SCAG
INNOVATING FOR A BETTER TOMORROW

SOUTHERN CALIFORNIA
ASSOCIATION OF GOVERNMENTS
900 Wilshire Blvd., Ste. 1700
Los Angeles, CA 90017
T: (213) 236-1800
www.scag.ca.gov

MEETING OF THE

AUDIT COMMITTEE

Thursday, June 27, 2019
10:30 a.m. – 12:00 p.m.

SCAG Main Office
900 Wilshire Blvd., Ste. 1700
Policy Room A
Los Angeles, CA 90017
(213) 236-1800

See Next Page for Other Meeting Locations

If members of the public wish to review the attachments or have any questions on any of the agenda items, please contact Carmen Summers at (213) 236-1984 or via email at summers@scag.ca.gov. Agendas & Minutes for the Audit Committee are also available at: www.scag.ca.gov/committees

SCAG, in accordance with the Americans with Disabilities Act (ADA), will accommodate persons who require a modification of accommodation in order to participate in this meeting. SCAG is also committed to helping people with limited proficiency in the English language access the agency's essential public information and services. You can request such assistance by calling (213) 236-1908. We request at least 72 hours (three days) notice to provide reasonable accommodations and will make every effort to arrange for assistance as soon as possible.

This Page Intentionally Left Blank

REVISED*

List of Audit Committee Members Participating at SCAG Offices and Other Meeting Locations

Date: Thursday, June 27, 2019
Time: 10:30AM-12:00PM
Location: SCAG Main Office
900 Wilshire, Suite 1700 – Policy Room A
Los Angeles, CA 90017

TELECONFERENCE INSTRUCTIONS & INFORMATION PURSUANT TO GOVERNMENT CODE §54953.
For Brown Act compliance, please post a copy of the agenda at your teleconference location.

	LIST OF MEMBERS	MEETING LOCATIONS
1.	**Hon. Rex Richardson, Chair** *City of Long Beach, District 29*	SCAG Main Office 900 Wilshire, Suite 1700 Los Angeles, CA 90017
2.	**Hon. Randon Lane** *City of Murrieta, District 5*	~~SCAG Main Office~~ ~~900 Wilshire, Suite 1700~~ ~~Los Angeles, CA 90017~~ 730 M Street Fresno, CA 93721*
3.	**Hon. Alan Wapner** *City of Ontario, SBCTA*	Indianapolis Marriott Downtown 350 West Maryland Street Indianapolis, IN, 46225, USA
4.	**Hon. Sean Ashton** *City of Downey, District 25*	SCAG Main Office 900 Wilshire, Suite 1700 Los Angeles, CA 90017
5.	**Hon. Michael Carroll** *City of Irvine, District 14*	Irvine City Hall Council Conference Room 3 1 Civic Plaza Irvine, CA 92606
6.	**Hon. Margaret Clark** *City of Rosemead, District 32*	Rosemead City Hall 8838 E. Valley Blvd. Rosemead, CA 91770
7.	**Hon. Steve Manos** *City of Lake Elsinore, District 63*	Lake Elsinore City Hall City Council Office 130 S Main Street Lake Elsinore, CA 92530
8.	**Hon. Fred Minagar** *City of Laguna Niguel, District 12*	23272 Mill Creek Drive, Suite 240* Laguna Hills, CA 92653
9.	**Sup. Linda Parks** *Ventura County*	625 West Hillcrest Drive Thousand Oaks, CA 91360
10.	**Hon. Carmen Ramirez** *City of Oxnard, District 45*	Oxnard City Hall 300 W. Third Street, 4th Floor Oxnard, CA 93030

REVISED*

List of Audit Committee Members Participating at SCAG Offices and Other Meeting Locations
Date: Thursday, June 27, 2019
Time: 10:30AM-12:00PM
Location: SCAG Main Office
900 Wilshire, Suite 1700 – Policy Room A
Los Angeles, CA 90017

TELECONFERENCE INSTRUCTIONS & INFORMATION PURSUANT TO GOVERNMENT CODE §54953.
For Brown Act compliance, please post a copy of the agenda at your teleconference location.

11.	**Hon. Ali Saleh** *City of Bell, District 27*	Bell City Hall 6330 Pine Avenue Bell, CA 90201
12.	**Hon. Marty Simonoff** *City of Brea, District 22*	Indianapolis Marriott Downtown 350 West Maryland Street Indianapolis, IN, 46225, USA
13.	**Hon. Cheryl Viegas-Walker** *City of El Centro, District 1*	Walker & Driskill, PLC 3205 S. Dogwood Road, Suite B El Centro, CA 92243
14.	**Hon. Edward H.J. Wilson, CPA** *City of Signal Hill*	

AUDIT COMMITTEE AGENDA

Southern California Association of Governments

900 Wilshire Boulevard, Suite 1700
Los Angeles, California 90017
Thursday, June 27, 2019
10:30 AM

The Audit Committee may consider and act upon any of the items listed on the agenda regardless of whether they are listed as Information or Action Items.

CALL TO ORDER AND PLEDGE OF ALLEGIANCE
(The Honorable Rex Richardson, Chair)

ROLL CALL

PUBLIC COMMENT PERIOD
Members of the public desiring to speak on items on the agenda, or items not on the agenda, but within the purview of the Committee, must fill out and present a Public Comment Card to the committee staff prior to speaking. Comments will be limited to three (3) minutes per speaker. The Chair has the discretion to reduce the time limit based upon the number of speakers and may limit the total time for all public comments to twenty (20) minutes.

REVIEW AND PRIORITIZE AGENDA ITEMS

SELECTION OF VICE CHAIR

CONSENT CALENDAR	**Time**	**Page No.**
Approval Item		
1. Minutes of the March 21, 2019 Meeting		**1**
INFORMATION ITEMS		
2. Fiscal Year (FY) 2018-19 External Auditor Preliminary Update *(Joshua Margraf, Internal Auditor)*	**30 mins**	**5**
3. Caltrans Audits Corrective Action Plans *(Kome Ajise, Executive Director)*	**20 min**	**11**
4. Internal Audit Status Report *(Joshua Margraf, Internal Auditor)*	**10 min**	**112**

ACTION/DISCUSSION ITEMS

5.	Annual Audit Workplan *(Joshua Margraf, Internal Auditor)*	**10 mins**	**116**

RECOMMENDED ACTION: Approve internal audit work plan.

6.	Audit Standards *(Joshua Margraf, Internal Auditor)*	**15 mins**	**121**

RECOMMENDED ACTION: Approve adoption and use of Red Book standards for internal audit function.

STAFF REPORT
(Joshua Margraf, Internal Auditor)

- Audit Committee Meeting Schedule

FUTURE AGENDA ITEM/S

ANNOUNCEMENT/S

ADJOURNMENT

REPORT

Southern California Association of Governments
900 Wilshire Blvd., Suite 1700, Los Angeles, CA 90017
March 21, 2019

AUDIT (AC) COMMITTEE
MINUTES OF THE MEETING
THURSDAY, March 21, 2019

THE FOLLOWING MINUTES ARE A SUMMARY OF ACTIONS TAKEN BY THE AUDIT COMMITTEE. A DIGITAL RECORDING OF THE ACTUAL MEETING IS AVAILABLE FOR LISTENING IN SCAG'S OFFICE.

The Audit Committee met at SCAG, 900 Wilshire Blvd., 17th Floor, Los Angeles, CA 90017. The meeting was called to order By Chair, Randon Lane. A quorum was present.

Members Present:

Hon. Randon Lane, Chair	***Murrieta***	**District 5**
Hon. Alan D. Wapner	*Ontario*	SBCTA
Hon. Sean Ashton	*Downey*	District 25
Hon. Jim Hyatt	*Calimesa*	District 3
Hon. Steve Manos	*Lake Elsinore*	District 63
Hon. Ray Marquez	*Chino Hills*	District 10
Hon. Fred Minagar	*Laguna Niguel*	District 12
Sup. Linda Parks	*Ventura County*	
Hon. Ali Saleh	*Bell*	District 27
Hon. Marty Simonoff	*Brea*	District 22
Hon. Cheryl Viegas-Walker	*El Centro*	District 1

Members Not Present

Hon. Carmen Ramirez, Vice Chair	***Oxnard***	**District 45**
Hon. Bill Jahn	*Big Bear Lake*	District 11
Hon. Margaret Finlay	*Duarte*	District 35
Hon. Clint Lorimore	*Eastvale*	District 4

CALL TO ORDER AND PLEDGE OF ALLEGIANCE

Chair Lane called the meeting to order at 10:30 a.m. A roll call announcement was made and it was determined that a quorum was present. At 10:35 a.m., Chair Lane excused himself from the meeting and asked President Wapner to chair the meeting in his absence.

PUBLIC COMMENT PERIOD

There were no public comments.

REVIEW AND PRIORITIZE AGENDA ITEM

There was no reprioritization of the agenda.

CONSENT CALENDAR

Approval Item

1. Minutes of the January 8, 2019 Meeting

A MOTION was made (Ashton) and SECONDED (Simonoff) to approve the Consent Calendar. The motion was passed by the following roll call vote:

FOR: Wapner, Ashton, Hyatt, Manos, Marquez, Parks, Saleh, Simonoff and Viegas-Walker (9).
AGAINST: None (0).
ABSTAIN: None (0)

ACTION/DISCUSSION ITEM

2. Financial Auditors Contract Extension

Basil Panas, Chief Financial Officer (CFO), provided background information regarding the extension of SCAG's contract with Vavrinek, Trine, Day and Company, LLP (VTD), SCAG's financial auditors for the last two years. He asked the Committee to authorize the extension of SCAG's contract with its financial auditors by two years.

A MOTION was made (Ashton) and SECONDED (Simonoff) to approve Staff's recommendation. The motion was passed by the following roll call vote:

FOR: Wapner, Ashton, Hyatt, Manos, Marquez, Parks, Saleh, Simonoff and Viegas-Walker (9).
AGAINST: None (0).
ABSTAIN: None (0).

INFORMATION ITEMS

3. IT Governance – A Framework for Success

Julie Loats, Chief Information Officer (CIO), as a follow-up on the IT discussions at the January 2019 Audit Committee meeting, provided a brief presentation on IT Governance at SCAG. The presentation focused on the current state of SCAG's IT and progress towards implementing a collaborative governance framework to assist the agency in achieving its goals. Some presentation highlights included:

- A snapshot on the projects currently in progress
- Prioritization schedule
- Benefits of Shared IT Governance
- Best standards

SCAG staff responded to comments and questions expressed by the Committee members, including concerns on SCAG's IT effectiveness on Cyber Security. Ms. Loats reported that SCAG is in the process of hiring an Infrastructure and Operations manager to closely focus on Cyber Security needs in-house.

