefit rate, was in compliance with 2 CFR 200 and the LAPM. The 2017-18 ICAP and fringe benefit rate include transactions related to actual costs incurred and billed to Caltrans in 2015-16.

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<sup>1</sup> Caltrans Division of Transportation Planning website <http://www.dot.ca.gov/transplanning/>

<sup>2</sup> Excerpts were obtained from San Joaquin Council of Governments website <https://www.sjco.org/145/About>



Additionally, at the request of IOAI, we expanded our scope to include SJCOG's 2017-18 actual direct labor costs to determine compliance with 2 CFR 200 and the LAPM. Our audit of the 2017-18 actual direct labor costs could impact SJCOG's ICAP for 2019-2020, when submitted.

SJCOG is responsible for preparing its ICAP 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.

## **METHODOLOGY**

In planning the audit, we gained an understanding of SJCOG operations, and identified relevant ICAP requirements by reviewing 2 CFR 200, the LAPM, the Master Fund Transfer Agreement (MFTA), and applicable SJCOG policies and procedures, and interviewing key Caltrans and SJCOG personnel.

We conducted a risk assessment, including evaluating whether key internal controls relevant to our audit objective such as reviews and approvals, reconciliations, and separation of duties were properly designed, implemented, and operating effectively. Our assessment included observing processes and testing transactions related to accounts payable, time keeping/payroll, billing, cash disbursements, and cash reconciliations for effectiveness of existing documented processes and procedures. Deficiencies in internal control 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 SJCOG's financial management system, RCMS and New World. Our assessment included reviewing information process flows, testing transactions for completeness and accuracy, and determining if costs were separately categorized by tracing to accounting records. We determined the financial management system data was not sufficiently reliable for the purpose of our 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
<p>Determine whether the 2017-18 ICAP is in compliance with 2 CFR 200 and the LAPM.</p>	<ul style="list-style-type: none"> <li>• Selected a non-generalizable sample of 2015-16 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, fringe benefit, and the indirect costs pool.               <ul style="list-style-type: none"> <li>○ Sample selection for direct and indirect salaries was based on quantitative factors such as total hours charged; and qualitative factors such as the type (i.e. description) of costs.</li> <li>○ The most quantitatively significant fringe benefit costs were selected for testing.</li> <li>○ Sample selection for indirect costs pool were based on quantitative factors such as costs with a potential impact to the ICAP rate by 1 percent or greater; and qualitative factors such as the timing and type (i.e. description) of costs.</li> </ul> </li> <li>• Determined if direct and indirect salaries were allowable, supported, segregated, and allocated, by tracing amounts and task coding to accounting records, reviewing timesheets and payroll records, interviewing key staff, reviewing SJCOG's organizational chart, and comparing actual tasks performed to eligible Work Element (WE) tasks.</li> <li>• Determined if fringe benefit costs were allowable, supported, segregated, and allocated, by interviewing key staff, reviewing invoices to ensure accurate coding, tracing amounts to accounting records, and comparing education reimbursement documents to SJCOG's employee handbook.</li> <li>• Determined if indirect costs pool were allowable, supported, segregated, and allocated, by interviewing key staff, reviewing invoices for accurate coding, comparing vendor invoice descriptions to vendor websites for services provided, reviewing bank transaction and source documents to ensure costs were not for personal use as defined by 2 CFR 200, comparing travel expense claims to CalHR per diem rates, and verifying SJCOG's facility was used in its entirety by conducting onsite visit of the three-story building.</li> <li>• Verified the actual indirect costs recovered by SJCOG were billed at the Caltrans approved indirect cost rate by dividing the total indirect costs pool by direct salaries and wages.</li> <li>• Verified the actual fringe benefit costs recovered by SJCOG were billed at the Caltrans approved fringe benefit cost rate by dividing the total fringe benefit cost by direct salaries and wages.</li> <li>• Recalculated a proposed ICAP rate as a result of indirect costs pool audit adjustments greater than 1 percent.</li> </ul>



Audit Objective	Methods
Determine whether the 2017-18 direct labor costs are in compliance with 2 CFR 200 and the LAPM.	<ul style="list-style-type: none"> <li>• Selected a non-generalizable sample of 2017-18 direct salaries to verify compliance with 2 CFR 200 and the LAPM. <ul style="list-style-type: none"> <li>○ Sample selection was based on quantitative factors such as total hours charged; and qualitative factors such as the type (i.e. description) of costs.</li> </ul> </li> <li>• Determined if direct salaries were allowable, supported, segregated, and allocated, by tracing amounts to the accounting records, reviewing timesheets and payroll records, interviewing key staff, and comparing actual tasks performed to eligible WE tasks.</li> </ul>

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 obtained, we determined SJCOG's 2017-18 ICAP is not in compliance with 2 CFR 200 and the LAPM. We identified weaknesses in SJCOG's financial management system's ability to accumulate and segregate reasonable, allowable, and allocable project costs as noted in Finding 1. Additionally, as described in Finding 2, we identified unallowable costs that impacted the 2017-18 ICAP rate and recommend a rate change decrease of 7.60 percent as identified in Table 1 below. No change to the fringe benefit rate was identified. Further, a review of the 2017-18 actual direct labor costs as noted in Finding 3 could impact SJCOG's ICAP for 2019-20, when submitted.

