



## City of Visalia

Department of Public Works  
Engineering Division and Transit Division  
Indirect Cost Rate Proposals  
Fiscal Years 2016-17 and 2017-18

### **Team Members**

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

You can contact our office at:

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

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November 19, 2019

Ms. MarSue Morrill, Chief, Planning and Modal Office  
Independent Office of Audits and Investigations  
California Department of Transportation  
1304 O Street, Suite 200  
Sacramento, CA 95814

Dear Ms. Morrill:

**Final Report—City of Visalia, 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 of Visalia Department of Public Works' (City) Indirect Cost Rate Proposals for fiscal years 2016-17 and 2017-18, Caltrans Audit Number P1594-0091 and P1594-0092.

The enclosed report is for your information and use. The City's response to the report finding is incorporated into this final report. The City agreed with our finding. We appreciate the City's assistance and cooperation during the engagement, and its willingness to implement corrective actions. 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:

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

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

# BACKGROUND, SCOPE, AND METHODOLOGY

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## BACKGROUND

The California Department of Transportation's (Caltrans) 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 of Visalia, Department of Public Works (City), is responsible for providing maintenance and repair of the City's infrastructure, keeping streets clean and well-maintained, providing solid waste and waste water utility services, and providing various City departments with a safe and reliable means of transportation.<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 submitted an ICRP for each of the following divisions: Transit, Streets, Engineering, and Airport.

## SCOPE

At the request of IOAI, the California Department of Finance, Office of State Audits and Evaluations, audited the City's ICRPs for fiscal years 2016-17 and 2017-18.

The audit objectives were to:

1. Determine if the 2016-17 and 2017-18 ICRPs were in compliance with 2 CFR 200 and the LAPM.
2. Recalculate the 2016-17 and 2017-18 ICRP rates if unallowable costs are identified.

The scope of the audit is limited to the divisions that billed Caltrans for indirect costs: Transit and Engineering. Accordingly, we did not audit the Streets and Airport divisions. The 2016-17 and 2017-18 ICRP rates include transactions related to actual costs incurred and billed to Caltrans in 2014-15 and 2015-16.

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

<sup>2</sup> Excerpts obtained from the City of Visalia website [https://www.visalia.city/depts/public\\_works/default.asp](https://www.visalia.city/depts/public_works/default.asp).

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 reviewing 2 CFR 200, the LAPM, and applicable City policies and procedures, and interviewing IOAI and City's personnel.

We conducted a risk assessment, including evaluating whether key internal controls relevant to our audit objectives such as reviews and approvals, knowledge of tasks, separation of duties, and separation of indirect and direct costs, were properly designed, implemented, and operating effectively. Our assessment included observing processes and testing transactions related to accounts payable, timekeeping/payroll, and billing for the 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, ONESolution, and its timekeeping system, Stromberg. Further, we assessed the reliability of the data in the spreadsheets used to calculate labor billing rates and reconcile expenditures from the ICRP to the City's financial statements. Our assessment included reviewing information process flows, testing transactions for completeness and accuracy, recalculating labor billing rates, and determining if costs were separately categorized by tracing to the accounting records, vendor invoices, purchase orders, and employee timesheets. We determined the data were sufficiently reliable to address the audit objectives.

Based on the results of our planning, we developed specific methods for gathering evidence to obtain reasonable assurance to address the audit objectives. Our methods are detailed in the Table of Methodologies on the following page.

## Table of Methodologies

Audit Objective	Methods
<p><b>Objective 1:</b> Determine whether the 2016-17 and 2017-18 ICRPs are in compliance with 2 CFR 200 and the LAPM.</p>	<ul style="list-style-type: none"> <li>• Selected significant and high-risk cost categories to verify compliance with 2 CFR 200 and the LAPM. Specifically, costs were selected from the direct salaries and wages, fringe benefits, and the indirect costs pool.               <ul style="list-style-type: none"> <li>○ Selection of direct salaries and wages and fringe benefits was 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 impact to 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 the direct salaries and wages and fringe benefits were supported, segregated, and allocated, by interviewing staff, tracing the amounts to accounting and payroll records, recalculating rates, and verifying fringe benefits were included in employee billable rates.</li> <li>○ Determined if indirect costs pool were allowable, authorized, supported, segregated, and equitably allocated, by interviewing staff, and reviewing invoices, contracts, credit card statements, purchase orders, cleared checks, citywide cost allocation plans, vendor websites, general ledgers, and journal postings.</li> <li>○ Verified the actual indirect costs recovered by the City were billed at the IOAI approved indirect cost rate by reviewing invoices, verifying support for direct labor hours and rates, and recalculating the indirect cost billed to Caltrans.</li> </ul> </li> </ul>
<p><b>Objective 2:</b> Recalculate the 2016-17 and 2017-18 ICRP rates if unallowable costs are identified.</p>	<ul style="list-style-type: none"> <li>• Determined identified unallowable costs do not result in a recalculation of the ICRP 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 that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

