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December 17, 2020

JEANIE WARD-WALLER  
DEPUTY DIRECTOR  
Planning and Modal Programs  
California Department of Transportation

Dear Ms. Ward-Waller:

The Independent Office of Audits and Investigations (IOAI) performed an incurred cost audit of the City of Santa Ana (City) of five projects with costs totaling \$2,632,460 reimbursed by the California Department of Transportation (Caltrans). The audit was performed to determine whether project costs claimed by the City were allowable, and adequately supported in accordance with respective Caltrans agreement provisions and state and federal regulations. The final audit report, including the City's response, is enclosed.

Based on our audit we determined that project costs totaling \$504,283 were not in compliance with Caltrans agreement provisions and state and federal regulations. In addition, we identified deficiencies with City's labor and indirect cost billing practices, procurement and contracting, construction management and project oversight, and project reporting and outcomes.

Please provide our office with a corrective action plan addressing the recommendations in the enclosed report, including timelines, by January 29, 2021.

Ms. Jeanie Ward-Waller  
December 17, 2020  
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If you have any questions contact MarSue Morrill, Audit Chief, at  
marsue.morrill@dot.ca.gov.

Sincerely,

RHONDA L. CRAFT  
INSPECTOR GENERAL

Enclosures  
Final Audit Report

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P1575-0062

# County of Alameda

## Incurred Cost Audit

Audit Report  
P1575-0063  
December, 2020



**PREPARED BY:**

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# **BACKGROUND, SUMMARY, OBJECTIVES, SCOPE, METHODOLOGY, VIEWS OF RESPONSIBLE OFFICIALS**

## **BACKGROUND**

The 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.

The City of Santa Ana (City) was established in 1952 as a charter city and adopted the council-manager form of government. The City provides a full range of municipal services, including but not limited to, the construction and maintenance of streets and related infrastructure, municipal utilities such as water, sewer, refuse and sanitation, and recreational activities. The City's Public Works Agency is responsible for the development and management of the City's Capital Improvement Program, which includes neighborhood street improvements, arterial widening, street reconstruction/resurfacing, traffic and infrastructure improvements, city facility improvements, and bikeway/park improvements.

## **SUMMARY**

The Independent Office of Audits and Investigations (IOAI) performed an incurred cost audit of five City projects with costs totaling \$2,632,460, reimbursed by the California Department of Transportation (Caltrans) as of June 30, 2019.

We identified questioned labor and indirect costs totaling \$504,283 that were not in compliance with Caltrans agreement provisions, and state and federal regulations. We also identified deficiencies with the City's labor and indirect cost billing practices, procurement and contracting, construction management and project oversight, and project reporting and outcomes. See Attachment A for a summary of questioned costs.

## **OBJECTIVES**

We performed the audit to determine whether project costs claimed and reimbursed were allowable, and adequately supported in accordance with Caltrans agreement provisions, and state and federal regulations. In addition, our audit included determining whether project deliverables/ outputs and benefits/outcomes were consistent with the project scope.

**SCOPE**

The audit scope included costs claimed and reimbursed during the period of July 1, 2016, through June 30, 2019, for the following projects:

Project Number	Project Name/Description	Amount
ATPL-5063 (160) / No. 16-6871	Safe Routes to School Enhancement for King Elementary	\$463,163
BTA 1213-12-ORA-04 / No. 14-6814	First Street Class II Bikeway	\$68,414
HSIPL-5063 (154) / No. 15-6830	Pedestrian Countdown Heads and Push Buttons	\$754,014
HSIPL-5063 (156) / No. 15-6834	Traffic Signal Modifications: Intersections of Edinger Ave. & Sullivan St., 17th & English Streets, MacArthur Blvd. & Plaza Dr., and Westminster Ave. & Clinton St.	\$941,989
STPL-5063 (176) / No. 17-6881	Fairview Street Pavement Improvements	\$404,880
Total Project Costs:	-	\$2,632,460

The audit was limited to financial and compliance activities. The audit was less in scope than an audit performed for expressing an opinion on the City's financial statements. Therefore, we did not audit, and are not expressing an opinion on the City's financial statements.