**Table 1 – Accepted and Audited 2017-18 ICAP and Fringe Benefit Rates<sup>3</sup>**

Rate Type	Accepted Rate	Audited Rate	Difference
ICAP	168.29%	160.69 %	(7.60%)
Fringe Benefit	62.02%	62.02%	0%

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

## FINDINGS AND RECOMMENDATIONS

### Finding 1: Inadequate and Inconsistent Internal Practices

SJCOG does not have adequate time reporting practices and does not consistently comply with its internal practices. Specifically, 17 of 30 staff timesheets sampled identified staff charging to direct projects for attending an eight-hour general, non-project related all-staff training. SJCOG believed the training was beneficial to direct projects; therefore, did not instruct staff to charge the hours to an indirect charge code. Similarly, 3 of the 30 staff timesheets charged hours to direct projects using a pre-established ratio based on the budget instead of actual hours worked. Due to a lack of Board-approved written policies outlining time reporting practices, SJCOG staff are inaccurately reporting time, thereby, overstating direct labor costs to some direct work elements that may result in overbilled labor costs to Caltrans. Further, without proper segregation of time related to direct and indirect activities, SJCOG's future calculation of indirect cost allocation rates would be misstated.

Additionally, SJCOG is not ensuring their education reimbursement policy is consistently followed. SJCOG's Employee Handbook Amendment Memo (Memo), issued August 2013, allow education reimbursements for 50 percent of tuition, registration, books, and fees. However, SJCOG's management made an exception and approved reimbursements in excess of the policy. The Memo does not allow for exceptions. Inconsistent application of internal policies results in inaccurate amounts reported and overstating fringe benefit.

2 CFR 200.302 (a) requires each state to expend and account for the Federal award in accordance with state laws and procedures for expending and accounting for the state's own

<sup>3</sup> The ICAP and Fringe Benefit Rate submitted by SJCOG was approved by Caltrans on April 26, 2018.

funds. In addition, the state's and the other non-Federal entity's financial management systems, including records documenting compliance with Federal statutes, regulations, and the terms and conditions of the Federal award, must be sufficient to permit the preparation of reports required by general and program specific terms and conditions; and the tracing of funds to a level of expenditures adequate to establish that such funds have been used according to the Federal statutes, regulations, and the terms and conditions of the Federal award.

2 CFR 200.302 (b) (4) requires the financial management system of each non-federal entity to provide effective control over, and accountability for, all funds, property, and other assets. Further, 2 CFR 200.303 (a) requires maintainance of effective internal control over the Federal award and provide reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award.

2 CFR 200.400 (a) requires efficient and effective administration of the Federal award through the application of sound management practice. In addition, 2 CFR 200.400 (b) requires administering federal funds in a manner consistent with underlying agreements, program objectives, and the terms and conditions of the federal awards. Further, 2 CFR 200.403 (c) requires costs be consistent with policies and procedures and applied uniformly to both federally-financed and other activities of the non-Federal entity. Similarly, 2 CFR 200.413 (a) requires costs incurred for the same purpose in like circumstances be treated consistently as either direct or indirect costs.

#### **Recommendations:**

- A. Develop procedures that defines appropriate charging practices for direct and indirect activities.
- B. Develop review procedures to ensure direct billing to Caltrans are based on actual labor costs incurred.
- C. Obtain Board approval for internal policies and ensure those polices, such as the timekeeping and education reimbursement, are consistently adhered and applied.

#### **Finding 2: Unallowable Costs Included in the Indirect Cost Pool**

SJCOG's indirect cost pool included unallowable and unsupported costs totaling \$146,512. Specifically, we reviewed 142 transactions within 11 indirect cost categories and identified the following:

- Membership costs for the Self-Help Counties Coalition and the National Association of the Regional Council, totaling \$11,692, are for associations that perform lobbying activities. The costs on the invoices did not distinguish between lobbying and non-lobbying activities; therefore, the total costs were disallowed. 2 CFR 200.450 (a) states costs of certain influencing activities associated with obtaining grants, contracts, cooperative agreements, or loans is unallowable.
- Office Expense costs, totaling \$4,844, for late fees and purchases of personal use items such as coffee, carbonated beverages, paper plates, and cups as well as other unsupported costs were incurred. 2 CFR 200.441 states costs resulting from violations or failure to comply with federal, state, tribal, local, or foreign laws and regulations are unallowable. Additionally, 2 CFR 200.445 and 2 CFR 200.403 (g) states goods or services for personal use are unallowable and must be adequately documented, respectively.