The Committee thanked Ms. Loats for a great presentation as well as her leadership.

4. Caltrans Indirect Cost Allocation Plan (ICAP) Audit Results

Darin Chidsey, Interim Executive Director, provided an update of the completed Incurred Cost Audit and the Indirect Cost Allocation Plan (ICAP) Audit Corrective Action Plans from Caltrans. He noted that SCAG's own corrective action plan will provide the steps and actions required for SCAG to take to address audit findings and recommendations. Mr. Chidsey reported that in the interim, until SCAG receives the official Correction Action Plans from Caltrans, SCAG staff will continue to make progress and improvements developing the policies and procedures required in the several areas specified in the audits' findings and recommendations.

Mr Chidsey stated that when the final documents from Caltrans are received, (ICAP and the Incurred Cost Audit) the results will be provided to the Committee.

5. Independent Cost Estimate for SCAG Request for Proposals

Joshua Margraf, Internal Auditor (IA), reported on a review of SCAG cost estimates. The review focused on comparing SCAG-developed estimates with winning proposal estimates fora random sample of active contracts from SCAG's Financial Management System. The report focused on significant differences between SCAG's cost estimates and the cost estimates of selected consultant proposals. Mr. Margraf noted that understanding why these differences occur can help improve SCAG's processes for developing cost estimates as well as be reflected in any updates to policies and procedures that are occurring.

Discussion ensued on several topics ranging from using IRS guidelines as a template for cost estimating, to how similar some vendor bids were to SCAG's actual project budgets.

Staff explained that SCAG's budgets are transparent and included in the Overall Work Program (OWP), which help the cost estimates in vendor bids and SCAG's project budgets to seem aligned. Mr. Margraf also indicated that staff could also be developing a cost estimate based on the amount of funds available rather than the type of work needed since there is a lack of guidance for staff on how to develop estimates.

6. Internal Audit Status Report

Joshua Margraf, Internal Auditor, provided a brief overview of the Internal Audit Status Report. He focused the report on the *Audit Standards* update and noted that at the last Audit Committee meeting in January 2019, discussion ensued on comparisons and definitions between Red and Yellow Book standards and which standards SCAG should adopt. Mr. Margraf noted that if the Committee needed more time to decide on which standard to use, a recommendation could be made at a later date.

Mr. Chidsey noted that it is important to have a clear standard of audit work to be performed, and how the comparisons of the Red and Yellow book can be effectively applied based on the composition of the audit

function and type of work the Internal Audit performs. Mr. Chidsey recommended that both he and Josh Margraf discuss in detail which standards would be a good fit for SCAG, and report those recommendations at the next Audit Committee meeting.

FUTURE AGENDA ITEM

ANNOUNCEMENTS

ADJOURNMENT

There being no further business, President Wapner adjourned the Audit Committee meeting at 11:28 a.m.

Respectfully submitted by:

Carmen Summers
Audit Committee Clerk

//

REPORT

Southern California Association of Governments
900 Wilshire Boulevard, Suite 1700, Los Angeles, California 90017
June 27, 2019

To: Audit Committee (AC)

EXECUTIVE DIRECTOR'S APPROVAL

Kome Ajise

From: Joshua Margraf, Internal Auditor, AC - Audit Committee, (213) 236-1890, margraf@scag.ca.gov

Subject: Fiscal Year (FY) 2018-19 External Auditor Preliminary Update

RECOMMENDED ACTION:
For Information Only – No Action Required

STRATEGIC PLAN:
This item supports the following Strategic Plan Goal 7: Secure funding to support agency priorities to effectively and efficiently deliver work products.

EXECUTIVE SUMMARY:
SCAG's external independent auditor will present the preliminary FY 2017-18 audit report.

BACKGROUND:
SCAG's external independent auditors, Vavrinek, Trine, Day, and Company, LLP (VTD), have started audit work on SCAG's FY 2018-19 financial statements. VTD plans to complete the audit and report the results to the committee in November or December of 2019. They will present their audit plan to the Audit Committee.

FISCAL IMPACT:
None

ATTACHMENT(S):
1. Audit Committee Presentation - SCAG 2019

Southern California Association of Governments

AUDIT COMMUNICATIONS

For Discussion Purposes

Audit Scope and Timing

Perform the audit of the:

- Comprehensive Annual Financial Report (CAFR)
- OMB Uniform Grant Guidance – Single Audit

Timeline:

- Planning and Interim Fieldwork – May
- Final Fieldwork – September/October
- Report Delivery – November/December

For Discussion Purposes

Our Responsibility

U.S. Generally Accepted Auditing Standards and *Government Auditing Standards*

Express opinions about whether the financial statements that have been prepared by management are presented fairly, in all material respects, in conformity with generally accepted accounting principles

- Reasonable, not absolute assurance
- Audit does not relieve the management of its responsibilities

For Single Audit, express an opinion on compliance applicable to major federal programs

For Discussion Purposes

Our Responsibility

Our audit will include obtaining an understanding of the entity and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing and extent of further audit procedures –

- Material misstatements may result from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or regulations that are attributable to the entity or to acts by management or employees acting on behalf of the entity
- No opinion on internal control will be expressed

For Discussion Purposes

Our Responsibility

Communicate other matters:

- Qualitative aspects of accounting policies, accounting estimates and note disclosures
- Difficulties encountered
- Uncorrected misstatements
- Material corrected misstatements
- Disagreements with management
- Management representations
- Consultations with other accountants

For Discussion Purposes

Management's Responsibilities

- Design, implement, establish, and maintain effective internal control over financial reporting, federal awards, and goals and objectives
- Prevent and detect fraud, and inform us of any known or suspected fraud
- Compliance with laws and regulations
- Ensure that management and financial information is reliable and properly reported
- Make all personnel, financial records, and related information available to us
- Prepare the financial statements
- Provide us a written representation letter

VALUE THE difference

For Discussion Purposes

Our Approach

Planning and Risk Assessment:

- Meet with Management
- Obtain an understanding of the entity, its environment and risks
- Identify audit risk areas
- Inspect financial and other information
- Consider/inquire regarding fraud risks
- Understand the design and implementation of internal control
- Prepare risk assessment and audit plan
- Test key business cycles – revenue, disbursements, payroll, investments, capital assets, financial reporting, IT and budget

For Discussion Purposes

Our Approach

Final:

- Address key audit areas
- Perform tests, on a sample basis, on account balances and classes of transactions
- Prepare draft CAFR
- Test journal entries
- Assess accounting principles used and significant estimates
- Confirm contingencies with legal counsel
- Consider subsequent events

Exit:

- Propose / discuss audit adjustments
- Present findings and recommendations
- Provide required communications to those charged with governance

VALUE THE difference

For Discussion Purposes

Questions

Contact information
Roger Alfaro, Partner
ralfaro@vtdcpa.com
909-466-4410

VALUE THE difference

AGENDA ITEM 3

REPORT

Southern California Association of Governments
900 Wilshire Boulevard, Suite 1700, Los Angeles, California 90017
June 27, 2019

To: Audit Committee (AC)

EXECUTIVE DIRECTOR'S APPROVAL

Kome Ajise

From: Kome Ajise, Executive Director, Executive Management, 213-236-1835, Ajise@scag.ca.gov

Subject: Caltrans Audits Corrective Action Plans

RECOMMENDED ACTION:
For Information Only - No Action Required

STRATEGIC PLAN:
This item supports the following Strategic Plan Goal 7: Secure funding to support agency priorities to effectively and efficiently deliver work products.

EXECUTIVE SUMMARY:
On May 7, 2019, SCAG received from Caltrans the final Corrective Action Plans to address the findings in the Incurred Cost Audit issued on September 21, 2018 and the Indirect Cost Allocation Plan Audit issued on January 9, 2019. SCAG's Executive Management met with representatives from Caltrans, FHWA and FTA in Sacramento on June 21, 2019 to discuss SCAG's approach for finalizing its responses to the Corrective Action Plans which are due to Caltrans August 1, 2019.

BACKGROUND:
On May 5, 2016 Caltrans informed SCAG that it would be audited with respect to certain incurred and indirect costs. The scope of the audit was to determine:

- Whether costs claimed by and reimbursed to SCAG between April 1, 2015 and June 30, 2015, are adequately supported and in accordance with respective Caltrans Agreement Provisions and state and federal regulations.
- Whether SCAG's FY2015/15 Indirect Cost Rate Proposal was prepared in accordance with Title 2 Code of Federal Regulations Part 200, Chapter 5 of the Caltrans Local Assistance Procedures Manual.

Caltrans issued the final Incurred Cost Audit report on September 21, 2018 and the final Indirect Cost Allocation Audit Report on January 9, 2019 (attached). The reports cited:

- Improper procurement practices
- Deficient charging practices
- Contract management deficiencies
- Labor and fringe benefit deficiencies
- Billing and reporting deficiencies
- Possible conflict of interest with the sponsorship program

Caltrans issued the final Corrective Action Plans for both audits on May 7, 2019 (also attached). The corrective steps are very similar to the recommendations found in the final audit reports therefore SCAG began the process of implementing the required steps in late 2018. The status is described in the two attached matrixes and summarized below:

- Incurred Cost Audit: 11 of 24 recommendations have been fully implemented and another 6 are between 70% and 95% implemented.
- Indirect Cost Allocation Plan Audit: 10 of 16 recommendations have been fully implemented and another 5 are between 70% and 95% implemented.

At a meeting in Sacramento on June 21, 2019, SCAG updated representatives from Caltrans, FTA and FHWA on the steps taken so far to implement the Corrective Action Plans and on the associated organizational changes made recently, specifically the creation of the position of Chief Strategy Officer and the Office of Project Management.

FISCAL IMPACT:
The final Corrective Action Plans issued by Caltrans seek $4,401,565 in reimbursement from SCAG as follows: $2,148,589 for disallowed costs in Incurred Cost Audit and $2,252,976 for disallowed costs in the Indirect Cost Allocation Plan Audit. The final amount of repayment is subject to ongoing negotiations. Staff will report regularly on progress in this area.

