



## City and County of San Francisco

Department of Public Works  
Indirect Cost Rate Proposal  
Fiscal Year 2017-18

Report No. 19-2660-075  
March 2020

### **Team Members**

Cheryl L. McCormick, CPA, Chief  
Rebecca G. McAllister, CPA, Assistant Chief  
Humberto E. Cervantes, CPA, Manager  
Jeremy Cameron Jackson, CPA, Supervisor  
Jonathan Cox, Lead  
Jeremy Bunting  
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

---



DEPARTMENT OF  
**FINANCE**

**GAVIN NEWSOM - GOVERNOR**  
915 L STREET ■ SACRAMENTO CA ■ 95814-3706 ■ WWW.DOF.CA.GOV

Transmitted via e-mail

March 20, 2020

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

**Final Report—City and County of San Francisco, Department of Public Works Indirect Cost Rate Proposal Audit**

The California Department of Finance, Office of State Audits and Evaluations, has completed its audit of the City and County of San Francisco Department of Public Works' (City) Indirect Cost Rate Proposal, for fiscal year 2017-18, Caltrans Audit Number P1594-0096.

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

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

Sincerely,

Original signed by Becky McAllister for:

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

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

# BACKGROUND, SCOPE, AND METHODOLOGY

---

## BACKGROUND

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

The City and County of San Francisco Department of Public Works (City) provides services ranging from cleaning, repairing, and maintaining city streets and sewers, to greening urban landscape and designing and managing construction of public facilities.<sup>2</sup>

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

The City submits an ICRP for eight bureaus in Public Works: Building Design and Construction (BDC); Building Repair (BBR); Infrastructure Design and Construction (IDC); Street and Environmental Services (SES); Street and Sewer Repair (SSR); Street-Use and Mapping (BSM); Urban Forestry (BUF); and General Administration (GA).

The City calculates the ICRP rate for each bureau by adding the individual bureau indirect cost rate with a Department Overhead indirect cost rate. The individual bureau rates consist of costs from its programs while the Department Overhead rate consists of costs allocated to each bureau from the Director's Office, Deputy Director Buildings, Deputy Director Infrastructure, Deputy Director Operations, and the Office for Financial Management and Administration. A separate ICRP rate is calculated for each bureau, except for BDC and IDC which are combined into a single shared ICRP rate.<sup>3</sup>

---

<sup>1</sup> Excerpts obtained from Caltrans, Division of Local Assistance website:  
<http://www.dot.ca.gov/localassistance/index.html>

<sup>2</sup> Excerpts obtained from the City's website: <https://sfgov.org/mod/department-public-works>

<sup>3</sup> Excerpts obtained from the City's 2017-18 ICRP dated July 1, 2017.

## **SCOPE**

At the request of IOAI, the California Department of Finance, Office of State Audits and Evaluations, audited the City's ICRP for fiscal year 2017-18.

The audit objectives were to:

1. Determine if the 2017-18 ICRP is in compliance with 2 CFR 200 and the LAPM.
2. Recalculate the 2017-18 ICRP rates if unallowable costs are identified.

The scope of the audit is limited to three bureaus that billed Caltrans for indirect costs: BDC, IDC, and BSM. Accordingly, we did not audit the ICRP rates for BBR, SES, SSR, BUF, and GA.

The City uses fixed indirect cost rates based on estimated costs with a carry-forward adjustment to account for the difference between estimated and actual costs from a prior period. Specifically, the 2017-18 ICRP rates were calculated based on estimated costs with adjustments from the 2015-16 carry-forward year. Because the 2017-18 costs were estimates and not actual costs from a prior period, specific 2017-18 costs/transactions were not tested. Rather, specific costs/transactions were selected from the actual costs included in the 2015-16 carry-forward.

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

## **METHODOLOGY**

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

We conducted a risk assessment, including evaluating whether key internal controls relevant to our audit objectives were properly designed, implemented, and operating effectively. Key controls evaluated focused on the separation of indirect and direct costs including labor, and preparation of the ICRP. Our assessment included observing processes and testing transactions related to accounts payable, time keeping/payroll, billing, and ICRP preparation for effectiveness of existing documented processes and procedures. Deficiencies in internal controls that were identified during our audit and determined to be significant within the context of our audit objectives are included in this report.

Additionally, we assessed the reliability of data from the City's financial management system, Financial Accounting and Management Information System (FAMIS), and the system used to generate reports from FAMIS, Electronic Information System (EIS). Further, we assessed the reliability of labor data from MyTime and Project Management Database (PMDB), the City's electronic time reporting system and the system used to

generate labor reports for our audit. Our assessments included reviewing information process flows, testing transactions for completeness and accuracy, and tracing report data to accounting records, employee timesheets, payroll records, and vendor invoices. We determined the following data was sufficiently reliable to address the audit objectives: accounting reports from FAMIS and EIS to support costs included in the 2017-18 ICRP, electronic timesheets from MyTime, and a labor report from PMDB to support labor hours and index codes, respectively. While we ultimately received a PMDB labor report we could rely on, the City generated six different versions of the report to provide sufficiently reliable data. With the first five reports, we identified errors rendering the data unreliable, such as incomplete employee populations and salary costs that did not agree to the accounting records in FAMIS.

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.

**Table of Methodologies**

Audit Objective	Methods
<p><b>Objective 1:</b> Determine whether the 2017-18 ICRP is in compliance with 2 CFR 200 and the LAPM.</p>	<ul style="list-style-type: none"> <li>• Selected 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 benefits, and the indirect costs pool.               <ul style="list-style-type: none"> <li>○ Selected items for direct and indirect salaries and wages, and fringe benefits were based on quantitative factors such as total costs billed to Caltrans, and qualitative factors such as the type (i.e., description) of costs.</li> <li>○ Selected items for indirect costs pool costs were based on quantitative factors, such as costs with a potential to impact the ICRP rate by 1 percent or greater, and qualitative factors such as the timing and type (i.e., description) of costs.</li> <li>○ Determined if direct and indirect salaries and wages, and fringe benefits were supported, segregated, and allocated, by interviewing staff and reviewing duty statements, tracing amounts to accounting and payroll records, recalculating Paid Time Off (PTO) rates, and reviewing the methodology used to determine the amount of indirect PTO costs.</li> <li>○ Determined if indirect costs pool costs were allowable, authorized, supported, segregated, and equitably allocated, by interviewing staff, reviewing invoices, contracts, allocation spreadsheets, cleared checks, general ledgers, and journal postings.</li> </ul> </li> <li>• Determined the carry-forward calculations were supported by:               <ul style="list-style-type: none"> <li>○ Verifying the 2015-16 rates were supported by the approved 2015-16 ICRP submission.</li> <li>○ Verifying the 2015-16 actual costs were supported by accounting records and reconciled to audited financial data.</li> </ul> </li> </ul>

	<ul style="list-style-type: none"> <li>○ Recalculating the 2015-16 recovered indirect costs, carry-forward, and the 2017-18 adjusted indirect costs.</li> <li>● Verified the indirect costs recovered by the City were billed appropriately by reviewing invoices to ensure the City used the IOAI approved ICRP rates, tracing direct labor costs to accounting records, and recalculating the indirect cost billed to Caltrans.</li> </ul>
<p><b>Objective 2:</b> Recalculate the 2017-18 ICRP rates if unallowable costs are identified.</p>	<ul style="list-style-type: none"> <li>● Recalculated the ICRP rates by removing unallowable costs from the indirect costs pool, adjusting the indirect cost bases, recalculating carry-forward adjustments, and removing the inequitable allocation of the Department Overhead rates.</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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

**CONCLUSION**

Based on procedures performed and evidence gathered, we determined the City's 2017-18 ICRP is not in compliance with 2 CFR 200 and the LAPM as described in Findings 1 and 2. Additionally, we identified weaknesses in the City's fiscal controls related to the preparation of the ICRP, as described in Finding 3. We recommend the City reconcile its 2017-18 indirect cost billings using the audited ICRP rates identified in Table 3 below and reimburse Caltrans for any overpayments.