The City is responsible for the claimed costs and compliance with applicable Caltrans agreement provisions, and state and federal regulations. In addition, the City is responsible for the adequacy of their financial management system. Considering the inherent limitations in any financial management system, misstatements due to error or fraud may occur and not be detected.

**METHODOLOGY**

We gained an understanding of the projects and program and identified relevant criteria by reviewing the executed project agreements, Caltrans guidelines, applicable state and federal regulations, and by interviewing the City's personnel.

We performed a risk assessment, including identifying and evaluating whether key internal controls relevant to our audit objectives were properly designed, implemented, and operating effectively. Key internal controls evaluated focused on invoices reimbursed from Caltrans, review and approval processes of expenditures, procurement processes, and reporting of project deliverables and outcomes. Our assessment included conducting interviews with key personnel, observing processes, analyzing relevant documentation, and testing transactions related to costs billed and reimbursed, and documentation to support project deliverables and project outcomes reports. Significant issues with internal controls were identified and are included in the Findings and Recommendations of this report.

In addition, we assessed the reliability of data obtained from the City's financial management system used to identify and track project costs. Our assessment included reviewing information process flows, testing transactions for completeness and accuracy, and determining if costs were supported by source documentation. We determined that the data was sufficiently reliable to meet our audit objectives, except for the City's labor billing practices.

We conducted this performance audit according to 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 findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions.

### **VIEWS OF RESPONSIBLE OFFICIALS**

Our findings and recommendations take into account the City's response dated November 4, 2020, to our October 19, 2020 draft report. Our findings and recommendations, the City's response, and our analysis of the response are set forth in the Findings and Recommendations section of this report. A copy of the City's full written response is included as Attachment B.

The report is a matter of public record and will be placed on IOAI's webpage, which can be viewed at <<https://ig.dot.ca.gov>>.

If you have questions, please contact MarSue Morrill, Audit Chief, at (916) 202-7626, or at [marsue.morrill@dot.ca.gov](mailto:marsue.morrill@dot.ca.gov).



## FINDINGS AND RECOMMENDATIONS

### CONCLUSION

The Independent Office of Audits and Investigations (IOAI) performed an incurred cost audit of five City of Santa Ana's, Public Works Agency (City), projects with costs totaling \$2,632,460, reimbursed from the California Department of Transportation (Caltrans), as of June 30, 2019.

We identified questioned labor and indirect costs totaling \$504,283 that were not in compliance with Caltrans agreement provisions, and state and federal regulations. We also identified deficiencies with the City's labor and indirect cost billing practices, procurement and contracting, construction management and project oversight, and project reporting and outcomes. See Attachment A for a summary of questioned costs.

### FINDING 1 – Unsupported Labor and Indirect Costs Claimed

The City could not support the labor and indirect costs billed to Caltrans for the five projects audited. Deficiencies identified are outlined below.

- The City included indirect costs in their labor billings but did not have an approved indirect cost rate. This was also noted as a finding in IOAI's Indirect Cost Rate Proposal audit report issued on October 5, 2018. During this audit we followed up on the status. The results include internal control weaknesses that could affect the City's ability to accurately develop, record, and bill labor costs. We issued a management letter, dated August 31, 2020, to Caltrans to communicate these results.
- The City billed labor costs using outdated billing rates, not actual costs. The billing rates were based on the 2013/14 actual costs when current actual costs were required.
- The City was unable to identify the billing components on the invoices the City submitted to Caltrans. The City did not break down costs into eligible direct and/or indirect cost components.
- The City inconsistently billed labor costs by using two different billing methods, hourly billing rates (which included indirect costs) and actual hourly rates (which did not include indirect costs). Invoices did not distinguish between employees using hourly billing rates or actual hourly rates.

Because of the deficiencies noted above, the City is unable to support the claimed billing rates. As a result, the total claimed labor costs of \$504,283 are questioned.