ATTACHMENT(S):
1. Caltrans Final Incurred Cost Audit Report (September 21, 2018)
2. Caltrans Final Indirect Cost Allocation Plan Audit Report (January 9, 2019)
3. Corrective Action Plan for Incurred Cost Audit (May 7, 2019)
4. Corrective Action Plan for Indirect Cost Allocation Plan Audit (May 7, 2019)
5. Status Matrix for Incurred Cost Audit Corrective Action Plan
6. Status Matrix for Indirect Cost Allocation Plan Audit for Corrective Action Plan

State of California
DEPARTMENT OF TRANSPORTATION

California State Transportation Agency

Memorandum

Making Conservation a California Way of Life.

To: COCO BRISENO
Deputy Director
Planning and Modal Programs

Date: September 21, 2018

File: P1580-0022

From: WILLIAM E. LEWIS
Assistant Director
Independent Office of Audits and Investigations

Subject: **INCURRED COST AUDIT – SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS**

We audited costs claimed by and reimbursed to the Southern California Association of Governments (SCAG) totaling $12,485,538 for work performed under Master Agreements 53-6049R and 74A0822 between Caltrans and SCAG. The audit was performed to determine whether the costs were supported and in compliance with agreement provisions and state and federal regulations. The final audit report, which includes SCAG's response, is attached.

Based on our audit, we determined that project costs totaling $7,015,036 were not supported and did not comply with respective agreement provisions and state and federal regulations. $2,510,015 of these costs are disallowed. In addition, we found deficiencies in labor charges, consultant procurements, contract management, and billing and reporting.

Please provide our office with a corrective action plan addressing the recommendations in the report, including estimated timelines, by December 21, 2018.

This report is a matter of public record and will be placed on Caltrans Independent Office of Audits and Investigations' website. If you have questions or need additional information, please contact MarSue Morrill, Chief, External Audits - Local Governments, at (916) 323-7105.

c: Hasan Ikhrata, Executive Director, Southern California Association of Governments
Darin Chidsey, Chief Operating Officer, Southern California Association of Governments
Debbie Dillon, Deputy Executive Director, Administration, Southern California Association of Governments
Basil Panas, Chief Financial Officer, Southern California Association of Governments
Rodney Whitfield, Director of Financial Services, Federal Highway Administration
Tashia Clemons, Director, Planning and Environment, Federal Highway Administration
Veneshia Smith, Financial Manager, Federal Highway Administration
John Bulinski, Director, District 7, Caltrans
Steve Novotny, District Local Assistance Engineer, District 7, Caltrans
Eraina Ortega, Inspector General, Independent Office of Audits and Investigations, Caltrans
MarSue Morrill, Chief, External Audits-Local Governments, Independent Office of Audits and Investigations, Caltrans
Chris Schmidt, Chief, Division of Transportation Planning, Caltrans
Erin Thompson, Chief, Regional Planning, Division of Transportation Planning, Caltrans
Rihui Zhang, Chief, Division of Local Assistance, Caltrans
Kamal Sah, Acting Chief, Office of Guidance and Oversight, Division of Local Assistance, Caltrans
Daniel Burke, Acting Audit Liaison, Division of Local Assistance, Caltrans
Nancy Kataoka, Acting Chief, Division of Accounting

Southern California Association of Governments Incurred Cost Audit

Caltrans

Final Audit Report

September 2018

PREPARED BY:

California Department of Transportation
Independent Office of Audits and Investigations – MS 2
Post Office Box 942874
Sacramento, California 94274-0001
www.dot.ca.gov/hq/audits

AUDIT TEAM

MarSue Morrill, Chief, External Audits-Local Governments
Teresa Greisen, Audit Manager
Carvin Seals Jr., Auditor in Charge
Vincent Miranda, Auditor
Yung Jo Ryoo, Auditor

P1580-0022

TABLE OF CONTENTS

SUMMARY, OBJECTIVES, SCOPE, METHODOLOGY, BACKGROUND, AND CONCLUSION

SUMMARY

The Independent Office of Audits and Investigations (IOAI), California Department of Transportation (Caltrans), audited reimbursed costs totaling $12,458,538 to the Southern California Association of Governments (SCAG) and found costs totaling $2,510,015 were not in compliance with Caltrans agreement provisions and state and federal regulations.

OBJECTIVES

The audit was performed to determine whether costs claimed by and reimbursed to SCAG were allowable, adequately supported, and in compliance with the Caltrans agreement provisions and state and federal regulations.

The audit included testing costs incurred on two agreements, Master Agreement 53-6049R relating to the Value Pricing Pilot Program (VPPP-6049(010)), and Federal Overall Work Program Agreement number 74A0822 with Caltrans. Our audit period covered April 1, 2014, through June 30, 2015. Our audit also included testing of three consultant contracts procured prior to April 1, 2014 with costs incurred through March 30, 2018. See Attachment I for the list of audited agreements.

SCOPE

The scope of the audit was limited to financial and compliance activities related to the above-referenced agreements. Our audit of SCAG's claimed costs included interviews of SCAG staff necessary for obtaining an understanding of SCAG's financial management system and review of SCAG's financial statements for fiscal years 2014 and 2015. The audit consisted of transaction testing of claimed costs to evaluate compliance with Title 2 of the Code of Federal Regulations (CFR), Part 200; 48 CFR Chapter 1 Part 31; 49 CFR Part 18; 23 CFR Part 172; California Public Contract Code; Caltrans' Local Assistance Procedures Manual; and requirements stipulated in the agreements. Field work was completed on April 30, 2018, and transactions occurring subsequent to this date were not tested and, accordingly, our conclusion does not pertain to costs or credits arising after this date.

SCAG is responsible for the costs incurred and billed to Caltrans; compliance with applicable agreement provisions and state and federal regulations; and the adequacy of their financial management system to accumulate and segregate reasonable, allowable costs that can be allocated to projects. Because of inherent limitations in any financial management system, misstatements due to error or fraud may occur and not be detected. Also, projections of any evaluation of the financial management system to future periods are subject to the risk that the financial management

system may become inadequate because of changes in conditions or that the degree of compliance with the policies and procedures may deteriorate.

METHODOLOGY

IOAI conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that IOAI 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. IOAI believes that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The audit was less in scope than an audit performed for the purpose of expressing an opinion on the financial statements of the SCAG. Therefore, IOAI did not audit and is not expressing an opinion on SCAG's financial statements.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records selected. An audit also includes assessing the accounting principles used and significant estimates made by SCAG, as well as evaluating the overall presentation of costs claimed.

BACKGROUND

Caltrans has a legal and fiduciary responsibility to ensure that all state and federal funds are expended in compliance with state and federal laws, regulations, and agreements. IOAI performs audits to ensure Caltrans is meeting its legal and fiduciary responsibilities and that state and federal funds are properly expended by local government agencies.

CONCLUSION

Based on our audit, of the total reimbursed costs of $12,458,538, we determined $5,443,502 were adequately supported and in compliance with agreement provisions, and state and federal regulations. Reimbursed costs totaling $7,015,036, however, were not supported and/or were not in compliance with respective agreement provisions and state and federal regulations. Of this amount $2,510,015 is disallowed. Specifically, we found deficiencies in labor charges, consultant procurements, contract management, billing and reporting, and agency-wide policies and procedures.

VIEWS OF RESPONSIBLE OFFICIALS

Our findings and recommendations considered SCAG's response dated August 10, 2018 to our July 24, 2018 draft report. Our findings and recommendations, SCAG's response, and our analysis of the response are set forth in the Findings and Recommendations section of this report. A copy of the SCAG's full written response is included as Attachment IV.

This report is a matter of public record and will be placed on the Caltrans webpage, which can be viewed at <www.dot.ca.gov/audits/INC.html>.

If you have any questions, please contact Teresa Greisen, Audit Manager at (916) 323-7910, or Carvin Seals Jr., Auditor, at (916) 323-7965.

MarSue Morrill

MARSUE MORRILL, CPA
Chief
External Audits – Local Government Agency
Independent Office of Audits and Investigations

September 21, 2018

FINDINGS AND RECOMMENDATIONS

FINDING 1 – Improper Procurement Practices

Southern California Association of Governments (SCAG) did not ensure that fair and open competition was performed or that proper procurement procedures were followed as required by state and federal regulations and the California Department of Transportation's (Caltrans) agreement provisions. Additionally, SCAG's Procurement Policy and Procedures Manual that was in effect during the period of the procurements tested did not fully comply with state and federal procurement regulations and Caltrans agreement provisions. Specifically, we found the following procurement deficiencies:

I. Consultant Procurement Deficiencies

AECOM Technical Services, Inc. and Parsons Brinckerhoff, Inc.

SCAG issued RFP 13-008 for the Value Pricing Pilot Project (VPPP) that resulted in two consultant contracts. The VPPP was federally funded and considered a "Project of Division Interest." SCAG executed two contracts from the RFP, one with AECOM Technical Services, Inc. (AECOM) and one with Parsons Brinckerhoff, Inc. (Parsons). SCAG used price as an evaluation factor in the selection of the consultants. We reviewed the related procurement documents for the two consultants and found the following:

- The scope of work of the RFP included two tasks and several sub-tasks that required professional engineering judgement, traffic engineering, environmental specialties, roadway design/infrastructure cost estimates, and system integration. The inclusion of tasks requiring specialized services and professional engineering judgement requires an Architectural & Engineering (A&E) firm to perform the work. Title 23 CFR Part 172, states, "price shall not be used as a factor in the evaluation, ranking and selection process" when procuring engineering services. SCAG's RFP included both non-A&E and A&E tasks which required management decisions be made to ensure compliance with state and federal regulations. SCAG should have separately procured the tasks requiring A&E services or treated the entire RFP as an A&E procurement.

- The RFP did not include the identification of the requirements for any discussions (interviews) that may be conducted with three or more of the most highly qualified consultants following submission and evaluation of proposals. SCAG performed interviews of the consultants and included interview evaluations in the selection process.

- Notifications (Notice of Intent to Award) of the final ranking of the three most highly qualified consultants were not issued to all corresponding consultants.

II. Procurement Policies and Procedures Manual Deficiencies

We reviewed SCAG's Procurement Policies and Procedures Manual and determined the following procedures were missing or misstated:

- Procedures for procuring Architectural and Engineering (A&E) consultants.
- Procedures for documenting the justification for non-competitive procurements, including preparation of a Public Interest Finding on the Division of Local Assistance (DLA) funded projects.
- Section 6.6.2 Formal Solicitation was unclear as it began with language related to an Invitation for Bids, however, the documented detailed procedures relate to a Request for Proposal process for non-A&E consultants.
- SCAG's threshold of $25,000 for waiving competition for non A&E General Fund consultant procurements was higher than the requirements of the California Public Contract Code (PCC) of $20,000.