The accepted and audited Bureau rates, Department Overhead rates, and ICRP rates are illustrated in Tables 1, 2, and 3.

**Table 1 – Summary of Accepted and Audited ICRP Bureau Rates for 2017-18<sup>4</sup>**

Bureau	Accepted Bureau Rate (a)	Audited Bureau Rate (b)	Bureau Rate Difference (a) – (b)
BDC*	64.04%	58.07%	(5.97%)
IDC*	64.04%	58.07%	(5.97%)
BSM	31.13%	28.81%	(2.32%)

\* The City combines costs for BDC and IDC to calculate a common indirect cost rate.

**Table 2 – Summary of Accepted and Audited ICRP Department Overhead Rates for 2017-18<sup>4</sup>**

Bureau	Accepted Department Overhead Rate (c)	Audited Department Overhead Rate (d)	Department Overhead Rate Difference (c) – (d)
BDC*	58.48%	0%	(58.48%)
IDC*	58.48%	0%	(58.48%)
BSM	45.86%	0%	(45.86%)

\* The City combines costs for BDC and IDC to calculate a common indirect cost rate.

**Table 3 – Summary of Accepted and Audited ICRP Rates for 2017-18<sup>4</sup>**

Bureau	Total Accepted Rate (e) = (a) + (c)	Total Audited Rate (f) = (b) + (d)	Total Rate Difference (e) – (f)
BDC*	122.52%	58.07%	(64.45%)
IDC*	122.52%	58.07%	(64.45%)
BSM	76.99%	28.81%	(48.18%)

\* The City combines costs for BDC and IDC to calculate a common indirect cost rate.

<sup>4</sup> The ICRP Rate is the sum of the Bureau Rate and Department Overhead Rate. The ICRP rates submitted by the City were accepted by IOAI on April 20, 2018.

See Appendices A and B for the Summary of Accepted and Audited Costs and Rates for the 2017-18 ICRP for detailed information.

## **FINDINGS AND RECOMMENDATIONS**

### **Finding 1: Inequitable Allocation of Department Overhead Costs**

The City does not appropriately reconcile Department Overhead costs and includes bureau costs in the Department Overhead cost pool, resulting in an inequitable allocation of Department Overhead costs to the bureaus and inaccurate ICRP rates for each bureau.

- The City does not appropriately reconcile budgeted to actual Department Overhead rates. To calculate the Department Overhead rates, the City allocates estimated Department Overhead costs—consisting of costs from the Director's Office, Office of Financial Management and Administration, and the deputy director offices—to each bureau based on the ratio of permanent positions in the bureau to total permanent positions across all bureaus. The City then divides each bureau's allocated Department Overhead costs by the bureau's indirect cost base (direct salaries and wages) to determine a Department Overhead rate for each bureau.

Although the City allocates budgeted Department Overhead costs to each bureau, it does not calculate the carry-forward adjustment for budget to actual Department Overhead cost for each bureau. Instead, the City performs the Department Overhead carry-forward adjustment in aggregate (i.e., the carry-forward adjustment is applied to the total Department Overhead costs) rather than calculating an adjustment for each bureau. The City's carry-forward calculation is inequitable and does not appropriately reconcile Department Overhead costs allocated to each individual bureau.

- Costs that can be specifically identified to a specific bureau were included in the Department Overhead indirect cost pool and allocated to all bureaus. For example, in the 2015-16 ICRP, the City allocated approximately 9 percent of estimated Department Overhead costs to BUF. During testing of Department Overhead costs, we identified a total of \$4,572,163 of actual Workers' Compensation Claims (Claims) in the 2015-16 Department Overhead pool. Based on the 9 percent allocation, BUF was allocated \$411,495 (9% x \$4,572,163) of the Claims. Our testing identified the Claims were traceable to the responsible bureaus, and we calculated Claims totaling \$1,468,533 attributable to BUF for the period of July 2015 through September 2015. The City's carry-forward adjustment method did not reconcile and adjust the underestimated BUF claims. In this example, the other bureaus' ICRP rates, including BDC, IDC, and BSM, included over \$1 million (\$1,468,533 - \$411,495) of inappropriate costs that should have been allocated to the BUF ICRP rate.

The City's control deficiencies related to the preparation of the ICRP (as detailed in Finding 3) and lack of staff knowledge of 2 CFR 200 requirements, results in an inequitable allocation of Department Overhead costs to the bureaus and inaccurate ICRP rates for each bureau.

Appendix VII to 2 CFR 200, section C.3 (c) states actual conditions must be taken into account in selecting the base to be used in allocating expenses. When allocation can be made by assignment of a cost grouping to the function benefitted, the allocation must be made in that manner. When the expenses in a grouping are more general in nature, the allocation should be made through the use of a selected base which produces results that are equitable.

Appendix VII to 2 CFR 200, section B.5 states a fixed rate means an indirect cost rate which has the same characteristics as a predetermined rate, except that the difference between the estimated costs and the actual, allowable costs of the period covered by the rate is carried forward as an adjustment to the rate computation of a subsequent period.

**Recommendations:**

- A. Remove Department Overhead rates from the 2017-18 ICRP rates, and future ICRP rates, until an appropriate and equitable allocation and carry-forward adjustment methodology is developed. (See Appendices A and B for adjustments to the 2017-18 ICRP rates.)
- B. Develop a Department Overhead allocation and carry-forward adjustment methodology that is consistent and results in an appropriate and equitable allocation of Department Overhead indirect costs to each bureau. Additionally, ensure indirect costs attributable to a specific benefitting bureau are not included in the Department Overhead cost pool.
- C. Revise policies and procedures, train staff, and update future ICRPs using the new Department Overhead allocation and carry-forward methodology.
- D. Reconcile the 2017-18 billings using the audited ICRP rates in Table 3 and reimburse Caltrans for any overpayments.

**Finding 2: Unallowable Costs Included in 2015-16 Indirect Costs Pools**

The City included unallowable costs totaling \$2,445,621 in the BDC, IDC, BSM, and Department Overhead indirect costs pools as illustrated in Table 4 below. As a result, the accepted rates are overstated and should be reduced as illustrated in Table 3.

**Table 4 – Unallowable Indirect Costs Included in the Indirect Costs Pool.**

Bureau	Salaries and Wages	Fringe Benefits	Paid Time Off	Other	Total
BDC	\$ 0	\$ 0	\$ 1,627,993	\$ 4,692	\$ 1,632,685
IDC	0	0	596,293	0	596,293
<b>Sub Total</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 2,224,286</b>	<b>\$ 4,692</b>	<b>\$ 2,228,978</b>
BSM	121,001	53,242	32,209	0	206,452
Department Overhead	0	0	0	10,191	10,191
<b>Total</b>	<b>\$ 121,001</b>	<b>\$ 53,242</b>	<b>\$ 2,256,495</b>	<b>\$ 14,883</b>	<b>\$ 2,445,621</b>

Insufficient policies and procedures and staff knowledge of 2 CFR 200 requirements resulted in the following unallowable costs:

- Indirect costs totaling \$174,243, consisting of salaries and wages (\$121,001) and fringe benefits totaling (\$53,242) for two employees, were incorrectly included in the indirect costs pool of BSM as detailed in Table 5. Based on our review of organizational charts, duty statements, and interviews with employees, we determined these employees were performing activities specifically identifiable to BUF and should not have been included in the BSM indirect costs pool. 2 CFR 200.413 (a) states direct costs are 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.