- Professional and Special Services costs, totaling \$21,232, for personal use of water filters and legal and sales tax reporting costs related to direct projects were included. 2 CFR 200.445 states goods or services for personal use are unallowable. Further, 2 CFR 200.413 (a) states costs that can be identified specifically with a particular final cost objective or, be directly assigned to such activities relatively easily with a high degree of accuracy, must be treated consistently as either direct or indirect costs.
- Transportation, Travel, and Training costs totaling \$783 for per diem and hotel rates that are in excess of California Department of Human Resources (CalHR) allowable amounts as well as unsupported expenses were included. MFTA Section 2 executed November 30, 2014 for the period covering January 1, 2015 through December 31, 2024 states that payments for travel expenses are not to exceed rates under current CalHR policies. Additionally, 2 CFR 200.403 (g) states costs must be adequately documented.
- Facility-related costs totaling \$107,960 were charged for SJCOG's third floor office building, which was vacant and structurally undeveloped for occupancy as of October 11, 2018. Caltrans' 2009-10 prior audit<sup>4</sup> identified the same third floor as being vacant and disallowed 33 percent of the associated building costs. Additionally, SJCOG estimated and Caltrans accepted, five percent as an appropriate measure for disallowed utilities with the understanding that SJCOG's utility bill does not delineate the cost by floor and it would be difficult to determine when the usage of gas and electric occurred for the third floor. SJCOG accepted the same disallowed percentages to be applied for this current finding. Discussions with SJCOG indicated that the vacant floor was anticipated to be leased. 2 CFR 200.46 states the costs for idle facilities are not allowable. See Table 2 for disallowed costs related to the idle facility.

**Table 2 – Unallowable Idle Facility Costs**

<b>2015-16 Costs Categories</b>	<b>Amounts Claimed as Indirect Costs (a)</b>	<b>Unallowable Percent (b)</b>	<b>Unallowable Amount (c = a*b)</b>
Depreciation	\$ 177,566	33%	\$ 58,597
Insurance	99,018	33%	32,676
Interest – Building Debt Service	30,672	33%	10,122
Maintenance – Taxes	7,588	33%	2,504
Maintenance - Utilities (gas and electric)	81,211	5%	4,061
<b>Total Unallowable Facility Costs</b>			<b>\$ 107,960</b>

SJCOG has established and implemented a review process to verify only allowable costs are included within the indirect cost pool. However, SJCOG did not perform a comprehensive review. As a result of not properly segregating and excluding unallowable costs from the indirect cost pool, adjustments to the indirect cost pool may affect the accepted rate.

**Recommendations:**

- Adjust the 2015-16 actual indirect cost pool by \$146,512 for the unallowable costs and ensure these costs are not included in future indirect cost pools. In addition, SJCOG must reconcile their 2017-18 billings using the audited rate of 160.69 percent and reimburse Caltrans any overpayments.

<sup>4</sup> Caltrans' SJCOG Audit of Indirect Cost Allocation Plan for Fiscal Year 2009-10 issued June 4, 2012.

- B. Review all indirect accounts to ensure costs are in compliance with 2 CFR 200, properly segregated between direct, indirect, and unallowable costs, and supported by original source documentation.
- C. Ensure SJCOG’s travel policies and procedures and MFTA provisions related to travel are adhered.

**Finding 3: Unallowable Direct Labor Costs**

SJCOG inaccurately charged a total of \$535,042 of direct labor hours (1038.5 and 816 hours for 2015-16 and 2017-18, respectively), to a cost category designated for a specific purpose. The cost category, referred as Work Element (WE) 1001.01 SJCOG Overall Work Program (OWP) Administration, is for the development of the OWP, preparation of the annual budget and amendments to the budget, and preparation of the quarterly progress reports (QPR). SJCOG stated the hours charged were for reviewing/approving consultant invoices, timesheets, and other general administrative tasks, not the designated eligible tasks. This error was due to SJCOG being unfamiliar with the eligible tasks for WE 1001.01. As a result, the total indirect and fringe benefit costs were affected and the QPRs inaccurately reported the work actually performed. For detail of the disallowed costs, see Table 3.

**Table 3 – Unallowable Direct Labor, Indirect, and Fringe Benefit Costs**

Category	2015-16	2017-18
Direct Labor (a)	\$82,457	\$69,487
Accepted Indirect Cost Rate (b)	178.64%	168.29%
Indirect Cost Amount (c=a*b)	\$147,301	\$116,940
Accepted Fringe Benefit Rate (d)	91.88%	62.02%
Fringe Benefit Amount (e=a*d)	\$75,761	\$43,096
<b>Total Unallowable Costs (a+c+e)</b>	<b>\$305,519</b>	<b>\$229,523</b>

SJCOG’s MFTA Article III, Section 1.A states a MPO agrees to comply with 2 CFR 200. 2 CFR 200.302 (b) (2) requires accurate, current, and complete disclosure of the financial results of each Federal award or program in accordance with the outlined reporting requirements.