The Caltrans Local Assistance Procedures Manual (LAPM) Chapter 5.3, Reimbursable Project Costs – Indirect Costs, states in part, “Should any department, division or other organization unit within the local agency seek reimbursement of their indirect costs, they must receive an Approval/Acceptance Letter of the local agency’s Indirect Cost Rate Proposal (ICRP)/Indirect Cost Allocation Plan (ICAP) for the fiscal year(s) involved from the Caltrans Division of Audits and Investigations (A&I) prior to billing for any indirect costs....”

Article IV, paragraph 7, of the Master Agreements No. 12-5063R and No. 12-5063F15 states, “Payments to administering agency can only be released by state as reimbursement of actual allowable project costs ...”

LAPM Chapter 5.3, Reimbursable Project Costs, states in part, “The costs of salaries, wages and related project costs may be reimbursable for the following activities. All costs must be broken down into eligible direct and/or indirect cost components.”

2 CFR § 200.34 (a) states, “The charges may be reported on a cash or accrual basis, as long as the methodology is disclosed and is consistently applied.”

The City does not have policies and procedures in place that address accurate and consistent labor billing practices. Without approved indirect cost rates and proper labor billing policies and procedures, the City will continue to bill Caltrans for ineligible labor and indirect costs.

## **RECOMMENDATIONS**

- A. Remit \$504,283 in questioned costs. Alternatively, work with Caltrans and the Federal Highway Administration to determine any allowable amounts that may be included in the \$504,283 questioned costs.
- B. Comply with the master agreements and the LAPM Chapter 5.3 and submit an ICRP for approval annually moving forward and prior to billing Caltrans for indirect costs.
- C. Develop and implement policies and procedures to address the roles and responsibilities over labor billing practices, and a consistent methodology in billing labor costs according to applicable state and federal regulations.
- D. Caltrans should also review billings on other projects to determine if indirect costs were reimbursed.

## **SUMMARY OF CITY'S RESPONSE**

The City acknowledged they are aware of organizational deficiencies and indicated they have undergone a reorganization. The City also indicated they are currently working with a consultant and are nearing the final stages of submitting Indirect Cost Rate Proposals (ICRPs) for Caltrans acceptance and approval for a series of fiscal years.

The City requested an opportunity to work with Caltrans and the Federal Highway Administration to reconcile and identify allowable costs that may be among the \$504,283 in costs reported as questioned. The City requested detailed backup and calculations of the total questioned costs.

## **ANALYSIS OF CITY'S RESPONSE**

The City will need to work with Caltrans and the Federal Highway Administration on any corrective action. We have provided the details and backup requested that support the amount questioned. We appreciate the City's acknowledgment and steps taken to address the issues identified. Any processes, and policies and procedures implemented subsequent to our fieldwork have not been audited or reviewed.

## **FINDING 2 – Procurement Deficiencies**

The City did not consistently follow state and federal requirements when procuring consultant and construction contracts. We tested the procurements of one consultant architectural and engineering (A&E) firm and two construction contractors. Deficiencies identified are outlined below.

### **Task Order Process Deficiencies**

The City used a rotational basis procedure to award task orders to qualified A&E firms, which is not considered a competitive process under federal regulations. Specifically, the City entered into contracts with the top three ranked firms.

The City did not perform an additional qualification-based selection process when awarding task orders among the firms awarded contract. Instead, the top ranked firm was automatically assigned the first task order. Once a firm was assigned a task order, that firm was moved to the bottom of the list. The second top ranked firm was then assigned the second task order, and the rotation continued.

In addition, we noted other deficiencies in the task order process:

- The City did not specify in the contracts the procedure the City would use to award/execute task orders among the three firms.
- The City lacked panel members' evaluation and ranking records such as the scoring sheets, for the original award of the three consulting firm contracts.

23 CFR § 172.9 (a)(3)(iv) states in part, "If multiple consultants are to be selected and multiple on-call or IDIQ contracts awarded through a single solicitation for specific services...(B) Specify the procedures the contracting agency will use in competing and awarding task or work orders among the selected, qualified consultants...Under competitive negotiation procurement, each specific task or work order shall be awarded to the selected, qualified consultants: (1) Through an additional qualifications-based selection procedure, which may include, but does not require, a formal RFP in accordance with § 172.5 (a)(1)(ii)...."