SCAG staff stated they lacked training and guidance on proper procurement processes and applicable procurement regulations. Without proper procurement practices, and procurement policies and procedures, SCAG may not be able to support fair and open procurements at a reasonable price.

See Attachment I for a summary of audited agreements, and procurements tested with the associated costs.

See Attachment III finding 1 for detailed criteria.

RECOMMENDATION

We recommend SCAG:

- Revise the Procurement Policies and Procedures Manual to ensure it is current and complies with all applicable Caltrans requirements and state and federal procurement regulations. Include revising Section 6.6.2 to describe the different competitive procurement processes available and when each should be used in compliance with state and federal regulations.
- Ensure proper management decisions are made when preparing RFPs that include tasks or sub-tasks that require an A&E consultant to perform the work for compliance with state and federal procurement regulations.
- Ensure management and staff receive proper training in procurement procedures.
- Ensure staff that are involved in the consultant procurement process perform all required actions and comply with SCAG policies and procedures, Caltrans requirements, and state and federal procurement regulations.
- Ensure all documentation is maintained to support that proper procurement procedures are followed in accordance with state and federal regulations.
- Take Caltrans, Division of Local Assistance (DLA) A&E consultant procurement training either in person or online at http://www.dot.ca.gov/hq/LocalPrograms/training.html

In addition, we recommend Caltrans' Division of Transportation Planning (DOTP) and Division of Local Assistance (DLA) provide enhanced oversight over SCAG's future procurements.

SUMMARY OF AUDITEE'S RESPONSE

SCAG disagrees the scope of work for RFP 13-008 was for the procurement of A&E services and indicated that IOAI staff during the exit conference said written guidance regarding A&E projects could have been clearer. Additionally, SCAG referenced Section 9.2 of the Caltrans Consultant Procurement Manual (CPM) issued by the DLA dated April 2017 that states ITS projects that are the "development of a concept of operations" are non-A&E. This project was a concept of operations and therefore, SCAG asserts it was not an A&E project.

SCAG also disagrees that a Public Interest Finding (PIF) was required for System Metrics Group (SMG) and makes note, per discussions with District 7 and staff within HQ's (Caltrans) that the PIF form does not apply to non-construction contracts.

SCAG is in the process of updating their procurement policies and procedures and will be providing training to staff.

See Attachment IV for SCAG's full response.

ANALYSIS OF AUDITEE'S RESPONSE

Based on our review of SCAG's response and further discussions with FHWA and DLA staff, IOAI re-worded the finding related to the procurements of the consultants AECOM and Parson's to provide clarity. The RFP for the procurement included one task and several sub-tasks in each category that included activities that would require engineering judgement to perform the work. The Caltrans agreement, E76, and the cooperative agreement (between SCAG, Caltrans and FHWA) included numerous references to criteria and guidance that required SCAG's compliance to Chapter 13 of the Caltrans Local Assistance Program Guidelines and 23 CFR Part 940 that provided detailed information relating to ITS projects. SCAG was responsible for maintaining proper policies and procedures and ensuring compliance with state and federal regulations when implementing projects and seeking reimbursement of costs. This includes maintaining proper documentation to support decisions made. Additionally, SCAG's response includes the Federal Transit Administration's Best Practices Procurement & Lessons Manual (October 2016) as support for its position. The VPPP was a DLA funded project and therefore, the Federal Transit Administration's Best Practices are not applicable to the finding.

SCAG also asserts that eliminating price would not have altered the outcome. SCAG cannot ensure that using price as a factor would not or did not affect the outcome of the procurement. The evaluators' scoring decisions were made throughout the evaluation and full pricing information was included within the consultant proposals (not segregated and provided in a separate sealed document).

With regard to the finding related to the consultant SMG, SCAG contends the Caltrans guidance on single proposer/sole source procurements has not been clear and remains unclear today. We concur that there is no clear guidance regarding sole source procurements relating to the Division of Transportation Planning (DOTP) projects and have removed the finding from the report. We will request DOTP update their Planning Handbook and include guidance regarding sole source procurements funded with planning funds.

Based on our analysis of the response, the finding has been revised as noted above.

FINDING 2 – Contract Management Deficiencies

SCAG's contract management system did not comply with state and federal regulations and Caltrans agreement provisions. We found that SCAG billed Caltrans for unsupported and unallowable consultant costs. Furthermore, we found that SCAG improperly managed consultant contracts, did not properly close-out consultant contracts, executed amendments on expired contracts, and could not support all local match requirements were met. Additionally, SCAG lacked contract management policies and procedures detailing proper processes to manage consultant and sub-recipient contracts and detailed procedures for reviewing and approving invoices. SCAG billed and was reimbursed $590,537 in unsupported consultant costs, and $361,426 on an expired consultant contract. These costs are disallowed.

Specifically we found the following:

I. Consultant Invoice Deficiencies

We tested 23 consultant invoices (from ten consultants) and found that SCAG lacked documented support for consultant costs charged to projects/work elements, and they approved and paid consultant costs lacking adequate support.

- Ten of 23 consultant invoices were arbitrarily split and allocated to more than one project/work element with no source documentation to support the actual costs applicable to each project/work element. The unsupported consultant costs total $590,538 and are disallowed.
- Seven of 23 consultant progress reports submitted with the invoices did not include the percentage of work completed as required in the consultant contracts.
- One of 23 consultant invoices was approved without a required progress report.

SCAG's review and approval process of consultant and sub-recipient invoices was performed by project managers, section managers, accountants, contract administrators (for consultants) and budgets and grants staff (for sub-recipients). SCAG's review and approval process was not documented, and staff were unclear as to the roles and responsibilities of each area in the process. SCAG's accounting staff stated that based on the lack of detailed information included on the consultant invoices, there was no way to determine to which project(s) the consultant costs related. The practice of accepting and arbitrarily splitting consultant invoices that lack appropriate information detailing what tasks/activities the consultant performed increases the risk of unallowable costs being charged to Caltrans.

SCAG's Budgets and Grants Management Policies and Procedures were not clear and did not define the roles and responsibilities of project managers. Furthermore, SCAG did not have written policies and procedures for project managers and other staff reviewing and approving invoices of sub-recipients and consultants. SCAG staff acknowledged they had inadequate Project Management and Grant Management Policies and Procedures in place to provide staff guidance. SCAG stated that they are in the process of developing policies and procedures for staff that define staff roles and responsibilities and provide guidance to the project managers. The lack of policies and procedures and weak invoice approval processes increase the risk of unallowable costs being billed to Caltrans.

II. Consultant and Sub-recipient Contract Deficiencies

We tested three consultant contracts and found that SCAG billed costs incurred on an expired contract and did not perform and/or document required actions related to properly managing consultant contracts. We also tested three sub-recipient agreements and found all three lacked required language to comply with Caltrans agreement provisions. Specifically we found the following:

- SCAG executed an amendment on an expired contract for the consultant contract with Parsons and billed costs to Caltrans that were incurred after the contract expiration date. Additionally, work was amended into the contract for the LA County Express Lane Strategic Plan on behalf of another agency that was outside of the original scope of work. Parsons original contract of $1,859,803 was amended 12 times to add $195,500 to total $2,058,303. Amendment 5 was executed after the contract expiration date. Therefore, amendments 5 through 12 are invalid and subsequent costs billed to Caltrans totaling $361,426 are disallowed.
- The scope of work for the RFP and the AECOM consultant contract were not clearly defined as evidenced by the contract being amended 15 times. Nine amendments changed the scope of work and six amendments added additional funds. The original contract amount was $2,065,599. Amendments totaling $2,306,337 were added for a total contract amount of $4,371,936, an increase of 112 percent. In addition, the contract was executed even though the Terms and Conditions did not appear to be finalized. One proposed sub-consultant was deleted from task seven on the executed contract with no documented justification. Additionally, five amendments included changes to the scope, and additions of sub-consultants and dollars to task seven.
- The scope of work on the RFP for the SMG consultant procurement was not clearly defined as evidenced by the contract being amended 14 times. Three amendments added additional funds. The original contract amount was $1,839,422. Amendments totaling $622,900 were added for a total contract amount of $2,463,322, an increase of 34 percent.
- The project manager and contract administrator did not always perform an independent cost estimate, an analysis of the cost proposal, and cost negotiation when they amended the AECOM and SMG consultant contracts. In addition, not all cost estimates that were prepared for the AECOM, Parsons and SMG contracts were signed and dated to support they were prepared prior to cost negotiation and execution.
- SCAG extended the contract terms for the SMG consultant contract over 36 months without re-solicitation in violation of SCAG's Procurement Policies and Procedures.

- Three sub-recipient Memorandums of Understanding (MOU) agreements tested lacked required language below:
  - Project related travel and subsistence expense of contractors should be in accordance with California Department of Personnel Administration rates.
  - Sub-contractor and third party compliance for applicable cost principles should reference 48 CFR Ch. 1 Part 31.
  - Requirement to specify the type of contract as required by the Caltrans Local Assistance Procedures Manual (LAPM), Chapter 10.

The MOUs also included inaccurate regulations. The MOUs cited that sub-recipients were to comply with 48 CFR Chapter 1 Part 31 instead of 49 CFR Part 18.

III. **Consultant Contract Close-out Deficiencies**

SCAG's contract close-out process was not in compliance with Caltrans agreement provisions and state requirements on both consultant contracts tested. The project managers for these contracts did not perform a contact performance evaluation or a post evaluation of the consultants as required by DLA's Local Assistance Procedures Manual (LAPM) Chapter 10.8 and the PCC section 10369. Additionally, both contracts were closed out with no support to indicate all deliverables had been met or completed as required by the contract. Specifically, the first contract close-out lacked documentation of required summary memos for a workshop and whether five meetings and presentations were held or given. The second lacked documentation of five meetings held, two presentations, a summary report, a catalog of public comment, and a project completion plan.

The contract close-out procedures in SCAG's Procurement Policy and Procedures Manual were not developed in compliance with Caltrans LAPM and state regulations. One project manager was not aware of SCAG's contract close-out process and the departments involved. Lack of proper contract close-out processes impacts the ability of staff to understand and ensure compliance of the contracted work or services as specified in the contract.