**Table 5 – 2015-16 Unallowable BSM Indirect Labor Costs**

<b>BSM Employee</b>	<b>Salary</b>	<b>Fringe Benefits</b>	<b>Total Indirect Labor Costs</b>
Employee A	\$ 81,105	\$ 38,718	\$ 119,823
Employee B	39,896	14,524	54,420
<b>Total</b>	<b>\$ 121,001</b>	<b>\$ 53,242</b>	<b>\$ 174,243</b>

- PTO costs totaling \$2,256,495 were incorrectly included in the indirect costs pool for BDC, IDC, and BSM, as detailed in Table 6. The City does not use a consistent accounting basis for costing the leave, resulting in inequitable and unallowable PTO costs in the indirect costs pools.

**Table 6 – 2015-16 Unallowable Indirect PTO Costs**

<b>Bureau</b>	<b>Unallowable PTO Costs</b>
BDC	\$ 1,627,993
IDC	596,293
BSM	32,209
<b>Total</b>	<b>\$ 2,256,495</b>

The City bills direct PTO accrued costs. However, the City used a combination of cash and accrual basis accounting to determine the amount of indirect PTO resulting in the use of an inconsistent accounting basis. 2 CFR 200.431 (b) states the cost of fringe benefits in the form of regular compensation paid to employees during periods of authorized absences from the job, are allowable if the accounting basis (cash or accrual) selected for costing each type of leave is consistently followed by the entity.

- Permit fee costs totaling \$4,692 were incorrectly included in the BDC indirect costs pool. The costs are for Navigation Center Civic Center Hotel Permit Fees and are identifiable to a specific cost objective and should have been classified as direct costs. 2 CFR 200.413 (a) states direct costs are 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.

The City also included unallowable promotional items, such as lapel pins, cups, and shirts, totaling \$10,191 in the Department Overhead indirect cost pool. An adjustment is not made because all of Department Overhead rates were disallowed in Finding 1. 2 CFR 200.421 (e) (3) and (4) state unallowable advertising and public relations costs include costs of promotional items.

## Recommendations:

- A. Adjust the 2015-16 actual indirect costs pools by \$2,445,621 for the unallowable costs and ensure these costs are not included in future indirect costs pools. (See Appendices A and B for the specific adjustments for each bureau.)
- B. Review all indirect accounts to ensure costs are in compliance with 2 CFR 200; assigned to the correct bureau; and properly segregated between direct, indirect, and unallowable costs.
- C. Develop a methodology to ensure direct and indirect PTO costs are in compliance with 2 CFR 200 by using a consistent accounting basis (accrual or cash).
- D. Reconcile the 2017-18 billings using the audited rates in Table 3 and reimburse Caltrans for any overpayments.

## Finding 3: Strengthen Fiscal Controls for Preparation of the ICRP

The City should strengthen its controls related to the preparation, support, and review of the ICRP to ensure it is accurate, supported, and does not include unallowable indirect costs. The control deficiencies listed below significantly impact the reliability and accuracy of the City's ICRP rate calculations. Further, the control deficiencies contributed to the unallowable costs and non-compliance with 2 CFR 200 described in Findings 1 and 2 above.

- ICRP policies and procedures do not include adequate instructions necessary for the preparation and support of the ICRP. The City prepares its ICRP using a complex spreadsheet based on a 1978 financial model. The 31 tab spreadsheet contains numerous cross references and calculations with minimal instructions regarding the purpose or impact to the ICRP. The spreadsheet also contains approximately seven reports generated from the City's information systems and another seven pivot tables created from those reports. The data from the reports is used for the preparation of the ICRP. However, the City does not have adequate instructions on how to create the reports and pivot tables, such as the system and report parameters to use, or how the data from the reports should be used in the ICRP.
- The spreadsheet includes inconsistencies in rounding, and a combination of manually input and linked cells. Due to inconsistent rounding, there was a \$262 error in the carry-forward adjustment calculation for BDC and IDC.
- The City does not use a templated spreadsheet. Rather, each year the City updates a prior year's version of the workbook. Due to the size and complexity of the spreadsheet and inadequate instructions, as described above, using a prior year workbook increases the risk incorrect data is used to calculate the ICRP rates.
- The City's February 2018 ICRP policies and procedures refer to outdated criteria. Specifically, the policies and procedures refer to 2 CFR 225, which was superseded by 2 CFR 200 for fiscal years beginning after December 31, 2014.
- The City did not follow its established policies and procedures for its ICRP submission. Specifically, the City did not include adequate financial data to

support the 2015-16 indirect cost bases (direct salaries and wages) in its ICRP submission, as required by its policies and procedures and 2 CFR 200.

In its ICRP submission, the City provided a reconciliation for actual indirect costs to its 2015-16 Comprehensive Annual Financial Report (CAFR); however, it did not provide a reconciliation for the actual direct salaries and wages. Without a reconciliation to audited financial data for direct salaries and wages, the City could not support the accuracy or validity of the amounts used in the carry-forward calculations.

During our audit, the City created a reconciliation for the actual direct salaries and wages used in the carry-forward calculation to its 2015-16 CAFR. While the City was able to create a reconciliation, it was created during our audit and not included in the ICRP submission. Based on the reconciliation, the direct salaries and wages used in the ICRP carry-forward calculation required adjustments by the amounts displayed in Table 7 below to agree to audited financial data.

**Table 7 – 2015-16 Indirect Cost Bases**

<b>Bureau</b>	<b>ICRP - Direct Salaries and Wages</b>	<b>CAFR - Direct Salaries and Wages</b>	<b>Variance (Adjustments)</b>
BDC	\$ 12,878,870	\$ 12,775,506	\$ 103,364
IDC	\$ 18,668,057	\$ 18,833,063	\$ (165,006)
<b>Total</b>	<b>\$ 31,546,927</b>	<b>\$ 31,608,569</b>	<b>\$ 61,642</b>
BSM	\$ 7,135,751	\$ 7,042,273	\$ 93,478

Outdated and inadequate policies and procedures, inconsistent cell formatting, and use of a prior year workbook, increases the risk of inaccurate or unsupported ICRP rates. Additionally, providing inadequate financial data can lead to inaccurate ICRP rates and rejection of ICRP submissions by Caltrans.

2 CFR 200.62 states the City must maintain internal control processes to provide reasonable assurance transactions are properly accounted for, in order to demonstrate compliance with Federal requirements, and terms and conditions of awards from Caltrans.

Procedure 4 (c) from the City's ICRP Policies and Procedures (approved February 2018) states financial data (financial statements, comprehensive annual financial report, single audit reports, and management reports, if applicable) that support the rate shall be included with each ICRP proposal.

Appendix VII to 2 CFR 200, section D.2 (a) and (b) states ICRP submissions must include the rates proposed, including subsidiary worksheets and other relevant data, cross referenced and reconciled to the financial data (financial statements, comprehensive annual financial report, executive budgets, accounting reports, etc.) upon which the rates are based. Adjustments resulting from the use of unaudited data will be recognized, where appropriate, by Caltrans for indirect costs in a subsequent proposal.