23 CFR § 172.7 (a)(1)(iv)(F) states in part, "The contracting agency must retain supporting documentation of the solicitation, proposal, evaluation, and selection of the consultant...."

### **Required Procurement Procedures Not Completed**

Our review of procurement files found that the City's procurement practices omitted several procedures as outlined in Table 1 below.

Table 1 – Procurement Deficiencies

Deficiencies	Name	Criteria
Did not submit the Caltrans Exhibit 10-T, Panel Member Conflict of Interest & Confidentiality Statement	AESCO, Inc. <sup>4</sup>	LAPM Chapter 10.5, Consultant Selection Using the One-Step RFP Method
Did not prepare the independent estimates	AESCO, Inc.	23 CFR §172.7(a)(1)(v)(B)
No record of negotiations, including a separate profit negotiation	AESCO, Inc.	23 CFR §172.7(a)(1)(v)(A) & (E)
Did not establish elements of contract cost (often called a price/cost analysis)	AESCO, Inc.	23 CFR §172.7(a)(1)(v)(C) & (E)
No record (verification) showing the consultant/contractor was not debarred/suspended	AESCO, Inc., All American Asphalt <sup>5</sup> , California Professional Engineering <sup>2</sup>	23 CFR §172.7(b)(3), 23 CFR §635.110(e), Public Contract Code §6109(b)
No debarment and suspension certification	California Professional Engineering	23 CFR §635.112(g)

4 A&E consultant

5 Construction contractors

According to the City, different procedures followed by different departments within the Public Works Agency led to discrepancies in the enforcement of federal requirements for projects. Without following proper procurement procedures, the City risks not procuring contracts at a fair and reasonable price. The City stated they recently combined the Design and Construction Departments to ensure compliance with all state and federal requirements going forward.

The City does not have policies and procedures in place that address all the required state and federal requirements. By not properly assigning task orders, the City cannot ensure fair and open competition or that selection is based on demonstrated competence and qualifications. The

City stated they are actively changing the policy to ensure all consultants are selected based on a qualifications-based process for contracts and task orders.

### **RECOMMENDATIONS**

- A. Consistently apply state and federal requirements when procuring contracts.
- B. Update and implement procurement policies and procedures to conform with state and federal requirements, including the issuance of task orders, and train employees on the updated requirements.
- C. Have managers and staff involved with procurement take Caltrans Division of Local Assistance's consultant procurement training.

### **CITY'S RESPONSE**

The Capital Delivery Task Order processes have been revised, eliminating the rotational selection procedure. Staff has since maintained a competitive process in compliance with federal regulations in which all short-listed firms are considered for all task orders. All Task Orders issued by the Capital Delivery Team for grant-funded projects adhere to Chapter 10 of the Local Assistance Procedure Manual (LAPM) Chapter 10 for Consultant Selection. References to this manual are included in the Division's RFP instructions document. Additionally, staff has participated in Caltrans A&E Training regarding Consultant Selection and has been restructured accordingly.

### **ANALYSIS OF CITY'S RESPONSE**

We appreciate the City's acknowledgment and steps taken to address the issues identified. Any processes, and policies and procedures implemented subsequent to our fieldwork have not been audited or reviewed.

### **FINDING 3 - Contract Management Deficiencies**

Based on our review of one consultant A&E contract and two construction contracts, we noted several missing required contract provisions. The missing contract provisions are outline in Table 2 below.

**Table 2 - Missing Required Contract Provisions**

Missing Provisions	Contract	Criteria
Cost principles	AESCO, Inc.	LAPM Exhibit 10-R, A&E Boilerplate Agreement Language
Retention of records/ audits	All American Asphalt, and California Professional Engineering	Caltrans/City Agreements No. 12-5063F15 and No. 12-00289S, Article V, Paragraph 3
Audit review procedures	AESCO, Inc.	LAPM Exhibit 10-R
Subcontracting	AESCO, Inc., All American Asphalt, and California Professional Engineering	LAPM Exhibit 10-R, Caltrans/City Agreements No. 12-5063R, No. 12-5063F15, and No. 12-00289S, Article V, Paragraph 7
Equipment purchases	AESCO, Inc.	LAPM Exhibit 10-R
Rebates, kickbacks, other unlawful consideration	AESCO, Inc.	LAPM Exhibit 10-R
Debarment and suspension certification	AESCO, Inc.	LAPM Exhibit 10-R
Termination	All American Asphalt, and California Professional Engineering	Greenbook <sup>4</sup> Chapters 6-7 and 6-8