In addition, 2 CFR 200.303 (a) requires the non-Federal entity to establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. Further, 2 CFR 200.405 (c) states any costs allocable to a particular Federal award may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by Federal statutes, regulations, or terms and conditions of the Federal awards, or for other reasons.

**Recommendations:**

- A. Reimburse Caltrans for overpayment of \$305,519 in unallowable costs for 2015-16 and \$229,523 for 2017-18.<sup>5</sup>
- B. Ensure personnel responsible for preparing and reviewing billings are familiar with each work element’s eligible tasks and report accurate QPRs accordingly.

<sup>5</sup> Adjustments to the direct cost pool is not allowed until SJCOG reimburses Caltrans.

# APPENDIX A

Summary of Accepted and Audited Costs and Rates  
Indirect Cost Allocation Plan  
San Joaquin Council of Governments  
2017-18

Description	Accepted Amounts <sup>6</sup>	Audit Adjustments	Audited Amounts	Finding No.
<b>Direct Costs</b>				
Salaries and Wages	\$ 1,353,172	\$ 0 <sup>7</sup>	\$ 1,353,172	
<b>Indirect Costs Pool</b>				
Salaries and Wages	\$ 1,290,402	\$ 0	\$ 1,290,402	
Office Expense	140,119	(4,844)	135,275	2
Communications	44,969	0	44,969	
Memberships	43,489	(11,693)	31,796	2
Rent - Equipment	148,393	0	148,393	
Capital Lease Interest Payments	2,472	0	2,472	
Transportation, Travel and Training	16,756	(783)	15,973	2
Professional and Special Services	180,085	(21,232)	158,853	2
Departmental Costs Allocated	1,341	0	1,341	
Insurance	99,018	(32,676)	66,342	2
Rents - Other	984	0	984	
Interest - Building Debt Service	30,672	(10,122)	20,550	2
Maintenance - Equipment	6,198	0	6,198	
Maintenance- Building and Grounds - Taxes	88,076	(2,504)	85,572	2
Maintenance - Building and Grounds - Utilities	88,222	(4,061)	84,161	2
Depreciation	367,374	(58,597)	308,777	2
<b>Total Indirect Costs Pool</b>	<b>\$ 2,548,570</b>	<b>\$ (146,512)</b>	<b>\$ 2,402,058</b>	
Carry Forward (2015-16)	\$ 708,855	\$ 0	\$ 708,855	
Adjustments to Indirect Cost	0	(146,512)	(146,512)	2
<b>Total Carry Forward Adjustments</b>	<b>\$ 708,855</b>	<b>\$ (146,512)</b>	<b>\$ 562,343</b>	2
Budgeted Indirect Costs	\$ 2,534,856	\$ 0	\$ 2,534,856	
Total Indirect Costs*	3,243,711	(146,512)	3,097,199	2
Total Direct Salaries and Wages	1,927,415	0	1,927,415	
<b>Indirect Cost Rate**</b>	<b>168.29%</b>	<b>(7.60%)</b>	<b>160.69%</b>	2
*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				

<sup>6</sup> The ICAP and Fringe Benefit Rate submitted by SJCOG was approved by Caltrans on April 26, 2018.

<sup>7</sup> Adjustments to direct costs from Finding 3 is not allowed until SJCOG reimburses Caltrans.



# APPENDIX B

Summary of Accepted and Audited Costs and Rates  
Fringe Benefit Rate  
San Joaquin Council of Governments  
2017-18

Description	Accepted Amounts	Audit Adjustments	Audited Amounts
<b>Direct Costs</b>			
Salaries and Wages	\$ 1,353,172	\$ 0 <sup>8</sup>	\$1,353,172
<b>Fringe Benefit Costs Pool</b>			
AFLAC Insurance	\$ 336	\$ 0	\$ 336
401 Employee Retirement	186,456	0	186,456
457 Employee Retirement	26,839	0	26,839
Cafeteria	252,311	0	252,311
Medicare	32,282	0	32,282
Group Dental	18,765	0	18,765
Dependent Dental Clearing	75	0	75
Group Medical	168,556	0	168,556
Dependent Medical Clearing	29,115	0	29,115
Vision	3,472	0	3,472
Dependent Vision Clearing	15	0	15
Workers Compensation	15,411	0	15,411
Life Insurance	2,804	0	2,804
Supplement Life Insurance Clearing Account	139	0	139
Payroll Clearing Account In Shape	201	0	201
Unemployment Insurance	10,919	0	10,919
Employment Training Tax	252	0	252
Long Term Care Insurance	6,135	0	6,135
LTC Employee Clearing Account	327	0	327
Disability Insurance	24,623	0	24,623
Educational Reimbursement <sup>9</sup>	10,838	0	10,838
<b>Total Fringe Benefit Costs Pool</b>	<b>\$ 789,872</b>	<b>\$ 0</b>	<b>\$ 789,872</b>
Carry Forward (2015-16)	\$ (20,773)	\$ 0	\$ (20,773)
Budgeted Fringe Benefit Costs	1,216,209	0	1,216,209
<b>Total Fringe Benefit Costs*</b>	<b>1,195,436</b>	<b>0</b>	<b>1,195,436</b>
Budgeted Direct Salaries and Wages	1,927,415	0	1,927,415
<b>Fringe Benefit Cost Rate**</b>	<b>62.02%</b>	<b>0%</b>	<b>62.02%</b>
*Total Fringe Benefit Costs is the sum of Carry Forward (2015-16) and Budgeted Fringe Benefit Costs.			
**Fringe Benefit Cost Rate is the quotient of Total Fringe Benefit Costs divided by Budgeted Direct Salaries and Wages.			