**Recommendations:**

- A. Update the ICRP rate calculation model and supporting policies and procedures with appropriate criteria and detailed preparation steps to ensure the ICRP rates are accurate and in compliance with applicable criteria.
- B. Ensure established policies and procedures are followed, and future ICRP submissions include financial data that is clearly cross referenced and reconciled to support the ICRP rates.

**Summary of Accepted and Audited Costs and Rates  
Indirect Cost Rate Proposal  
City and County of San Francisco, Department of Public Works  
Bureau of Building Design and Construction (BDC)  
Bureau of Infrastructure Design and Construction (IDC)  
2017-2018**

<b>Table A.1 – 2015-16 Actual Costs (Carry-Forward Year)</b>						
<b>Description</b>	<b>BDC Accepted Amounts</b>	<b>IDC Accepted Amounts</b>	<b>BDC+IDC Combined Accepted Amounts</b>	<b>BDC+IDC Combined Audit Adjustments</b>	<b>BDC+IDC Combined Audited Amounts</b>	<b>Finding No.</b>
<b>Direct Costs</b>						
Direct Salaries and Wages*	\$ 12,878,870	\$ 18,668,057	\$ 31,546,927	\$ 61,642	\$ 31,608,569	3
<b>Indirect Costs Pool</b>						
Salaries and Wages	\$ 2,942,444	\$ 2,896,425	\$ 5,838,869	\$ 0	\$ 5,838,869	
Fringe Benefits	1,194,948	1,099,423	2,294,371	0	2,294,371	
Travel	5,240	2,726	7,966	0	7,966	
Training	64,977	76,895	141,872	0	141,872	
Employee Expenses	7,296	18,043	25,339	0	25,339	
Membership Fees	13,089	1,331	14,420	0	14,420	
Entertainment and Promotion	65	0	65	0	65	
Professional and Specialized Services	96,410	90,718	187,128	0	187,128	
Maintenance Services - Building and Structures	95,516	139,699	235,215	0	235,215	
Maintenance Services - Equipment	16,131	6,561	22,692	0	22,692	
Rents and Leases - Buildings and Structures	1,684	20,959	22,643	0	22,643	
Rents and Leases - Equipment	1,211	0	1,211	0	1,211	
Other Current Expenses	341,757	315,824	657,581	0	657,581	
Taxes; Licenses and Permits	28,079	78,490	106,569	(4,692)	101,877	2
Utilities	146	0	146	0	146	
Building and Construction Supplies	25,880	8,783	34,663	0	34,663	
Equipment Maintenance Supplies	19,953	8,406	28,359	0	28,359	
Hospital; Clinics and Laboratory Supplies	13,328	0	13,328	0	13,328	
Safety	19,718	29,661	49,379	0	49,379	
Food	2,191	4,124	6,315	0	6,315	
Other Materials and Supplies	486,226	346,373	832,599	0	832,599	
Services of Other Departments (AAO Funds)	2,244,181	2,697,341	4,941,522	0	4,941,522	
PTO	1,627,993	596,293	2,224,286	(2,224,286)	0	2
Depreciation	40,873	81,427	122,300	0	122,300	
<b>Total Indirect Costs Pool**</b>	<b>\$ 9,289,336</b>	<b>\$ 8,519,502</b>	<b>\$ 17,808,838</b>	<b>\$ (2,228,978)</b>	<b>\$ 15,579,860</b>	<b>2</b>

\*2015-16 Indirect Cost Base (Direct Salaries and Wages) is forwarded to Table A.2 – 2015-16 Calculated Indirect Cost Recoveries.

\*\*2015-16 Total Indirect Costs Pool is forwarded to Table A.3 – 2015-16 Carry-Forward Calculation.

# APPENDIX A (Continued)

**Summary of Accepted and Audited Costs and Rates  
Indirect Cost Rate Proposal  
City and County of San Francisco, Department of Public Works  
Bureau of Building Design and Construction (BDC)  
Bureau of Infrastructure Design and Construction (IDC)  
2017-2018 ~Continued~**

Table A.2 – 2015-16 Calculated Indirect Cost Recoveries				
Description	BDC + IDC Combined Accepted Amounts	BDC + IDC Combined Audit Adjustments	BDC + IDC Combined Audited Amounts	Finding No.
<b>(A) Indirect Costs Base (Direct Salaries and Wages) (from Table A.1)</b>	\$ 31,546,927	\$ 61,642	\$ 31,608,569	3
<b>(B) 2015-16 Bureau Indirect Cost Rate<sup>^</sup></b>	50.75%	50.75%	50.75%	
<b>(C) Calculated Indirect Cost Recoveries (A) x (B)<sup>***</sup></b>	\$ 16,009,804 <sup>⌘</sup>	\$ 31,545 <sup>⌘</sup>	\$ 16,041,349	3

<sup>^</sup>2015-16 Bureau Indirect Cost Rate was accepted by Caltrans' IOAI on February 29, 2016. The Bureau rate is the accepted ICRP rate (105.31%) less the Department Overhead rate (51.48%) and the Countywide Cost Allocation Plan (COWCAP) rate (3.08%). 2015-16 rates were not included in the scope of our audit.  
<sup>\*\*\*</sup>Calculated Indirect Cost Recoveries is forwarded to Table A.3 – 2015-16 Carry-Forward Calculation.  
<sup>⌘</sup> The accepted Calculated Indirect Cost Recoveries was understated by \$262 due to a calculation error by the City, see Finding 3. Therefore, the Audit Adjustment amount of \$31,545 is equal to (\$61,642\*50.75%) + \$262.

Table A.3 – 2015-16 Carry-Forward Calculation				
Description	BDC + IDC Combined Accepted Amounts	BDC + IDC Combined Audit Adjustments	BDC + IDC Combined Audited Amounts	Finding No.
<b>(F) 2015-16 Indirect Costs Pool (from Table A.1)</b>	\$ 17,808,838	\$ (2,228,978)	\$ 15,579,860	2
<b>(G) Calculated Indirect Cost Recoveries (from table A.2)</b>	16,009,804	31,545	16,041,349	3
<b>(H) 2013-14 Carry-Forward<sup>^</sup></b>	(849,319)	Not Applicable	(849,319)	
<b>(I) 2015-16 Carry-Forward (F) – (G) + (H)<sup>****</sup></b>	\$ 949,715	\$ (2,260,523)	\$ (1,310,808)	2,3

<sup>^</sup>2013-14 Carry-Forward was accepted by IOAI on February 29, 2016. 2013-14 Carry-Forwards were not included in the scope of our audit.  
<sup>\*\*\*\*</sup>2015-16 Carry-Forward is forwarded to Table A.4 – 2017-18 ICRP Indirect Cost Rate.

Table A.4 – 2017-18 ICRP Indirect Cost Rate				
Description	BDC + IDC Combined Accepted Amounts <sup>◆</sup>	BDC + IDC Combined Audit Adjustments	BDC + IDC Combined Audited Amounts	Finding No.
<b>(J) 2017-18 Budgeted Indirect Cost Pool<sup>■</sup></b>	\$ 23,323,349	\$ 0	\$ 23,323,349	
<b>(K) 2015-16 Carry-Forward (from Table A.3)</b>	949,715	(2,260,523)	(1,310,808)	2,3
<b>(L) Net 2017-18 Budgeted Indirect Cost Pool (J) + (K)</b>	\$ 24,273,064	\$ (2,260,523)	\$ 22,012,541	2,3
<b>(M) 2017-18 Budgeted Direct Salaries and Wages<sup>■</sup></b>	\$ 37,904,440	\$ 0	\$ 37,904,440	
<b>(N) 2017-18 Bureau Rate (L) / (M)</b>	64.04%	(5.97%)	58.07%	2,3
<b>(P) 2017-18 Department Overhead Rate</b>	58.48%	(58.48%)	0%	1
<b>(Q) 2017-18 ICRP Rate (N) + (P)</b>	122.52%	(64.45%)	58.07%	1,2,3

<sup>◆</sup> The ICRP costs and calculated rates submitted by the City were accepted by IOAI on April 20, 2018.  
<sup>■</sup> Because the 2017-18 costs are budget estimates, specific costs/transactions were not tested.