4 Standard Specifications for Public Works Construction

In addition, the City failed to submit the LAPM Exhibit 10-C, Consultant Contract Reviewers Checklist as required by LAPM Chapter 10.6.

According to the City, they currently have no policies and procedure to reference to the LAPM Chapter 10 for necessary contract provisions for state and federal funded procurements. Also, the City stated that they did not think AESCO, Inc. was an A&E firm. Requirement of a professional engineer does constitute an A&E contract, which requires the submission of a completed Exhibit 10-C.

Without adequate contract provisions, the City risks not being able to enforce contract requirements and risks billing Caltrans for costs that are not allowable for reimbursement.

### RECOMMENDATIONS

- A. Update and implement policies and procedures to include all required contract provisions in state and federal funded projects and train employees on the updates.
- B. Complete the required Exhibit 10-C for all A&E consultant contracts.

### CITY'S RESPONSE

As part of the reorganization to combine the separate engineering groups into the Capital Delivery Team, all project and construction management policies and procedures are being reviewed, improved, and standardized. The updated procedures will incorporate all contract provisions, as identified in the audit.

### FINDING 4 – Invoices for Reimbursement Not Submitted Timely

The City did not submit eleven out of twenty-one invoices for reimbursement on four of the five projects audited within a minimum of every six months, as summarized in Table 3 below.

**Table 3 – Invoices for Reimbursement Not Submitted Timely**

Project Name	Billing Number	Months Late
Safe Routes to School Enhancement for King Elementary	2	8 months
First Street Class II Bikeway	3	9 months
First Street Class II Bikeway	4	8 months
Pedestrian Countdown Heads and Push Buttons	2	6 months
Pedestrian Countdown Heads and Push Buttons	3	7 months
Pedestrian Countdown Heads and Push Buttons	4	8 months
Pedestrian Countdown Heads and Push Buttons	5	9 months
Traffic Signal Modifications: Intersections of Edinger Ave. & Sullivan St., 17th & English Streets, MacArthur Blvd. & Plaza Dr., and Westminster Ave. & Clinton St.	2	6 months
Traffic Signal Modifications: Intersections of Edinger Ave. & Sullivan St., 17th & English Streets, MacArthur Blvd. & Plaza Dr., and Westminster Ave. & Clinton St.	3	7 months
Traffic Signal Modifications: Intersections of Edinger Ave. & Sullivan St., 17th & English Streets, MacArthur Blvd. & Plaza Dr., and Westminster Ave. & Clinton St.	4	14 months
Traffic Signal Modifications: Intersections of Edinger Ave. & Sullivan St., 17th & English Streets, MacArthur Blvd. & Plaza Dr., and Westminster Ave. & Clinton St.	6	8 months



Article IV, paragraph 4, of the State Master Agreement No. 00289S, Federal Master Agreements No. 12-5063R and No. 12-5063F15, and the LAPM Chapter 5.5, Invoice Guidelines, Format, and Checklist – General Guidelines, require the administering agency to submit invoices for reimbursement at least once every six months to maintain an active project status.

The City stated the design or construction phase may have been waiting for the E-76 (Authorization to Proceed) approval from the Federal Highway Administration, therefore, delayed the submission of invoices. By not billing every six months, the project could potentially be placed on the inactive list and be suspended, or it may lose project funding. Late invoices for reimbursement could also impact the timeliness of Caltrans' oversight and increase the risk that unallowable or unreasonable costs billed are not detected.

### **RECOMMENDATION**

Require billings to Caltrans be submitted at least once every six months per project.