<sup>8</sup> Adjustments to direct costs from Finding 3 is not allowed until SJCOG reimburses Caltrans.

<sup>9</sup> As noted in Finding 1, this category had an exception. However, materiality of exception did not require an adjustment to the fringe benefit rate.





**SAN JOAQUIN COUNCIL OF GOVERNMENTS**

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April 2, 2019

*Robert Rickman*  
CHAIR

*Doug Kuehne*  
VICE CHAIR

*Andrew T. Chesley*  
EXECUTIVE DIRECTOR

*Member Agencies*  
CITIES OF  
ESCALON,  
LATHROP,  
LODI,  
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STOCKTON,  
TRACY,  
AND  
THE COUNTY OF SAN  
JOAQUIN

Sherry Ma  
California Department of Finance  
Office of State Audits and Evaluations  
915 L Street, 6<sup>th</sup> Floor  
Sacramento, CA 95814

Subject: Management Responses to Report #19-2660-015, Audit Findings Letter for FY 17/18 ICAP

Dear Ms. Ma:

This letter is written in response to Department of Finance, Office of State Audits and Evaluations audit findings letter dated March 19, 2019. The following are SJCOG’s summary responses to the items noted on your letter.

**AUDIT RESULTS**

Based on the procedures performed and evidence obtained, it was determined SJCOG’s 2017-18 ICAP was not in compliance with 2 CFR 200 and LAPM. Weaknesses were identified in SJCOG’s financial management system’s ability to accumulate and segregate reasonable, allowable, and allocable project costs as noted in Finding#1. Additionally, as described in Finding #2, unallowable costs were identified that impacted the 2017-18 ICAP rate and recommend a rate change decrease of 7.6 percent as identified in Table 1 below. No change to the fringe benefit rate was identified. Further, a review of the 2017-18 actual direct labor costs as noted in Finding #3 could impact SJCOG’s ICAP for 2019-20 when submitted.

**Table 1 – Summary of Accepted and Audited 2017-18 ICAP and Fringe Benefit Rates<sup>3</sup>**

Rate Type	Accepted Rate	Audited Rate	Difference
ICAP	168.29%	160.69 %	(7.60%)
Fringe Benefit	62.02%	62.02%	0%

<sup>3</sup> The ICAP and Fringe Benefit Rate submitted by SJCOG was approved by Caltrans on April 26, 2018.

## **Audit Findings**

### **Finding 1: Inadequate and Inconsistent Internal Practices**

SJCOG does not have adequate time reporting practices and does not consistently comply with its internal practices. Specifically, 17 of 30 staff timesheets sampled identified staff charging to direct projects for attending an eight-hour general, non-project related all-staff training. SJCOG believed the training was beneficial to direct projects; therefore, did not instruct staff to charge the hours to an indirect charge code. Similarly, 3 of the 30 staff timesheets charged hours to direct projects using a pre-established ratio based on the budget instead of actual hours worked. Due to a lack of Board-approved written policies outlining time reporting practices, SJCOG staff are inaccurately reporting time, thereby, overstating direct labor costs to some direct work elements that may result in overbilled labor costs to Caltrans. Further, without proper segregation of time related to direct and indirect activities, SJCOG's future calculation of indirect cost allocation rates would be misstated.

Additionally, SJCOG is not ensuring their education reimbursement policy is consistently followed. SJCOG's Employee Handbook Amendment Memo (Memo), issued August 2013, allow education reimbursements for 50 percent of tuition, registration, books, and fees. However, SJCOG's management made an exception and approved reimbursements more than the policy. The Memo does not allow for exceptions. Inconsistent application of internal policies results in inaccurate amounts reported and overstating fringe benefit.

2 CFR 200.302 (a) requires each state to expend and account for the Federal award in accordance with state laws and procedures for expending and accounting for the state's own funds. In addition, the state's and the other non-Federal entity's financial management systems, including records documenting compliance with Federal statutes, regulations, and the terms and conditions of the Federal award, must be sufficient to permit the preparation of reports required by general and program specific terms and conditions; and the tracing of funds to a level of expenditures adequate to establish that such funds have been used according to the Federal statutes, regulations, and the terms and conditions of the Federal award

2 CFR 200.302 (b) (4) requires the financial management system of each non-federal entity to provide effective control over, and accountability for, all funds, property, and other assets. Further, 2 CFR 200.303 (a) requires maintenance of effective internal control over the Federal award and provide reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award.