**Summary of Accepted and Audited Costs and Rates  
Indirect Cost Rate Proposal  
City and County of San Francisco Department of Public Works  
Bureau of Street Use and Mapping (BSM)  
2017-2018**

<b>Table B.1 – 2015-16 Actual Costs (Carry-Forward Year)</b>				
<b>Description</b>	<b>Accepted Amounts</b>	<b>Audit Adjustments</b>	<b>Audited Amounts</b>	<b>Finding No.</b>
<b>Direct Costs</b>				
Direct Salaries and Wages*	\$ 7,135,751	\$ (93,478)	\$ 7,042,273	3
<b>Indirect Costs Pool</b>				
Salaries and Wages	\$ 696,268	\$ (121,001)	\$ 575,267	2
Fringe Benefits	273,887	(53,242)	220,645	2
Training	4,598	0	4,598	
Employee Expenses	20	0	20	
Professional and Specialized Services	38,737	0	38,737	
Maintenance Services - Equipment	777	0	777	
Rents and Leases - Buildings and Structures	23,320	0	23,320	
Other Current Expenses	12,597	0	12,597	
Taxes; Licenses and Permits	115	0	115	
Building and Construction Supplies	7,861	0	7,861	
Equipment Maintenance Supplies	4,704	0	4,704	
Safety	7,611	0	7,611	
Food	286	0	286	
Water Sewage Treatment Supplies	655	0	655	
Other Materials and Supplies	35,121	0	35,121	
Services of Other Departments (AAO Funds)	1,311,950	0	1,311,950	
PTO	32,209	(32,209)	0	2
Depreciation	8,458	0	8,458	
<b>Total Indirect Costs Pool**</b>	<b>\$ 2,459,174</b>	<b>\$ (206,452)</b>	<b>\$ 2,252,722</b>	<b>2</b>

\*2015-16 Indirect Cost Base (Direct Salaries and Wages) is forwarded to Table B.2 – 2015-16 Calculated Indirect Cost Recoveries.  
\*\*2015-16 Total Indirect Costs Pool is forwarded to Table B.3 – 2015-16 Carry-Forward Calculation.

<b>Table B.2 – 2015-16 Calculated Indirect Cost Recoveries</b>				
<b>Description</b>	<b>Accepted Amounts</b>	<b>Audit Adjustments</b>	<b>Audited Amounts</b>	<b>Finding No.</b>
<b>(A) Indirect Costs Base (Direct Salaries and Wages) (from Table B.1)</b>	\$ 7,135,751	\$ (93,478)	\$ 7,042,273	3
<b>(B) 2015-16 Bureau Indirect Cost Rate<sup>^</sup></b>	38.03%	38.03%	38.03%	
<b>(C) Calculated Indirect Cost Recoveries (A) x (B)<sup>***</sup></b>	\$ 2,713,726	\$ (35,550)	\$ 2,678,176	3

<sup>^</sup>2015-16 Bureau Indirect Cost Rate was accepted by IOAI on February 29, 2016. The Bureau rate is the accepted ICRP rate (85.07%) less the Department Overhead rate (43.75%) and the COWCAP rate (3.29%). 2015-16 rates were not included in the scope of our audit.  
<sup>\*\*\*</sup>Calculated Indirect Cost Recoveries is forwarded to Table B.3 – 2015-16 Carry-Forward Calculation.

# APPENDIX B (Continued)

**Summary of Accepted and Audited Costs and Rates  
Indirect Cost Rate Proposal  
City and County of San Francisco Department of Public Works  
Bureau of Street Use and Mapping (BSM)  
2017-2018 ~Continued~**

<b>Table B.3 – 2015-16 Carry-Forward Calculation</b>				
Description	Accepted Amounts	Audit Adjustments	Audited Amounts	Finding No.
<b>(D) 2015-16 Indirect Costs Pool (from Table B.1)</b>	\$ 2,459,174	\$ (206,452)	\$ 2,252,722	2
<b>(E) Calculated Indirect Costs Recoveries (from Table B.2)</b>	2,713,726	(35,550)	2,678,176	3
<b>(F) 2013-14 Carry-Forward<sup>^</sup></b>	(408,229)	Not Applicable	(408,229)	
<b>(G) 2015-16 Carry-Forward (D) – (E) + (F)<sup>****</sup></b>	\$ (662,781)	\$ (170,902)	\$ (833,683)	2,3

<sup>^</sup>2013-14 Carry-Forward was accepted by IOAI on February 29, 2016. 2013-14 Carry-Forwards were not included in the scope of our audit.  
<sup>\*\*\*\*</sup>2015-16 Carry-Forward is forwarded to Table B.4 – 2017-18 ICRP Indirect Cost Rate.

<b>Table B.4 – 2017-18 ICRP Indirect Cost Rate</b>				
Description	Accepted Amounts <sup>◆</sup>	Audit Adjustments	Audited Amounts	Finding No.
<b>(H) 2017-18 Budgeted Indirect Costs Pool<sup>■</sup></b>	\$ 2,962,072	\$ 0	\$ 2,962,072	
<b>(I) 2015-16 Carry-Forward (from Table B.3)</b>	(662,781)	(170,902)	(833,683)	2,3
<b>(J) Net 2017-18 Budgeted Indirect Costs Pool (H + I)</b>	\$ 2,299,291	\$ (170,902)	\$ 2,128,389	2,3
<b>(K) 2017-18 Budgeted Direct Salaries and Wages<sup>■</sup></b>	\$ 7,386,872	\$ 0	\$ 7,386,872	
<b>(L) 2017-18 Bureau Rate (J) / (K)</b>	31.13%	(2.32%)	28.81%	2,3
<b>(M) 2017-18 Department Overhead Rate</b>	45.86%	(45.86%)	0%	1
<b>(N) 2017-18 ICRP Rate (L) + (M)</b>	76.99%	(48.18%)	28.81%	1,2,3

<sup>◆</sup> The ICRP costs and calculated rates submitted by the City were accepted by IOAI on April 20, 2018.  
<sup>■</sup> Because the 2017-18 costs are budget estimates, specific costs/transactions were not tested.





March 6, 2020

Cheryl L. McCormick, Chief  
Office of State Audits and Evaluations  
915 L St.  
Sacramento, CA 95814

London N. Breed  
Mayor

RE: Department of Public Works Indirect Cost Rate Proposal Audit

**Alaric Degrafinried**  
Acting Director

Dear Ms. McCormick:

San Francisco Public Works  
1 Dr. Carlton B. Goodlett Pl.  
Room 348  
San Francisco, CA 94102  
tel 415-554-6920

Thank you for the opportunity to review and respond to the audit report prepared by your office. San Francisco Public Works is committed to working with the State to ensure its indirect cost rates fully comply with all applicable regulations.