IV. Local Match Deficiencies

During our testing of the AECOM consultant contract we found that SCAG inappropriately used two inconsistent federal funding sources to fund a consultant contract. One source of federal funds provided through DLA had a 20 percent local match and the second source provided through DOTP had an 11.47 percent local match. The AECOM contract did not segregate the tasks/activities by funding source to track work associated to the separate federal funding sources. We tested five AECOM consultant invoices and determined that SCAG arbitrarily allocated the costs between two separate work elements (one funded by DLA and one by DOTP) with no consultant documentation to support the allocation or split. Due to the lack of support for the allocation/split of costs, the local match cannot be supported and verified as accurate.

Additionally, we noted that SCAG included a term in a Funding Agreement amendment that allowed for the contract completion date to be subject to the completion of a separate consultant agreement as opposed to a required specific end date in the Funding Agreement amendment.

Several SCAG staff stated that they did not think it was the consultant's responsibility to identify work performed on each task and project on their invoices. SCAG accounting staff stated they were instructed by management to record local match costs to projects/work elements that were not supported by the consultant invoices. If SCAG is unable to support they are paying consultants for actual work performed on specific tasks separately from other funded work, they run the risk of billing Caltrans for unallowable costs.

See Attachment III finding 2 for detailed criteria.

RECOMMENDATION

We recommend SCAG reimburse Caltrans a total of $951,963 for the unallowable costs identified above ($590,538 of consultant costs + $361,426 on expired contract).

We also recommend SCAG:

- Ensure consultants provide adequate invoice detail to support costs claimed in compliance with consultant contract terms and 2 CFR Part 200 (which superseded 49 CFR Part 18, and 2 CFR Part 225). Additionally, ensure consultants are required to submit invoices that identify the work performed by task/activity and work element so proper documentation is maintained to support consultant billings and local match.
- Establish procedures that identify and define each staff's roles and responsibilities regarding consultant invoice reviews.
- Revise the Grants Management Policies and Procedures and develop a Project Management Policies and Procedures Manual to ensure compliance with all applicable state and federal regulations, and provide staff with detailed processes to follow.
- Ensure consultant contracts identify the funding sources and/or work elements of each task/activity when there are multiple funding sources and/or work elements.
- Ensure compliance with all state and federal regulations over the administration of consultant contracts and that the contracts contain language as required in the Caltrans' agreements.
- Ensure compliance with all state and federal regulations over the administration of sub-recipient (MOU) agreements, that agreements contain language as required in the Caltrans' agreements, and include specific contract end dates.
- Ensure staff are properly trained on the administration and management of consultant and sub-recipient pass through funds.

SUMMARY OF AUDITEE'S RESPONSE

SCAG concurs with the finding and recommendations except for two issues they requested be removed or revised. In Section I, SCAG disagrees with the bullet relating to "SCAG approved payment of a sub-recipient invoice with no supporting documentation to determine the reasonableness, allowability, and eligibility of the costs billed." SCAG contends the MOU included a clause that both parties agree to the value of the project as $158,000 and that the MOU takes precedence over the cost estimate.

In Section II (a), SCAG states, "Notwithstanding the requirements, SCAG relied on the retroactive language in Amendment No. 5 of the Parsons contract to keep the contract active despite it being executed after the contract's expiration date. Such language is an acceptable method for maintaining contracts, is legally binding, and is commonly used in expired commercial contracts." SCAG requests that IOAI eliminate the disallowance of the costs incurred after the Parsons contract expired.

Also in Section II (b), SCAG states, "The number of amendments to the AECOM contract are explained by the administrative needs of that contract and the fact that the outreach portion of the contract was put in abeyance and later restored when needed."

Furthermore in Section II(c), SCAG states, "Twelve of the SMG contract amendments were for administrative purposes, e.g., annual fiscal year funding, term and schedule changes, and line-item budget revisions. Three amendments were the result of the additional work added to the underlying AECOM contracts resulted to the new grant of $916,000 mentioned above."

SCAG indicated they received concurrence from United States Department of Transportation (USDOT) to proceed with the AECOM, Parsons, and SMG contracts without rebidding after 36 months.

See Attachment IV for SCAG's full response.

ANALYSIS OF AUDITEE'S RESPONSE

Based on IOAI's analysis of the response, we determined it was the sub-recipient's responsibility to receive proper documentation from its consultants, therefore, this bullet was removed from the report.

With regard to SCAG's position on amendments executed on expired contracts, we disagree. Per Chapter 10 of the LAPM, it states, "All contract amendments must be fully executed before the ending date of the contract." The disallowance of these costs will remain in the finding and recommendation.

With regard to the AECOM amendments and the proposed sub-consultant that was dropped from the executed contract, IOAI disagrees with SCAG's position that it is acceptable to execute a contract that substantially differs from the RFP task requirements that were solicited (Task 7 was the third largest task proposed and covered outreach that would be critical to the outcome of the project). Additionally, SCAG's procurement files lacked documentation to support and justify the management decisions made.

With regard to the SMG amendments, IOAI agrees some of the amendments were for administrative purposes, however three of the 14 amendments resulted in a change in the scope of work of the contract. Additionally, SCAG makes reference that the results of the dollar amendments to the SMG contract was the result of the AECOM contract. IOAI disagrees with SCAG's statement. The SMG contract relates to specific work associated to RTP (Planning

Project) whereas as the AECOM contract related to the Value Pricing Pilot Program (Local Assistance Project).

SCAG also makes note that they received concurrence from USDOT o to proceed with the AECOM, Parsons and SMG contracts without rebidding after 36 months. The information SCAG provided USDOT, however, did not disclose that the Parson's contract had already expired and that the 36 months had already lapsed on all the contracts involved. Furthermore, in SCAG's response they referred to SMG, however, SMG was not part of the Value Pricing Project.

Based on analysis of the response, the finding has been revised to remove of the one bullet noted above. In addition, AECOM and Parsons were removed from the finding relating to SCAG extending the contract terms over 36 months without re-solicitation.

FINDING 3 – Labor and Fringe Benefit Deficiencies

SCAG's labor and fringe benefit charging practices do not comply with Caltrans Agreement requirements, and state and federal regulations as noted below.

Labor Charges and Quarterly Reporting

Indirect and ineligible costs were charged to Work Element 120 which was established for direct costs related to Development and Administration of the Overall Work Program (OWP). Eligible tasks included the development of the OWP, preparation of the annual budget and amendments to the budget, and preparation of Quarterly Progress Reports.

Specifically we noted the following labor charging and reporting deficiencies:

- Accountants and contract administrators charged time for the review and approval of consultant invoices which were ineligible and indirect in nature.
- Thirteen project and section managers charged time for the review and approval of consultant invoices related to projects budgeted under work elements other than 120.
- Some project and section managers charged time related to managing other projects and activities to Work Element 120 when their budgets were depleted or underfunded.
- Ineligible labor for legal staff was charged to work element 120.
- Quarterly Progress Reports did not accurately represent the work that was actually performed and charged to Work Element 120.

SCAG staff acknowledged they mis-charged labor costs to work element 120 that were related to other projects and work elements when budgets were depleted or underfunded.

We determined SCAG billed and was reimbursed a total of $1,558,051 in ineligible direct labor charges to work element 120. These costs are disallowed. For a detail of the disallowed costs, see Attachment II,

In addition to the ineligible charges identified above, we noted instances where SCAG staff inconsistently charged time for staff meetings and an office holiday party.

Retroactive Pay and Merit Increases

SCAG's accounting for retroactive pay and merit increases occurred months after the increase was given, and the methodology used to allocate the increase did not accurately or equitably allocate to the month(s) and work element(s) worked by the employees. We found instances where accountants prepared or changed employee timesheets by adding hours (sometimes in excess of 20 hours in one day for a single employee) to adjust the ending pay to equal the total pay period. Additionally, there was no clear audit trail for charging and recording the pay increases.

Fringe Benefits

SCAG's methodology for billing fringe benefit costs was inaccurate and inconsistent with their Indirect Cost Allocation Plan (ICAP) calculation methodology which resulted in an inaccurate allocation of costs. SCAG did not allocate fringe benefit costs to intern and student assistant salaries. SCAG inappropriately allocated the intern and student assistant fringe benefit costs to all regular staff salaries (excluded intern and student assistant salaries). In addition, the ICAP calculation allocated the intern and student assistant fringe benefits to all staff salaries (included the interns and student assistants). The interns and student assistants have limited fringe benefit costs associated with their positions and require a separate fringe benefit allocation methodology to equitably allocate their costs.

SCAG does not have adequate policies and procedures related to labor charging practices, no documented procedures to account for time sheet corrections or retroactive pay and merit increases. In addition to billing ineligible costs identified, the inappropriate charging practices result in SCAG lacking accurate historical information related to actual costs for future budget purposes and overhead rate calculations.

See Attachment III finding 3 for detailed criteria.

RECOMMENDATION

We recommend SCAG:

- Reimburse Caltrans $1,558,051 for the disallowed costs identified above.
- Ensure billings to Caltrans are based on actual labor costs incurred.
- Ensure the accounting methodology for retroactive pay and merit increases provides for an audit trail for changes made to the employee time sheets and costs are allocated to the appropriate pay periods.
- Develop and implement written policies and procedures for proper and consistent labor charging practices. Ensure procedures define appropriate charging practices for staff meetings and other non-project or work element activities.

- Update the Accounting Manual to include procedures for time sheet corrections and retroactive pay and merit increases and train staff accordingly.
- Develop separate fringe benefit allocation methodologies for regular staff, interns and student assistants.

AUDITEE'S RESPONSE

Labor Charges and Quarterly Reporting
The practice of charging time to Work Element 120 other than that of Budget & Grants staff was begun many
years ago after consultation with District 7. Since the practice is no longer permissible, SCAG's fiscal year (FY) 18 actuals and FY19 budget will charge those hours to the Indirect Cost budget. SCAG requests
that the costs disallowed from Work Element 120 in FY15 be charged to the Indirect Cost budget in that year.

Retroactive Pay and Merit increases
SCAG has implemented new practices and is actively documenting new policies and procedures to more accurately account for retroactive pay rate changes.

Fringe Benefits
SCAG has implemented new practices and is actively developing new policies and procedures to more accurately allocate fringe benefit charges.

ANALYSIS OF AUDITEE'S RESPONSE

As SCAG was already reimbursed directly for the finding amount, SCAG would need to repay Caltrans the full $1,558,051 as indicated in the finding to avoid a double billing. Once SCAG repays the disallowed costs, they can make a request to DOTP to include the disallowed costs in the FY 2014/15 indirect cost pool. If the request is approved by DOTP, SCAG will then be required to submit a revised FY 2016/17 ICAP to IOAI that includes the adjustments to the carry forward year for review and approval prior to seeking reimbursement for any variance in the rate.