2 CFR 200.400 (a) requires efficient and effective administration of the Federal award through the application of sound management practice. In addition, 2 CFR 200.400 (b) requires administering federal funds in a manner consistent with underlying agreements, program objectives, and the terms and conditions of the federal awards. Further, 2 CFR 200.403 (c) requires costs be consistent with policies and procedures and applied uniformly to both federally-financed and other activities of the non-Federal entity. Similar, 2 CFR 200.413 (a) requires costs incurred for the same purpose in like circumstances be treated consistently as either direct or indirect costs.

### **Recommendations:**

- A. Develop procedures that defines appropriate charging practices for direct and indirect activities.
- B. Develop review procedures to ensure direct billing to Caltrans are based on actual labor costs incurred.
- C. Obtain Board approval for internal policies and ensure those policies, such as the time keeping and education reimbursement, are consistently adhered and applied.

### **SJCOG Response**

**SJCOG Management does not disagree with the findings and reports:**

- A. Procedures are being developed and published defining appropriate charging practices for direct and indirect activities.**
- B. Procedures have been developed to ensure direct billing to Caltrans are based on actual labor costs incurred.**
- C. The necessary steps have been implemented to obtain Board approval for internal policies and ensure those policies, such as the time keeping and education reimbursement, are consistently adhered and applied.**

### **Finding 2: Unallowable Costs Included in the Indirect Cost Pool**

SJCOG's indirect cost pool included unallowable and unsupported costs totaling \$146,512. Specifically, we reviewed 142 transactions within 11 indirect cost categories and identified the following:

- Membership costs for the Self-Help Counties Coalition and the National Association of the Regional Council, totaling \$11,693, are for associations that perform lobbying activities. The costs on the invoices did not distinguish between lobbying and non- lobbying activities; therefore, the total costs were disallowed. 2 CFR 200.450 (a) states costs of certain influencing activities associated with obtaining grants, contracts, cooperative agreements, or loans is unallowable.
- Office Expense costs, totaling \$4,844, for late fees and purchases of personal use items such as coffee, carbonated beverages, paper plates, and cups as well as other unsupported costs were incurred. 2 CFR 200.441 states costs resulting from violations or failure to comply with federal, state, tribal, local, or foreign laws and regulations are unallowable. Additionally, 2 CFR 200.445 and 2 CFR 200.403 (g) states goods or services for personal use are unallowable and must be adequately documented, respectively.
- Professional and Special Services costs, totaling \$21,232, for personal use of water filters and legal and sales tax reporting costs related to direct projects were included. 2 CFR 200.445 states goods or services for personal use are unallowable. Further, 2 CFR 200.413 (a) states costs that can be identified specifically with a particular final cost objective or, be directly assigned to such activities relatively easily with a high degree of accuracy, must be treated consistently as either direct or indirect costs.
- Transportation, Travel, and Training costs totaling \$783 for per diem and hotel rates that are more than California Department of Human Resources (CalHR) allowable amounts as well

as unsupported expenses were included. MFTA Section 2 executed November 30, 2014 for the period covering January 1, 2015 through December 31, 2024 states that payments for travel expenses are not to exceed rates under current CalHR policies. Additionally, 2 CFR 200.403 (g) states costs must be adequately documented.

- Facility-related costs totaling \$107,960 were charged for SJCOG's third floor office building, which was vacant and structurally undeveloped for occupancy as of October 11, 2018. Caltrans' 2009-10 prior audit<sup>4</sup> identified the same third floor as being vacant and disallowed 33 percent of the associated building costs. Additionally, SJCOG estimated and Caltrans accepted, five percent as an appropriate measure for disallowed utilities with the understanding that SJCOG's utility bill does not delineate the cost by floor and it would be difficult to determine when the usage of gas and electric occurred for the third floor. SJCOG accepted the same disallowed percentages to be applied for this current finding. Discussions with SJCOG indicated that the vacant floor was anticipated to be leased. 2 CFR 200.46 states the costs for idle facilities are not allowable.

SJCOG has established and implemented a review process to verify only allowable costs are included within the indirect cost pool. However, SJCOG did not perform a comprehensive review. As a result of not properly segregating and excluding unallowable costs from the indirect cost pool, adjustments to the indirect cost pool may affect the accepted rate.

#### **Recommendation:**

- A. Adjust the 2015-16 actual indirect cost pool by \$146,512 for the unallowable costs and ensure these costs are not included in future indirect cost pools. In addition, SJCOG must reconcile their 2017-18 billings using the audited rate of 160.69 percent and reimburse Caltrans any overpayments.
- B. Review all indirect accounts to ensure costs are in compliance with 2 CFR 200, properly segregated between direct, indirect, and unallowable costs, and supported by original source documentation.
- C. Ensure SJCOG's travel policies and procedures and MFTA provisions related to travel are adhered.