[sfpublicworks.org](http://sfpublicworks.org)  
[facebook.com/sfpublicworks](https://facebook.com/sfpublicworks)  
[twitter.com/sfpublicworks](https://twitter.com/sfpublicworks)

The audit report and in-depth conversations we had with the auditors who prepared it are essential contributions to our mission of delivering quality projects to the public on behalf of clients.

Attached is the Public Works' response to the Indirect Cost Rate Proposal Audit Report. If you have any questions, please feel free to call me at (425) 554-4831.

Sincerely,

Original signed by:

Julia Dawson  
Deputy Director for Financial Management and Administration

cc: Ms. MarSue Morrill, Chief, Planning and Modal Office, Independent Office of Audits and Investigations, California Department of Transportation  
Ms. Luisa Ruvalcaba, Audit Manager, Planning and Modal Office, Independent Office of Audits and Investigations, California Department of Transportation  
Mr. Bruce Robertson, Finance Manager, Department of Public Works, City and County of San Francisco  
Mr. Devin Macaulay, Budget Manager, Department of Public Works, City and County of San Francisco  
Ms. Jennifer Marquez, Accounting Manager, Department of Public Works, City and County of San Francisco

## INTRODUCTION

Public Works has reviewed the California Department of Finance, Office of State Audits and Evaluations (DOF) Draft Report. As a result, Public Works has incorporated necessary adjustments to the fiscal year 2017-18 accepted Indirect Cost Rate Proposal (ICRP) rates based on the DOF's findings and recommendations, Title 2 Code of Federal Regulations Part 200 (2 CFR 200) and California Department of Transportation (Caltrans) Local Assistance Procedures Manual Chapter 5 (LAPM). These recalculated rates and responses to all DOF findings and recommendations can be found below.

## SUMMARY

The accepted and audited bureau rates, department overhead rates, and ICRP rates, with Public Works adjustments are illustrated in Tables 1-3. These tables come from the DOF Draft Report, Public Works additions are highlighted in orange.

Table 1 below shows a Public Works recalculated bureau rate that is higher than the accepted bureau rate and audited bureau rate for the Bureau of Building Design & Construction (BDC), Bureau of Infrastructure Design & Construction (IDC) and Bureau of Street Use & Mapping (BSM). The primary reasons for these increases are necessary adjustments for Paid Time Off (PTO) recoveries and Workers' Compensation. Specifics of these adjustments are discussed in the response sections of this document.

**Table 1 – Summary of Accepted and Audited ICRP Bureau Rates for 2017-18**

<b>Bureau</b>	<b>Accepted Bureau Rate (a)</b>	<b>Audited Bureau Rate (b)</b>	<b>Bureau Rate Difference (a) – (b)</b>	<b>Public Works Recalculated Bureau Rate (g)</b>	<b>Public Works Recalculated Bureau Rate Difference (g) - (a)</b>
BDC	64.04%	58.07%	-5.97%	65.61%	1.57%
IDC	64.04%	58.07%	-5.97%	65.61%	1.57%
BSM	31.13%	28.81%	-2.32%	37.98%	6.85%

Table 2 shows a Public Works recalculated department rate that is lower than the accepted department overhead rate for BDC and IDC and higher for BSM. The primary reasons for these changes are necessary adjustments to Workers' Compensation and PTO and a change in methodology for allocation of Department General Administration (GEN) overhead costs. This change in allocation methodology has been accepted by Caltrans in the Public Works FY 2018-19 ICRP submittal. Public Works requests that recalculated rates and carry forward calculations be based on the methodology accepted by Caltrans rather than removing cost recovery for departmental overhead costs completely from the FY 2017-18 ICRP. Specifics of these adjustments are discussed in the response sections of this document.

**Table 2 – Summary of Accepted and Audited ICRP Department Overhead**

<b>Bureau</b>	<b>Accepted Department Overhead Rate (c)</b>	<b>Audited Department Overhead Rate (d)</b>	<b>Department Overhead Rate Difference (c) – (d)</b>	<b>Public Works Recalculated Department Rate (h)</b>	<b>Public Works Recalculated Department Rate Difference (h) - (c)</b>
BDC	58.48%	0%	-58.48%	52.70%	-5.78%
IDC	58.48%	0%	-58.48%	52.70%	-5.78%
BSM	45.86%	0%	-45.86%	49.72%	3.86%

Table 3 below shows a Total Public Works Recalculated Rate that is lower than the Accepted Department Overhead Rate for BDC, and IDC, and higher for BSM.

**Table 3 – Summary of Accepted and Audited ICRP Rates for 2017-18**

<b>Bureau</b>	<b>Total Accepted Rate (e) = (a) + (c)</b>	<b>Total Audited Rate (f) = (b) + (d)</b>	<b>Total Rate Difference (e) – (f)</b>	<b>Total Public Works Recalculated Rate (i) = (g) + (h)</b>	<b>Total Public Works Recalculated Rate Difference (i) - (e)</b>
BDC	122.52%	58.07%	-64.45%	118.31%	-4.21%
IDC	122.52%	58.07%	-64.45%	118.31%	-4.21%
BSM	76.99%	28.81%	-48.18%	87.70%	10.71%

See Appendices A, B, and C for the Summary of Accepted and Audited Costs and Rates with Public Works Adjustments for the FY 2017-18 ICRP for detailed information. Text goes here.

**RESPONSE TO FINDINGS AND RECOMMENDATIONS**

**Finding 1: Inequitable Allocation of Department Overhead Costs**

<b>Finding/Recommendation</b>	<b>Public Works Response</b>
<p>The City does not appropriately reconcile budgeted to actual Department Overhead rates. To calculate the Department Overhead rates, the City allocates estimated Department Overhead costs—consisting of costs from the Director’s Office, Office of Financial Management and Administration, and the deputy director offices—to each bureau based on the ratio of permanent positions in the bureau to total permanent positions across all bureaus. The City then divides each bureau’s allocated Department Overhead costs by the bureau’s indirect cost base (direct salaries and wages) to determine a Department Overhead rate for each bureau.</p> <p>Although the City allocates budgeted Department Overhead costs to each bureau, it does not calculate the carry-forward adjustment for budget to actual Department Overhead cost for each bureau. Instead, the City performs the Department Overhead carry-forward adjustment in aggregate (i.e., the carryforward adjustment is applied to the total Department Overhead costs) rather than calculating an adjustment for each bureau. The City’s carry-forward calculation is inequitable and does not appropriately reconcile Department Overhead costs allocated to each individual bureau.</p>	<p>Agree. The carryforward calculation methodology in the FY 2017-18 ICRP for Department Overhead is incorrect. To resolve this, Public Works has recalculated FY 2017-18 ICRP Department Overhead rates using a new methodology where GEN is rolled up to a single entity, making plan year and carryforward year consistent. This methodological change was reviewed and accepted by Caltrans as part of the FY 2018-19 Public Works ICRP submittal. This approach was also reviewed and validated by an external consultant to ensure consistency and compliance with 2 CFR 200. With this change, the plan year and carryforward year methodologies are now consistent.</p> <p>See Appendix C for details regarding the new methodology.</p>