### **SUMMARY OF CITY'S RESPONSE**

As previously noted, recent reorganization efforts consolidated the project grant reimbursement billings under the Agency's Administrative Services Division. This will

serve to centralize the functions required for timely billing submissions. All project costs will be more easily identifiable and reconciled since only one group, the Capital Delivery Team, will be involved in project delivery.

### **ANALYSIS OF CITY'S RESPONSE**

We appreciate the City's acknowledgment and steps taken to address the issues identified. Any processes, and policies and procedures implemented subsequent to our fieldwork have not been audited or reviewed.

### **FINDING 5 – Deficiencies in Project Deliverables and Outcomes**

We found deficiencies in the City's Active Transportation Program (ATP) project, ATPL-5063 (160), deliverables (reporting and milestones) and outcomes as outlined in Table 4 below.

Table 4 – Project Deliverables and Outcome Deficiencies

**Deliverables and Outcomes****Project Milestones and Goals**

Final Delivery Report Submitted Timely?	Construction Acceptance	Due Date	Submission Date
No	5/31/2017	5/31/2018	12/19/2018

Met Project Outcomes	Before Count	Projected Count	After Count
No	2,081	2,280	1,155

Met Scheduled Project Milestones?	Yes/No	Proposed Completion Date	Actual Completion Date	Days Behind
Design (PS&E)	No	9/30/2015	2/16/2016	139
Construction Award	No	5/31/2015	10/18/2016	506
Construction Acceptance	No	5/31/2017	10/5/2017	127

**Project Deliverable Deficiencies**

The Local Assistance Program Guidelines (LAPG), Chapter 22.17, Project Reporting states in part, “Within a year of the project becoming operable<sup>4</sup>, the implementing agency must provide a final delivery report to their DLAE....”

The City stated a lack of oversight led to the late submittal of the final delivery report. Failure to meet the project schedules, billings, and reporting requirements may not allow Caltrans to ensure projects are executed in a timely manner and within scope and budget.

**Project Outcomes Deficiencies**

The City used different methodologies to determine the before (beginning) and after (ending) user counts of pedestrian and bicyclists for the ATP project audited. Specifically, the beginning user counts occurred at a period of high usage during the spring months; while the ending user

<sup>4</sup> A project becomes operable when the construction contract is accepted.

counts occurred at a period of low usage during the fall months, which could result in a misleading sense of success.

The City stated they did not have any guidelines on how to estimate user counts. Without a consistent methodology to compare beginning and ending user counts, Caltrans may not be able to assess the effectiveness of projects as intended.

### **RECOMMENDATIONS**

- A. Comply with the reporting guidelines outlined in the LAPG.
- B. Implement the Caltrans Interim ATP Count Methodology Guidance issued September 16, 2019, for future ATP project scoping and planning purposes.

### **CITY'S RESPONSE**

The City indicated they had interim CTC and/or Caltrans actions and approvals to changes in the milestones schedule. The City also indicated that prior to the development of the ATP Traffic Count Methodology Guidance issued

September 16, 2019, there was no set standard criteria issued by the CTC or Caltrans on how to take traffic counts for ATP projects.

### **ANALYSIS OF CITY'S RESPONSE**

The City did not provide any interim CTC and/or Caltrans approvals for the changes to the project's milestone schedules. Regarding the lack of ATP Traffic Count Methodology Guidance, outside industry guidelines were available. For example, the National Bicycle and Pedestrian.

We appreciate the City's acknowledgment and steps taken to address the issues identified. Any processes, and policies and procedures implemented subsequent to our fieldwork have not been audited or reviewed.

**ATTACHMENT A – Questioned Labor and Indirect Costs**

<b>Finding</b>	<b>Project Number</b>	<b>Amount</b>
1	ATPL-5063 (160) / No. 16-6871	\$56,938
1	BTA 1213-12-ORA-04 / No. 14-6814	\$43,369
1	HSIPL-5063 (154) / No. 15-6830	\$168,707
1	HSIPL-5063 (156) / No. 15-6834	\$199,276
1	STPL-5063 (176) / No. 17-6881	\$35,993
-	Total Questioned Costs:	\$504,283

**ATTACHMENT B - The City of Santa Ana's Response to  
the Draft Report**