Based on analysis of the response, the finding remains as written.

FINDING 4 – Billing and Reporting Deficiencies

SCAG did not submit required documentation with their requests for reimbursement to support costs billed and did not submit Quarterly Progress Reports in accordance with the DOTP Master Fund Transfer Agreement and the DLA Master Agreement.

Specifically, we noted the following deficiencies:

- Three SCAG Consolidated Planning Grant billings did not include the CPG IT Reports, or comparable information, which would allow the Caltrans's district staff to reconcile and trace billed costs to supporting documentation. The Consolidated Planning Grant IT Reports provide a breakdown of the costs and funding sources by task associated to each respective work element, which provides a tie to the billings and SCAG's financial management system. By not providing all relevant information, Caltrans is not able to determine if costs are allowable and that costs are charged to the appropriate work elements.

- Two SCAG billings to DLA included a Funding Schedule with a column titled "Other Project" with no explanation. It was determined the "Other Project" column are costs related to consultant costs that are billed to another funding source. SCAG's billings should include schedules and support documentation that provide for transparency, full disclosure, and sufficient detail to support all activities performed that tie to SCAG's financial management system. The lack of adequate and relevant information included on schedules to support SCAG's billed costs increases the risk Caltrans will pay for unallowable costs.

The Master Fund Transfer Agreement requires Metropolitan Planning Organizations to prepare and submit requests for reimbursement of actual allowable costs incurred consistent with work elements described in their Overall Work Plan.

See Attachment III finding 4 for detailed criteria.

RECOMMENDATION

We recommend SCAG take the following actions:

- Ensure all billings to Caltrans include all applicable information and supporting documentation that trace to the billed costs and SCAG's financial management system. This includes ensuring the Consolidated Planning Grant IT Reports (or equivalent information) are provided and totaled by task associated to the respective work elements.
- Ensure supporting schedules provided with the billings include appropriate descriptions detailing where costs are being charged.

AUDITEE'S FULL RESPONSE

SCAG will be sure to include all applicable back up documentation in the future including items such as the CPG IT reports. Since the invoices were approved and reimbursed by CALTRANS, and SCAG commits to provide all applicable information in the future, ***SCAG requests that this finding be removed from the report.***

SCAG provided documentation after the exit interview for the Quarterly Progress reports and in return were informed that this item would be removed from the final report.

Regarding the column titled "Other Billing", SCAG will more fully describe its columns on the CPG invoice documentation.

ANALYSIS OF AUDITEE'S RESPONSE

SCAG states that "since the invoices were approved and reimbursed by Caltrans, and SCAG commits to provide all applicable information in the future" that this finding be removed from the report. We disagree because during our interviews with District 7 staff and the review of their billing files, not all applicable documents such as the Consolidated Planning Grants (CPG) IT Reports were submitted and available to be included in the files. Additionally, per interviews with SCAG's accounting staff, it was indicated the CPG IT Reports were not provided. It is SCAG's responsibility to provide all necessary documents that support each billing when submitting invoices to the District for reimbursement.

SCAG provided emails on July 24, 2018, related to submitting the FY 2014/15 Quarterly Progress Reports to District 7. The documentation provided supports that Quarterly Progress Reports were prepared and sent to the district, so this portion of the finding was removed as requested by SCAG. However, the content of the Quarterly Progress Reports supports the finding that SCAG submitted reports to Caltrans that did not accurately represent the work that was actually performed and charged to work element 120 as noted in finding 3.

Based on the analysis of the response, the finding remains as written except for the removal of the portion of the finding relating to the Quarterly Progress Reports.

FINDING 5 – Possible Conflict of Interest with Sponsorship Program

SCAG's Sponsorship Program gives the appearance of a possible conflict of interest. SCAG created a Sponsorship Program to solicit donations from individuals, entities, and organizations with an interest in accessing participants of SCAG's General Assembly for networking, relationship building, business opportunities, and information sharing. We noted that SCAG solicits and receives donations from consultants for its Sponsorship Program with whom they also enter into consultant contracts to perform work. SCAG lacks a documented process over the Sponsorship Program to ensure a conflict of interest does not occur. Additionally, SCAG does not have documented policies and procedures over the administration and management of the Sponsorship Program.

See Attachment III finding 5 for detailed criteria.

RECOMMENDATION

We recommend SCAG perform the following:

- Establish procedures over the Sponsorship program to ensure there is no real or appearance of a conflict of interest with consultants that provided donations to the Sponsorship Program and are awarded consultant contracts.
- Develop policies and procedures over the administration and management of the Sponsorship Program to ensure compliance with all state and federal regulations.

AUDITEE'S FULL RESPONSE

SCAG is in the process of developing written policies and procedures for its sponsorships, in compliance with all requirements, to ensure there are no real or apparent conflicts of interest.

ATTACHMENT I
INCURRED COST AUDIT OF SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS
LIST OF AUDITED AGREEMENTS / PROCUREMENTS

Federal/State Project Number	Caltrans Program	Caltrans Agreement Number	Project Name/Description	Caltrans Agreement Amount	SCAG Work Element	SCAG Consultant	Consultant Contract Amount	SCAG Invoice Number	SCAG Invoice Amount	Federal/ State Reimbursement Rate	Paid by Caltrans within Original Audit Period	Paid by Caltrans Outside Original Audit Period	Total Paid by Caltrans	Consultant Costs Reimbursed to SCAG
VPPP-6049(010)		53-6049R	Value Pricing Pilot Project	$ 4,116,802				5 and 6	$ 1,617,887	80.00%	$ 1,294,310	$ 2,967,371	$ 4,261,681	
Parsons Brinckerhoff, Inc.	DLA		Express Lane Project Component		265	Parsons Brinckerhoff, Inc.	$ 2,058,303							$ 1,517,802
AECOM Technical Services, Inc.	DLA		Cordon Project Component		265	AECOM Technical Services, Inc.	$ 4,071,936 (1)							$ 2,743,879
OWP FY 2014/15		74A0822	Federal Overall Work Program	$ 35,003,022				10 - 12	$ 8,679,186	88.53% / 80.00%	$ 7,828,453	$ 368,404	$ 8,196,857	
AECOM Technical Services, Inc.	DOTP		Cordon Project Component		015	AECOM Technical Services, Inc.	$ 4,071,936 (1)							$ 243,340
							Total Federal & State		$ 10,297,073		$ 9,122,763	$ 3,335,775	$ 12,458,538	$ 4,505,021

Note:
*** DOLA - Division of Local Assistance, DOTP - Division of Transportation Planning**

(1) SCAG entered into one consultant contract with AECOM for $4,071,936 that was used for multiple activities/tasks funded by two separate federal funding sources.

This page is intentionally left blank

ATTACHMENT II
INCURRED COST AUDIT OF SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS
DISALLOWED COSTS BY AGREEMENTS THROUGH 3/30/2018

Federal/State Project Number	Funded by DOTP / DOLA*	Caltrans Agreement Number	Project Name/Description	Work Element(s)	Consultant Name / SCAG Staff	Consultant Contract Amount	Period Costs Incurred	Finding 2 Contract Managment	Finding 3 Labor	Total Disallowed Costs Paid by Caltrans	Note
VPPP-6049(010) 6049(015)	DOLA	53-6049R	Value Pricing Pilot Project	265	Parsons Brinckerhoff, Inc.	$ 2,058,303	3/29/13-3/30/18	$ 361,426		$ 361,426	1
VPPP-6049(010) 6049(015)	DOLA	53-6049R	Value Pricing Pilot Project	265	AECOM Technical Services, Inc.	$ 4,071,936	4/25/13 - 3/30/18	$ 338,986		$ 338,986	1
Overall Work Program FY 14/15	DOTP	74A0822	Federal Overall Work Program	015	AECOM Technical Services, Inc.	$ 4,071,936	4/25/13 - 3/30/18	$ 103,971		$ 103,971	1,2
			" "	010/015/130	System Metrics Group, Inc.	$ 2,462,322	4/23/13 - 3/30/18	$ 134,083		$ 134,083	
			" "	130	Cambridge Systematics, Inc.	$ 420,404	4/30/14 - 3/30/18	$ 13,498		$ 13,498	
			" "	120	Accountants /Contract Administrators and Legal Staff	N/A	7/1/14 - 6/30/15		$ 1,558,051	$ 1,558,051	
			Total Consultant Contracts			$ 9,012,965					
							Total Disallowed Costs			$ 2,510,015	

Note:
*** DOLA - Division of Local Assistance, DOTP - Division of Transportation Planning**
1 - The amounts are included within the total per Attachment 1 (Consultant Cost Reimbursed to SCAG)
2 - The AECOM Contract related to DLA and DOTP. The contract amount was only include once in the total to avoid duplication.

This page is intentionally left blank

ATTACHMENT III
AUDIT CRITERIA

Finding 1 (Improper Procurement Practices)

1a. 23 CFR Part 172. 7 (a) (1) (ii) states that Request for proposal (RFP) shall provide all information and requirements necessary for interested consultants to provide a response to the RFP and compete for the solicited services. The RFP shall:

(B) Identify the requirements for any discussions that may be conducted with three or more of the most highly qualified consultants following submission and evaluation of proposals;

(F) require that submission of any requested cost proposals or elements of cost be in a concealed format and separate from technical/qualifications proposals, since these shall not be considered in the evaluation, ranking, and selection phase.

1b. 49 CFR Part 18. 36 (d) (3) (v) states that "Grantees and subgrantees may use competitive proposal procedures for qualifications-based procurement of architectural/engineering (A/E) professional services whereby competitors' qualifications are evaluated and the most qualified competitor is selected, subject to negotiation of fair and reasonable compensation. The method, where price is not used as a selection factor, can only be used in procurement of A/E professional services. It cannot be used to purchase other types of services though A/E firms are a potential source to perform the proposed effort."

1c. 23 CFR Part 172. 7 (a) (1) (iii) (B) states that "Price shall not be used as a factor in the evaluation, ranking, and selection phase. All price or cost related items which include, but are not limited to, cost proposals, direct salaries/wage rates, indirect cost rates, and other direct costs are prohibited from being used as evaluation criteria."

1d. 23 CFR Part 172.7(a) (1) (iv) (E) states that "Notification must be provided to responding consultants of the final ranking of the three most highly qualified consultants."