**CONCLUSION**

Based on the procedures performed and evidence gathered, we identified costs in the City’s 2016-17 and 2017-18 ICRPs that are not in compliance with 2 CFR 200 and the LAPM, as described in Finding 1. The unallowable costs do not significantly impact the City’s accepted ICRP rates; therefore, no change to the ICRP rates were calculated.

**Table 1 – Summary of Accepted and Audited ICRP Rates for 2016-17 and 2017-18<sup>3</sup>**

Fiscal Year	Division	Accepted Rate (a)	Audited Rate (b)	Rate Difference (a)–(b)
2016-17	Transit	73.97%	73.97%	0.00%
	Engineering	33.62%	33.62%	0.00%
2017-18	Transit	68.87%	68.87%	0.00%
	Engineering	29.31%	29.31%	0.00%

**FINDING AND RECOMMENDATIONS**

**Finding 1: Unallowable Costs Included in the Indirect Costs Pool**

The City included unallowable costs in the Transit division’s indirect costs pool. Costs related to food, awards, and an employee retirement party were included in the ICRP because the costs were coded to the incorrect sub-account. The City did not identify the errors because it did not perform a review of invoices to verify costs were correctly coded to the appropriate expense account. 2 CFR 200.438 and 200.445 (a) state these costs are unallowable as indirect costs. Although the unallowable costs were not significant to the 2016-17 and 2017-18 ICRP rates, inadequate reviews of invoice coding increases the risk of overstating ICRP rates and overbilling indirect costs in the future.

**Recommendations:**

- A. Develop and implement procedures to ensure invoices are reviewed for appropriate expense account codes.
- B. Review all indirect accounts to ensure costs are in compliance with 2 CFR 200 and properly segregated between allowable and unallowable costs.
- C. Remove unallowable costs from indirect costs prior to future ICRP submissions.

<sup>3</sup> The ICRPs rates submitted by the City were accepted by IOAI on February 27, 2017 and December 15, 2017.



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November 6, 2019

Cheryl L McCormick, Chief,  
Office of State Audits and Evaluations  
915 L Street  
Sacramento, CA 93291

Dear Ms. McCormick:

The City of Visalia is in receipt of your department's draft report for the audit of our Indirect Cost Rate Proposals for fiscal years 2016-17 and 2017-18. We have reviewed the draft report and are pleased that the items that were included in the finding were not significant and did not result in a recalculation of our indirect rates.

The City of Visalia understands that even with immaterial items there is always inherent risk and the following recommendations were made in the draft report to help mitigate that risk:

- A. Develop and implement procedures to ensure invoices are reviewed for appropriate expense account codes.
- B. Review all indirect accounts to ensure costs are in compliance with 2 CFR 200 and properly segregated between allowable and unallowable costs.
- C. Remove unallowable costs from indirect costs prior to future ICRP submissions.

To implement the recommendations above, the City of Visalia has educated our departments on how to code indirect costs to their appropriate accounts. Because there is a two level review before the item is expensed, it is important for the approver of these items ensure that the coding is correct. Even though the City of Visalia had already had objects created to segregate the allowable and unallowable costs, we understand that the cost may be placed in the wrong category. Making sure that the initial coding of the invoice or expense is correct will help the City of Visalia eliminate errors.

In conclusion, the City of Visalia would like to thank the audit team for their professionalism and their approach. We feel that they were knowledgeable and conveyed us a lot of advice that will be helpful in the future.

Original signed by,

Renee Nagel, Finance Director  
City of Visalia Finance Department