#### **SJCOG Response**

- A. SJCOG Management is generally in agreement with the determination that certain office expense items and professional and special service items have been deemed unallowable. Purchasing procedures have been implemented with items separated at point of purchase to ensure allowable items are charged separately. Regarding the facility related charges, SJCOG believes, after previous negotiations with Caltrans determining the 3<sup>rd</sup> floor was being used for storage, we appropriately were including associated costs in the indirect cost calculation. Notwithstanding, SJCOG has agreed to the terms in the finding.**

**The necessary steps have been implemented to adjust the 2015-16 actual indirect cost pool by \$146,512 for the unallowable costs and ensure these costs are not included in**



**future indirect cost pools. In addition, SJCOG must reconcile their 2017-18 billings using the audited rate of 160.69 percent and reimburse Caltrans any overpayments.**

- B. The necessary steps have been implemented to review all indirect accounts to ensure costs follow 2 CFR 200, properly segregated between direct, indirect, and unallowable costs, and supported by original source documentation.**

**SJCOG continues to assert that a portion of membership dues for the Self-Help Counties Coalition and National Association of Regional Councils should be allowable indirect costs. SJCOG has provided documentation from both the SHCC and NARC executive directors quantifying the amount of “lobbying” undertaken by their respective organizations. This was provided to the auditors during their field work. Those documents are attached.**

- C. The necessary steps have been implemented to ensure SJCOG’s travel policies and procedures and MFTA provisions related to travel are adhered to. Additionally, SJCOG will be holding a workshop for employees reviewing travel policies and procedures.**

### **Finding 3: Unallowable Direct Labor Costs**

SJCOG inaccurately charged a total of \$535,042 of direct labor hours (1038.5 and 816 hours for 2015-16 and 2017-18, respectively), to a cost category designated for a specific purpose. The cost category, referred as Work Element (WE) 1001.01 SJCOG Overall Work Program (OWP) Administration, is for the development of the OWP, preparation of the annual budget and amendments to the budget, and preparation of the quarterly progress reports (QPR). SJCOG stated the hours charged were for reviewing/approving consultant invoices, timesheets, and other general administrative tasks, not the designated eligible tasks. This error was due to SJCOG being unfamiliar with the eligible tasks for WE 1001.01. As a result, the total indirect and fringe benefit costs were affected and the QPRs inaccurately reported the work actually performed.

SJCOG’s MFTA Article III, Section 1.A states a MPO agrees to comply with 2 CFR 200. 2 CFR 200.302(b) (2) requires accurate, current, and complete disclosure of the financial results of each Federal award or program in accordance with the outlined reporting requirements.

In addition, 2 CFR 200.303 (a) requires the non-Federal entity to establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. Further, 2 CFR 200.405 (c) states any costs allocable to a particular Federal award may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by Federal statutes, regulations, or terms and conditions of the Federal awards, or for other reasons.

### **Recommendation:**

- A. Reimburse Caltrans for overpayment of \$305,519 in unallowable costs for 2015-16 and \$229,523 for 2017-18.**

- B. Ensure personnel responsible for preparing and reviewing billings are familiar with each work element's eligible tasks and report accurate QPRs accordingly.

**SJCOG Response**

**SJCOG Management does not disagree with the findings and reports:**

- A. The necessary steps have been implemented to reimburse Caltrans in the amount of \$305,519 for 2015-16 and \$229,523 for 2017-18
- B. The necessary steps have been implemented to ensure personnel responsible for preparing and reviewing billings are familiar with each work element's eligible tasks and report accurate QPRs accordingly.

**Conclusion:**

SJCOG understands it is appropriate to improve efficiencies and accuracies and has taken corrective action as necessary.

If you have any questions or require further documentation, please contact Steve Dial via e-mail at [dial@sjcog.org](mailto:dial@sjcog.org) or via phone at (209) 235-0600 or Grace Orosco at [orosco@sjcog.org](mailto:orosco@sjcog.org).

Sincerely



STEVE DIAL  
Deputy Executive Director/CFO

**NATIONAL ASSOCIATION OF REGIONAL COUNCILS**

MEMO TO: Leslie Wollack, Executive Director

FROM: Lee Ruck, General Counsel

DATE: March 1, 2017

**SUBJECT: NARC Lobbying Expenditures: Budgeting and Accounting (2016)**

As a 501(c)(3) organization, our tax exemption is conditioned on lobbying expenditures as an “insubstantial” portion of total funds expended. As a non-profit recipient of federal grant or contract funds, by OMB Circular A-122, NARC is prohibited from a number of activities designed to influence legislation or liaise with legislative entities. Further, 31 US Code Section 1352 prohibits using federal grant or contract funds to influence the awarding, extension, or renewal of any contract or grant funds.