1e. LAPM Chapter 10.5 Develop Final Ranking and Notify Consultants of Results states, in part, that "the selection committee discusses and documents the strengths and weaknesses of each proposal; interviews the three or more highest ranked consultants; and develop a final rankings of the highest ranked consultants. All consultants that submitted proposals must be informed about the final ranking of consultants."

1f. 49 CFR Part 18.36 (c) (1) states in part, "All procurement transactions will be conducted in a manner providing full and open competition consistent with the standards of Sec. 18.36..."

1g. 49 CFR Part 18.36 (c) (3) states in part, "Grantees will have written selection procedures for procurement transactions. These procedures will ensure that all solicitations: (i) Incorporate a clear and accurate description of the technical requirements for the material, product, or service to be procured…and (ii) Identify all requirements which the offerors must fulfill and all other factors to be used in evaluating bids or proposals."

1h. 49 CFR Part 18.36 (b) (9) states, "Grantees and subgrantees will maintain records sufficient to detail the significant history of a procurement. These records will include, but are not necessarily limited to the following rationale: rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price."

1i. 49 CFR Part 18, Section 36 (b) states that "Grantees and subgrantees will use their own procurement procedures which reflect applicable State and local laws and regulations, provided that the procurements conform to applicable Federal law and the standards identified in this section."

1j. LAPM Chapter 10.9 states, in part, "Procurement by noncompetitive proposals may be used only when the award of a contract is infeasible under small purchase procedures, sealed bids or competitive proposals (23 CFR 172.7(a)(3)). FHWA considers these types of contracts as Sole Source contracts and should be used only in very limited circumstances. A Public Interest Finding prepared by the local agency and approved by Caltrans is required before establishing these services.

1k. California Public Contract Code §10348 states that "the department shall prescribe the conditions under which some or all of the provisions of this article may be waived in order to assist agencies in obtaining services and consultant services in an efficient and timely manner for contracts of less than twenty thousand dollars ($20,000)."

Finding 2 (Contract Management Deficiencies)

2a. Public Contract Code Part 2, Chapter 2, Article 4, Section 10348.5 states, "Each state agency shall designate at least one currently existing person or position within the state agency as a contract manager. Every contract manager shall have knowledge of legal contractual arrangements."

2b. 2 CFR Part 200.302 (b) (4) states, "Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets."

2c. 2 CFR Part 200.400 states, (a) "The non-federal entity is responsible for the efficient and effective 2administration of Federal awards through the application of sound management practices, and (b) …assume responsibility for administering Federal funds in a manner consistent with underlying agreements, program objectives, and the terms and conditions of the Federal award."

2d. SCAG's Master Fund Transfer Agreement No. 74A0822, Article III, Section 3.A states MPO shall establish and maintain and shall require that its subrecipients, contractors and subcontractors shall establish and maintain, an accounting system conforming to Generally Accepted Accounting Principles (GAAP) to support Requests for Reimbursement which segregate and accumulate the costs of wok elements by line item (i.e. direct labor, other direct costs, subrecipients/subcontractor, etc.) and enable the determination of expenditures at interim points of completion, and provide support for reimbursement payment vouchers or invoices." Article II, (1) states, "Reimbursements under this MFTA will be allowed if based upon actual costs expended and supported by MPO's accounting system."

Section (6) (a), "All costs associated with the Project shall be identified on the invoice with proper backup, along with documentation of the match paid by the Sub-Recipient…."

2e. 2 CFR Part 200.318 (b) states, "Non-Federal entities must maintain oversight to ensure that contractors perform in accordance with the terms, conditions, and specifications of their contracts or purchase orders."

2f. 23 CFR Part 172.9 (a) (1) states, in part, that contracting agency use project-specific contract for the performance of services and defined scope of work related to a specific project or projects.

2g. SCAG's Procurement Policy and Procedures Manual 7.6 states that "if SCAG is unable to negotiate final contract terms and conditions that are acceptable to SCAG, SCAG reserves the right to award the contract to another proposer."

2h. Caltrans LAPM Chapter 10.8 states, in part, "the Contractor Administrator request a revised cost proposal from the consultant after: (1) negotiations have been completed" and "proposed contracts for consultant services including those for subcontracted work exceeding $150,000, must be reviewed by the local agency to verify that work activities and schedules are consistent with the nature and scope of the project."

2i. SCAG's Procurement Policy and Procedures Manual 8.3.2 states, in part, "the SCAG PM will prepare a Specification or Scope of Work (including the items added and or deleted) and a Cost Estimate for the amended work and forward both to Contracts. The cost estimate is an internal document that the PM and CA will use to perform a cost analysis of the consultant's amendment offer" and "after receiving the consultant's amendment offer, the SCAG PM and the CA will conduct a cost analysis and negotiate (as necessary) a fair and reasonable price for the amended work."

2j. 2 CFR Part 200.323 and 49 CFR Part 18.36 (f) (1) states, in part, "Grantees and subgrantees must perform a cost or price analysis in connection with every procurement action including contract modifications. The method and degree of analysis is dependent on the facts surrounding the particular procurement situation, but as a starting point, grantees must make independent estimates BEFORE receiving bids or proposals."…. "A cost analysis will be necessary when adequate price competition is lacking, and for sole source procurements, including contract modifications or change orders, unless price reasonableness can be established on the basis of a catalog or market price of a commercial product sold in substantial quantities to the general public or based on prices set by law or regulation."

2k. (LAPM), Chapter 10, Section 10.2 states in part "… An independent cost estimate is needed to ensure that consultant services are obtained at a fair and reasonable price. … The estimate must include a break-down of (1) Direct labor costs, (2) Indirect costs, (3) General and administrative cost, (4) Other direct costs, (5) Sub-consultant costs and (6) Net fee …"

2l. SCAG's Procurement Policy and Procedures Manual 8.3.1 A. states, in part, "amendments must be within the original scope of work (i.e., no new scope should be added)."

2m. SCAG's Procurement Policy and Procedures Manual 7.11 states that Consistent with the State of California Contract Manual, Section 7.8, each consultant agreement should be re-solicited after a total of thirty-six (36) months consecutive with the same consultant (including any amendment to extend the contract's term), unless Caltrans or the Federal government gives SCAG statutory authority or a written exemption.

2n. SCAG's Procurement Policy and Procedures Manual 8.3.1 K. states that "Once the term of the contract has expired, no further amendments can be made (i.e., an amendment must be fully executed before the ending date of the contract)"

2o. Caltrans LAPM Chapter 10.8 states, in part, "a consultant contract may be amended at any time. The most common amendment is to extend the ending date of the contract. All contract amendments must be fully executed before the ending date of the contract."

2p. Caltrans LAPM Chapter 10.2 states, in part, "the scope of work, which the contract must include, is a detailed description of the products or services the consultant is to provide. From a detailed scope of work, consultants respond to a project advertisement; determine personnel and time requirements; and develop a technical proposal. Therefore, the scope of work must be clear, concise, complete, and describe the deliverables and deadlines."

2q. 2 CFR Part 200.404 (c), states, "Any costs allocable to a particular Federal award under the principles provided for in this part may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by Federal statutes, regulations, or terms and conditions of the Federal awards, or for other reasons."

2r. 2 CFR Part 200.302 (b) (2) states, "Accurate, current, and complete disclosure of the financial results of each Federal award or program in accordance with the reporting requirements…."

2s. SCAG's Master Agreement 53-6049R states in part, "Any subcontract entered into by Administering Agency as a result of this Agreement shall contain all the provisions of Article IV, Fiscal Provisions, and this Article V, Audits, Third Party Contracting Records Retention and Reports, …"

2t. Caltrans Local Assistance Procedures Manual (LAPM) Chapter 10.8 states that "agencies are required to prepare an evaluation of the consultant when the project has been completed. The Contract Administrator evaluates the consultant's performance after the consultant's final report has been submitted, and the Contract Administrator has conducted a detailed evaluation with the consultant's project manager."

2u. California Public Contract Code (PCC) §10369 states that (a) each state agency shall conduct a post-evaluation, by completing the post-evaluation form, of each consulting services contract totaling five thousand dollars ($5,000) or more that it executes and (b) the agency shall evaluate the performance of the contractor in doing the work or delivering the services for which the contract was awarded.

PCC §10369 also states that (d) the post-evaluation be prepared within 60 days of the completion of the contract.

2v. SCAG's Master Fund Transfer Agreement No. 74A0822, Article I, Section 1 L states, "MPO shall use non-federal funds to finance the local share of eligible cost to ensure compliance with all applicable matching requirements for federal funds described in this MFTA and actually encumbered against the annual OWPA. Credit for local match will be allowed only for work performed during the approved term of each annual OWPA.

2w. Chapter 10.2 of the LAPM states in part, The Contract Administrator is responsible for ensuring the quality of consultant contract products or services. The Contract Administrator is appointed as soon as the need for consultant services is identified. The Contract Administrator is involved throughout the development of the selection process and the contract provisions, and in the administration of the consultant's work. The Contract Administrator must be a qualified local agency employee, or have staff that is qualified to ensure the consultant's work is complete, accurate, and consistent with the terms and conditions of the consultant contract.

Finding 3 (Labor and Fringe Benefit Deficiencies)

3a. SCAG's Master Fund Transfer Agreement No. 74A0822,

- Article III, Section 1.A states, "MPO agrees to comply with Title 2 CFR Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards."
- Article III, Section 3.A states MPO shall establish and maintain and shall require that its subrecipients, contractors and subcontractors shall establish and maintain, an accounting system conforming to Generally Accepted Accounting Principles (GAAP) to support Requests for Reimbursement which segregate and accumulate the costs of wok elements by line item (i.e. direct labor, other direct costs, subrecipients/subcontractor, etc.) and enable the determination of expenditures at interim points of completion, and provide support for reimbursement payment vouchers or invoices." Article II, (1) states, "Reimbursements under this MFTA will be allowed if based upon actual costs expended and supported by MPO's accounting system."

3b. 2 CFR Part 200.404 (c), states, "Any costs allocable to a particular Federal award under the principles provided for in this part may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by Federal statutes, regulations, or terms and conditions of the Federal awards, or for other reasons."

3c. 2 CFR Part 200.302 (b) (2) states, "Accurate, current, and complete disclosure of the financial results of each Federal award or program in accordance with the reporting requirements….."

3d. 2 CFR Part 200.431 (a) (b) states in part, (1) "Fringe benefits are allowances and services provided by employers to their employers as compensation in addition to regular salaries and

wages…(2) 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: they are provided under established written leave policies; the costs are equitably allocated to all related activities, including Federal awards; and, the accounting basis selected for cost each type of leave is consistently followed by the non-Federal entity."