Finding/Recommendation	Public Works Response
<p>Costs that can be specifically identified to a specific bureau were included in the Department Overhead indirect cost pool and allocated to all bureaus. For example, in the 2015-16 ICRP, the City allocated approximately 9 percent of estimated Department Overhead costs to BUF. During testing of Department Overhead costs, we identified a total of \$4,572,163 of actual Workers' Compensation Claims (Claims) in the 2015-16 Department Overhead pool. Based on the 9 percent allocation, BUF was allocated \$411,495 (9% x \$4,572,163) of the Claims. Our testing identified the Claims were traceable to the responsible bureaus, and we calculated Claims totaling \$1,468,533 attributable to BUF for the period of July 2015 through September 2015. The City's carry-forward adjustment method did not reconcile and adjust the underestimated BUF claims. In this example, the other bureaus' ICRP rates, including BDC, IDC, and BSM, included over \$1 million (\$1,468,533 - \$411,495) of inappropriate costs that should have been allocated to the BUF ICRP rate.</p>	<p>Agree. Public Works updated all relevant policies and procedures and desk manuals to reflect that actual expenditures and costs will be directly attributed to the appropriate bureau and will no longer include these costs entirely in the Department Overhead indirect cost pool.</p> <p>The recalculated rates in Tables 1-3 contain adjustments to correct Workers' Compensation, attributing costs to the bureaus that incurred them. See Appendix C Table C.2 for details.</p>
<p>A. Remove Department Overhead rates from the 2017-18 ICRP rates, and future ICRP rates, until an appropriate and equitable allocation and carry-forward adjustment methodology is developed. (See Appendices A and B for adjustments to the 2017-18 ICRP rates.)</p>	<p>Disagree. The Department Overhead indirect cost pool, except as noted in Findings 1 and 2 and addressed in Appendices A-C, contains valid, allowable costs. The issue, as noted in Finding 1, is the allocation of these costs.</p> <p>Tables 1 – 3 and Appendices A – C show revised calculations of rates based on the consistent allocation of GEN costs. The methodology used for these calculations was accepted and approved by Caltrans for the FY 2018-19 ICRP. Rather than completely removing FY 2017-18 Department Overhead rates, Public Works requests that the recalculated rates be reviewed and approved.</p>

Finding/Recommendation	Public Works Response
<p>B. Develop a Department Overhead allocation and carry-forward adjustment methodology that is consistent and results in an appropriate and equitable allocation of Department Overhead indirect costs to each bureau. Additionally, ensure indirect costs attributable to a specific benefitting bureau are not included in the Department Overhead cost pool.</p>	<p>Agree. Public Works has developed and implemented new carryforward methodology consistent with 2 CFR 200, see Appendix C. Accounting policies and procedures on billing review have been updated to ensure expenditures are recorded correctly and indirect costs attributable to specific benefitting bureaus are not included in the Department Overhead cost pool.</p>
<p>C. Revise policies and procedures, train staff, and update future ICRPs using the new Department Overhead allocation and carry-forward methodology.</p>	<p>Agree. Public Works updated all relevant policies and procedures and desk manuals and held training sessions with staff to ensure expenditures are recorded in a manner that complies with 2 CFR 200. A new ICRP framework was developed, reviewed, and accepted by Caltrans for the FY 2018-19 ICRP submittal. This approach was also reviewed and validated by an external consultant to ensure consistency and compliance with 2 CFR 200. The new framework addresses all audit findings and includes enhanced documentation.</p>
<p>D. Reconcile the 2017-18 billings using the audited ICRP rates in Table 3 and reimburse Caltrans for any overpayments.</p>	<p>Partially agree. Public Works does not agree with the recommendation to eliminate the Department Overhead rate but does agree with the premise that FY 2017-18 billings should be recalculated based on revised rates that reflect DOF audit adjustments and findings using the revised rates and any overpayment should be reimbursed, and any underpayment paid.</p> <p>See Tables 1-3 and Appendices A-C for recalculated rates.</p>

**Finding 2: Unallowable Costs Included in 2015-16 Indirect Costs Pools**

Finding/Recommendation	Public Works Response
<p>Indirect costs totaling \$174,243, consisting of salaries and wages (\$121,001) and fringe benefits totaling (\$53,242) for two employees, were incorrectly included in the indirect costs pool of BSM as detailed in Table 5. Based on our review of organizational charts, duty statements, and interviews with employees, we determined these employees were performing activities specifically identifiable to BUF and should not have been included in the BSM indirect costs pool. 2 CFR 200.413 (a) states direct costs are 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.</p>	<p>Agree. In FY 2015-16, the Public Works organizational structure included all permitting functions in BSM. In that year, the Bureau of Urban Forestry (BUF) was very small because all street tree maintenance was the responsibility of private owners. The positions identified were deployed to benefit both BSM and BUF permitting functions. We accept this adjustment as shown in Table 1, Table 3, and Appendix B Table B.3.</p>
<p>PTO costs totaling \$2,256,495 were incorrectly included in the indirect costs pool for BDC, IDC, and BSM, as detailed in Table 6. The City does not use a consistent accounting basis for costing the leave, resulting in inequitable and unallowable PTO costs in the indirect costs pools.</p> <p>The City bills direct PTO accrued costs. However, the City used a combination of cash and accrual basis accounting to determine the amount of indirect PTO resulting in the use of an inconsistent accounting basis. 2 CFR 200.431 (b) states the cost of fringe benefits in the form of regular compensation paid to employees during periods of authorized absences from the job, are allowable if the accounting basis (cash or accrual) selected for costing each type of leave is consistently followed by the entity.</p>	<p>Partially agree. Public Works did use an inconsistent accounting basis for the FY 2017-18 ICRP. It should be noted that Public Works’ FY 2017-18 ICRP carryforward methodology may not be allowed by 2 CFR 200, but it is <u>not</u> inequitable. Total PTO charges and recoveries are ultimately the same with mixed accounting carryforwards as they would be without them. Only the timing is different.</p> <p>To correct this issue, both PTO expenditures <u>and</u> recoveries for PTO must be excluded from the carryforward calculation. This changes the basis to pure accrual. DOF only excluded PTO expenditures in its recalculation of rates analysis.</p> <p>FY 2017-18 PTO accruals have been correctly charged to Caltrans.</p> <p>For corrected rates and calculations see Tables 1-3, and Appendices A-B.</p> <p>This issue has been resolved in the accepted FY 2018-19 ICRP by eliminating the PTO carryforward.</p>

Finding/Recommendation	Public Works Response
<p>Permit fee costs totaling \$4,692 were incorrectly included in the BDC indirect costs pool. The costs are for Navigation Center Civic Center Hotel Permit Fees and are identifiable to a specific cost objective and should have been classified as direct costs. 2 CFR 200.413 (a) states direct costs are 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.</p>	<p>Agree. The ICRP framework has been updated with new procedures for identifying and excluding 2 CFR 200 unallowable costs from indirect cost pools.</p>
<p>The City also included unallowable promotional items, such as lapel pins, cups, and shirts, totaling \$10,191 in the Department Overhead indirect cost pool. An adjustment is not made because all of Department Overhead rates were disallowed in Finding 1. 2 CFR 200.421 (e) (3) and (4) state unallowable advertising and public relations costs include costs of promotional items.</p>	<p>Agree. Public Works trained accounting staff on procedures to ensure costs are applied properly and correctly segregated between direct, indirect, and unallowable costs. The ICRP framework has been updated with new procedures for identifying and excluding 2 CFR 200 unallowable costs.</p>
<p>A. Adjust the 2015-16 actual indirect costs pools by \$2,445,621 for the unallowable costs and ensure these costs are not included in future indirect costs pools. (See Appendices A and B for the specific adjustments for each bureau.)</p>	<p>Disagree. See response to related Finding 1 above and see Appendices A-C for the specific recalculated adjustments for each bureau.</p>
<p>B. Review all indirect accounts to ensure costs are in compliance with 2 CFR 200; assigned to the correct bureau; and properly segregated between direct, indirect, and unallowable costs.</p>	<p>Agree. Public Works hired an external consultant to review methodology and ensure all costs are applied consistently and in full compliance with 2 CFR 200 and costs are properly segregated between direct, indirect, and unallowable costs.</p> <p>The ICRP framework has been updated with new procedures for identifying and excluding 2 CFR 200 unallowable costs.</p>
<p>C. Develop a methodology to ensure direct and indirect PTO costs are in compliance with 2 CFR 200 by using a consistent accounting basis (accrual or cash).</p>	<p>Agree. This issue has been resolved in the accepted FY 2018-19 ICRP by eliminating the PTO carryforward, ensuring the accounting basis is only accrual.</p>
<p>D. Reconcile the 2017-18 billings using the audited rates in Table 3 and reimburse Caltrans for any overpayments.</p>	<p>Partially agree. FY 2017-18 billings should be recalculated based on revised rates that reflect DOF audit adjustments and findings. Any overpayment should be reimbursed, and any underpayment paid.</p>