I have reviewed both NARC’s FY 2015 and FY 2016 budgets and FY 2016 unaudited financial statements to ascertain whether NARC is in compliance with the requirements of each regime. I find that NARC is in compliance based upon the assumptions and computations that follow

**FY 2016 ACTUAL**

**Assumptions concerning lobbying expenses:**

• 50% of salary of Erich Zimmerman attributed to lobbying	\$35,000
• 75% of fees to Bob Fogel attributed to lobbying	\$30,000
• 10% of salary of Leslie Wollack attributed to lobbying	\$15,000
• 10% of expenses of Annual Conference	\$13,000
• 50% of expenses of National Conference of Regions	\$45,000
<b>Total</b>	<b>\$138,000</b>

**Assumption of Non Federal Revenue**

Non federal contract or grant revenue must be identified so that such revenue may be used for “lobbying” purposes under on or another of the prohibition schemes.

**Total Revenues** **\$1,548,320**

**Total available for lobbying expenses (no lobbying restrictions)** **\$227,572**

Assumptions are based upon discussions with NARC’s Executive Director and Policy Manager, reviews of the FY 2016 NARC Budget, the FY 2015 approved Audit, Reports of the Financial Committee to the Board, and personal observations as counsel.

**Applicability of the Four Lobbying Restrictions**

**501(c)(3).** Based upon year-end analysis, NARC’s expenditures for FY15 were \$1,468,928. Based upon the formula in 501(h), NARC was authorized to expend up to 221,893 for lobbying. The most inclusive analysis of lobbying expenditures total \$138,000.

**Circular A-122.** NARC revenues other than federal grants or contracts far exceed the expenditures for lobbying and policy preparation; federal grant and contract dollars have not been used for such lobbying purposes.

**31 USC 1352.** Federal funds have not been used to influence the award, renewal, or extension of any federal grant or contract.

**2 CFR 225.** NARC revenues other than federal grants and contracts and membership dues (\$227,572) substantially exceed the expenditures for lobbying and policy preparation; membership dues have not been used for such lobbying purposes.

From: Keith Dunn <keithdunn@me.com>  
Date: Friday, October 19, 2018 at 11:44 AM  
To: Steve Dial <Dial@sjcog.org>  
Subject: Re: SHCC dues

Steve,  
60% of your San Joaquin County dues for Self Help Counties are Non-lobby related. They are used for Association activities. The remaining 40% are used towards lobbying activity.

Keith Dunn  
Executive Director  
Self Help Counties Coalition  
(916) 273-6567 office  
(916) 290-2900 cell

On Oct 19, 2018, at 9:52 AM, Steve Dial <Dial@sjcog.org> wrote:

Keith,  
Sorry to bother you. I know you are working on Focus (which I won't be able to attend this year), but you offered to get me something that stipulates the amount of lobbying SHCC does so I can support at least a portion of dues in our indirect cost plan.

Thanks,

Steve

# EVALUATION OF RESPONSE

SJCOG's response to the draft report has been reviewed and incorporated into the final report. We acknowledge SJCOG's willingness to implement our recommendations. SJCOG's response included comments for select portions of the draft audit report findings. SJCOG agreed to our findings and recommendations for Findings 1 and 3. We provide the following comments for Finding 2, where we believe further clarification is warranted.

## **Finding 2: Unallowable Costs Included in the Indirect Cost Pool**

### Membership Costs

SJCOG disagrees that the total cost of the membership dues for the National Association of Regional Councils (NARC) and Self-Help Counties Coalition (SHCC) should be disallowed and have included documentation to support its position within its response.

SJCOG provided the same documentation to us during fieldwork, which we stated the NARC documentation did not delineate the amount of lobbying and non-lobbying activities; therefore, all membership dues were disallowed. Further, subsequent documentation was not provided. Conversely, the documentation from SHCC was accepted as it identified what portion of its activities were for lobbying and non-lobbying. Forty percent of the invoice amount was disallowed due to its identification of lobbying activities. See the breakdown of the disallowed amounts below.

Organization	Applicable Invoice Period	Invoice Amount	Disallowed Percent	Disallowed Amount
NARC*	Jul 2015 – Dec 2015	\$4,966	100%	\$ 4,966
NARC*	Jan 2016 – Jun 2016	\$4,966	100%	\$ 4,966
SHCC		\$4,400	40%	\$ 1,760
Total				\$11,692

\* Total annual invoice was \$9,932. The annual invoice was based on calendar months; therefore, only the portion of the invoice applicable to fiscal year 2015-16 was considered.

### Facility-related Costs

SJCOG stated that although it agreed to the terms of the finding, it believes the facility charges related to the third floor were appropriately included in the indirect costs pool based on previous negotiations with Caltrans. SJCOG's assertion on October 16, 2014 indicated that the third floor was being used for storage and had no intention of subleasing any portion of the building. Therefore, Caltrans allowed SJCOG to include facility-related costs for the third floor. However, Caltrans advised SJCOG that if an audit was performed, the third floor was subject to inspection. During our fieldwork, we observed the third floor to be vacant and structurally undeveloped for occupancy; therefore, the third floor was considered an idle facility.

Because SJCOG did not provide additional supporting documentation, the finding and recommendation will remain unchanged.