	<p>As noted above, the PTO portion of Department and Bureau Overhead rates is correct and was billed correctly.</p> <p>See Table 3 recalculated department and bureau rates.</p>
--	--

**Finding 3: Strengthen Fiscal Controls for Preparation of the ICRP**

<b>Finding/Recommendation</b>	<b>Public Works Response</b>
<p>ICRP policies and procedures do not include adequate instructions necessary for the preparation and support of the ICRP. The City prepares its ICRP using a complex spreadsheet based on a 1978 financial model. The 31 tab spreadsheet contains numerous cross references and calculations with minimal instructions regarding the purpose or impact to the ICRP. The spreadsheet also contains approximately seven reports generated from the City’s information systems and another seven pivot tables created from those reports. The data from the reports is used for the preparation of the ICRP. However, the City does not have adequate instructions on how to create the reports and pivot tables, such as the system and report parameters to use, or how the data from the reports should be used in the ICRP.</p>	<p>A new ICRP framework has been developed for FY 2018-19. The new framework addresses all audit findings and includes enhanced documentation.</p>
<p>The spreadsheet includes inconsistencies in rounding, and a combination of manually input and linked cells. Due to inconsistent rounding, there was a \$262 error in the carry-forward adjustment calculation for BDC and IDC.</p>	<p>Agree. Public Works validated the spreadsheet for development of the ICRP and ensured that all formula errors have been eliminated in the new FY 2018-19 ICRP framework. Public Works hired an external consultant to review the spreadsheet model to validate no formula errors remain.</p>
<p>The City does not use a templated spreadsheet. Rather, each year the City updates a prior year’s version of the workbook. Due to the size and complexity of the spreadsheet and inadequate instructions, as described above, using a prior year workbook increases the risk incorrect data is used to calculate the ICRP rates.</p>	<p>Agree. A new ICRP framework has been developed for FY 2018-19. Public Works hired an external consultant to assist in the development of a templated spreadsheet that will address all audit findings and ensure compliance with 2 CFR 200. The consultant reviewed the spreadsheet model to validate no formula errors remain.</p>

Finding/Recommendation	Public Works Response
<p>The City's February 2018 ICRP policies and procedures refer to outdated criteria. Specifically, the policies and procedures refer to 2 CFR 225, which was superseded by 2 CFR 200 for fiscal years beginning after December 31, 2014.</p>	<p>Agree. A new ICRP framework has been developed for FY 2018-19. The updated policies and procedures address 2 CFR 200 policies and procedures. The policies and procedures are under review by the external consultant hired by Public Works to ensure compliance.</p>
<p>The City did not follow its established policies and procedures for its ICRP submission. Specifically, the City did not include adequate financial data to support the 2015-16 indirect cost bases (direct salaries and wages) in its ICRP submission, as required by its policies and procedures and 2 CFR 200. In its ICRP submission, the City provided a reconciliation for actual indirect costs to its 2015-16 Comprehensive Annual Financial Report (CAFR); however, it did not provide a reconciliation for the actual direct salaries and wages. Without a reconciliation to audited financial data for direct salaries and wages, the City could not support the accuracy or validity of the amounts used in the carryforward calculations.</p> <p>During our audit, the City created a reconciliation for the actual direct salaries and wages used in the carry-forward calculation to its 2015-16 CAFR. While the City was able to create a reconciliation, it was created during our audit and not included in the ICRP submission. Based on the reconciliation, the direct salaries and wages used in the ICRP carry-forward calculation required adjustments by the amounts displayed in Table 7 below to agree to audited financial data.</p>	<p>Partially Agree. Public Works included adequate financial data to support the FY 2015-16 indirect cost bases in its ICRP submission. Public Works provided audited financial data from the City's audited financial system. The FY 2018-19 ICRP uses a new methodology that eliminates the need for including direct salaries and wages by relying on General Ledger actual expenditure recoveries. The CAFR reconciliation using the new methodology was reviewed and accepted by Caltrans.</p> <p>Public Works agrees with the \$61,642 adjustment to FY 2015-16 BDC/IDC direct salaries and \$93,478 adjustment to FY 2015-16 BSM direct salaries.</p>

<b>Finding/Recommendation</b>	<b>Public Works Response</b>
A. Update the ICRP rate calculation model and supporting policies and procedures with appropriate criteria and detailed preparation steps to ensure the ICRP rates are accurate and in compliance with applicable criteria.	Agree. Public Works updated all relevant policies and procedures and desk manuals. Actual expenditures and costs will be directly attributed to the appropriate bureau. Trainings were held with staff to ensure policies and procedures are followed.
B. Ensure established policies and procedures are followed, and future ICRP submissions include financial data that is clearly cross referenced and reconciled to support the ICRP rates.	Agree. Public Works updated all relevant policies and procedures and desk manuals. Actual expenditures and costs will be directly attributed to the appropriate bureau. Trainings were held with staff to ensure policies and procedures are followed.

The City's response to the draft audit report has been reviewed and incorporated into the final report. However, attachments referenced in the City's response have been omitted for brevity. We acknowledge the City's willingness to implement our recommendations and in evaluating the City's response, we provide the following comments:

**Finding 1: Inequitable Allocation of Department Overhead Costs**

**Finding 2: Unallowable Costs Included in 2015-16 Indirect Costs Pools**

The City agrees with the findings and recommendations except for the recommendations to remove Department Overhead rates and PTO costs from the 2017-18 ICRP rate calculations. The City disagrees with these recommendations because it provided recalculated 2017-18 rates to address the Department Overhead rates and PTO deficiencies identified in our report. The City's recalculated ICRP rates differ from the accepted and audited rates.

The 2017-18 ICRP submission certification, section II A. states the acceptance of rate(s) found to be materially incomplete or inaccurate would be subject to renegotiation at the discretion of Caltrans. Therefore, we did not audit the recalculated ICRP rates and the City should work with Caltrans regarding the acceptance of the recalculated rates. As a result, the findings and recommendations will remain unchanged.

**Finding 3: Strengthen Fiscal Controls for Preparation of the ICRP**

The City partially agrees with the finding and fully agrees with the recommendations. The City states it provided adequate financial data to support the 2015-16 indirect cost basis in its ICRP submission. The City did not provide any additional documentation in its response to support the 2015-16 indirect costs basis. Additionally, the City acknowledges using a new methodology that will mitigate this issue. As a result, the finding will remain unchanged.