3e. 2 CFR Part 200.302 (b) (4) states, "Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets."

Finding 4 (Billing and Reporting Deficiencies)

4a. Article II, Section 2.A states in part, "MPO shall prepare and submit to state, one signed Requests for Reimbursements of actual allowable costs incurred by MPO consistent with work elements described in the OWP…Reimbursements under this MFTA will be allowed if based upon actual costs incurred and supported by MPO's accounting system…(1) Comparison of actual performances with work element-level goals and deliverables…"

4b. Article I, Section 2.A states, MPO agrees to submit to State, no later than 30 calendar days after the close of each quarter, Quarterly Progress Reports that include all work elements for transportation planning tasks, projects, and products funded wholly or in part by any of the fund sources listed in the "Recitals" section of this MFTA."

4c. Article I, Section 2.B states, State reserves the right to deem incomplete any Quarterly Progress Report that does not sufficiently document the above-required information and may withhold payment of Request for Reimbursement submitted pending the submission of required documentation.

4d. 2 CFR Part 200.302 (b) (4) states, "Internal Control. Effective control and accountability must be maintained for all grant and subgrant cash, real and personal property, and other assets."

4e. SCAG's Master Agreement 53-6049R, Article IV, Section 5 states, "Invoices must have at least one copy of supporting backup documentation for costs incurred and claimed for reimbursement by Administering Agency. Acceptable backup documentation includes, but is not limited to, agency's progress payment to the contractors, copies of cancelled checks showing amounts made payable to vendors and contractors, and/or a computerized summary of project costs."

Finding 5 (Possible Conflict of Interest with Sponsorship Program)

5a. 49 CFR Part 18.36 (b) (3) and 2 CFR Part 200.318 (C) (1), states in part, "Grantees and subgrantees will maintain a written code of standards of conduct governing the performance of their employees engaged in the award and administration of contracts. No employee, officer or agent of the grantee or subgrantee shall participate in selection, or in the award or administration of a contract supported by Federal funds if a conflict of interest, real or apparent, would be involved. Such a conflict would arise when: (i) The employee, officer or agent, (ii) Any member of his immediate family, (iii) His or her partner, or (iv) An organization which

employs, or is about to employ, any of the above, has a financial or other interest in the firm selected for award…"

5b. Public Contract Code Part 2, Chapter 2, Article 8, Section 10410 (a) states, "No officer or employee in the state civil service or other appointed state official shall engage in any employment, activity, or enterprise from which the officer or employee receives compensation or in which the officer or employee has a financial interest and which is sponsored or funded, or sponsored and funded, by any state agency or department through or by a state contract unless the employment, activity, or enterprise is required as a condition of the officer's or employee's regular state employment. No officer or employee in the state civil service shall contract on his or her own individual behalf as an independent contractor with any state agency to provide services or goods."

5c. Government Code, Title 9, Chapter 7, Article 1, Section 87100, states, No public official at any level of state or local government shall make, participate in making or in any way attempt to use his official position to influence a governmental decision in which he knows or has reason to know he has a financial interest.

5d. Government Code, Section 87103, states, "A public official has a financial interest in a decision within the meaning of Section 87100 if it is reasonably foreseeable that the decision will have a material financial effect, distinguishable from its effect on the public generally, on the official, a member of his or her immediate family, or on any of the following: (e) Any donor of, or any intermediary or agent for a donor of, a gift or gifts aggregating two hundred fifty dollars ($250) or more in value provided to, received by, or promised to the public official within 12 months prior to the time when the decision is made….."

This page is intentionally left blank

FINDINGS AND RECOMMENDATIONS

FINDING 1 – Improper Procurement Practices

Southern California Association of Governments' (SCAG) did not ensure that fair and open competition was performed, or that proper procurement procedures were followed, as required by state and federal regulations, and the California Department of Transportation's (Caltrans) agreement provisions. Additionally, SCAG's Procurement Policy and Procedures Manual that was in effect during the period of the procurements tested, did not fully comply with state and federal procurement regulations, and Caltrans agreement provisions. Specifically, we found the following procurement deficiencies:

I. Consultant Procurement Deficiencies

AECOM Technical Services, Inc. and Parsons Brinckerhoff, Inc.

SCAG issued RFP 13-008 for the Value Pricing Project that resulted in two consultant contracts. We determined that the RFP was for an Architectural & Engineering (A&E) consultant(s) as the scope of work as written was specialized and required professional engineering judgement, traffic engineering, environmental specialties, roadway design/infrastructure cost estimates, and system integration. SCAG executed two contracts from the RFP, one with AECOM Technical Services, Inc. (AECOM), and one with Parsons Brinckerhoff, Inc. (Parsons). We reviewed the related procurement documents for the two consultants and found the following:

- The scope of work for RFP 13-008 was for the procurement of A&E services and price was used as an evaluation factor in the selection of the two A&E consultants. Title 23 CFR Part 172, states, "price shall not be used as a factor in the evaluation, ranking and selection process" when procuring engineering services.

- The RFP did not include the following:

  - A requirement to submit the cost proposals in a concealed format, separate from technical/qualification proposals.
  - Identification of the requirements for any discussions (interviews) that may be conducted with three or more of the most highly qualified consultants following submission and evaluation of proposals. SCAG performed interviews of the consultants and included interview evaluations in the selection process.

- Notifications (Notice of Intent to Award) of the final ranking of the three most highly qualified consultants were not issued to all corresponding consultants.

System Metrics Group

SCAG issued RFP 13-023 for the Regional Transportation Plan Implementation and Project Management Assistance Services that resulted in a non-competitive (sole source) procurement with System Metrics Group (SMG). We found that SCAG did not prepare a Public Interest Finding for Caltrans approval prior to executing the contract with SMG as required by Caltrans agreement provisions.

II. Procurement Policies and Procedures Manual Deficiencies

We reviewed SCAG's Procurement Policies and Procedures Manual and determined the following procedures were missing or misstated:

- Procedures for procuring Architectural and Engineering (A&E) consultants.
- Procedures for documenting a Public Interest Finding on non-competitive procurements.
- Section 6.6.2 Formal Solicitation was unclear as it began with language related to an Invitation for Bids, however, the documented detailed procedures relate to a Request for Proposal process for non-A&E consultants.
- SCAG's threshold of $25,000 for waiving competition for non A&E General Fund consultant procurements was higher than the requirements of the California Public Contract Code (PCC) of $20,000.

SCAG staff stated they lacked training and guidance on proper procurement processes and applicable procurement regulations. Without proper procurement practices, and procurement policies and procedures, SCAG may not be able to support fair and open procurements at a reasonable price.

See Attachment I for a summary of audited agreements, and procurements tested with the associated costs.

See Attachment III finding 1 for detailed criteria.

RECOMMENDATION

We recommend SCAG:

- Review and revise their Procurement Policies and Procedures Manual to ensure it is current and complies with all applicable Caltrans requirements, and state and federal procurement regulations. Include revising section 6.6.2 to describe the different competitive procurement processes available and when each should be used in compliance with state and federal regulations.
- Ensure management and staff receive proper training in procurement procedures.
- Ensure staff that are involved in the consultant procurement process perform all required actions and comply with SCAG policies and procedures, Caltrans requirements, and state and federal procurement regulations.

- Ensure all documentation is maintained to support that proper procurement procedures are followed in accordance with state and federal regulations.
- Take Caltrans, Division of Local Assistance (DLA) A&E consultant procurement training either in person or online at http://www.dot.ca.gov/hq/LocalPrograms/training.html

In addition, we recommend Caltrans, Division of Transportation Planning (DOTP) and Division of Local Assistance (DLA) provide enhanced oversight over SCAG's future procurements.

AUDITEE'S RESPONSE

I. Consultant Procurement Deficiencies

AECOM Technical Services, Inc. and Parsons Brinckerhoff, Inc.

SCAG requests that this finding be removed from the report.

In the Exit Conference for this audit, IOAI staff stated that the written guidance regarding Architectural & Engineering projects could have been more clear for the years that relate to these findings. It was shared that IOAI had audited other funding recipients and made similar findings and that they learned that the guidance could have been more clear. This is supported by the publication of FTA's *Best Practices Procurement & Lessons Learned Manual* (October 2016), which had it been in existence at the time of this contract's inception, would have clarified that RFP 13-008 was not A&E in nature. Sec. 3.4.9 of the Manual (Attachment 1) states that:

Thus if services, such as program management, feasibility studies, or mapping, are not directly in support of, or directly connected to, or directly related to, or lead to construction, alteration, alteration, or repair of real property, then the recipient may not use qualifications-based procurement procedures to select the contractor that will perform those services. [Page 59]

Additionally, SCAG asserts that the related Cooperative Agreement among Caltrans, SCAG and FHWA which in Sec. 6.a (Attachment 2) refers to the work as Intelligent Transportation Systems work:

All pricing requirements must conform to 23 CFR 940 which requires a systems engineering analysis. Refer to CALTRANS Local Assistance Program Guide, Chapter 13 "Intelligent Transportation Systems (ITS) Program".

Sec. 9.2 of the Caltrans Consultant Procurement Manual issued by the Division of Local assistance dated April 2017 states that ITS projects that are the "development of a concept of operations" are non-A&E [page 59 (Attachment 3)]. This project was a concept of operations and therefore, SCAG asserts it was not an A&E project.

SCAG also asserts that eliminating price would not have altered the consultant selection and that John Yang of Caltrans District 7 staff participated in the procurement process and did not raise any objections to SCAG's procurement process at any time.

System Metrics Group
SCAG requests that this finding be removed from the report.

This procurement included Mr. Elhami Nasr from CALTRANS District 7 on the evaluation team. He was aware that there was only one proposer, yet did not cite any further steps required to complete the selection. CALTRANS guidance on single proposer/sole source procurements has not been clear and remains unclear today.

During the course of this audit, the IAOI staff advised SCAG to obtain approval from Caltrans of a Public Interest Finding (PIF) for single proposer/sole source procurements. However, SCAG has since been advised by Mr. Vijay Kopparam of District 7 and Ms. Erin Thompson of Caltrans Headquarters that the PIF form does not apply to non-construction contracts. This is supported by the language in the guidance for the Public Interest Finding form itself (Attachment 4) which states on page 1 that "A Public Interest Finding is required for Federal-aid ***highway construction projects*** (emphasis added) for…" SCAG was advised by FHWA in a July 5, 2018 email (Attachment 5), in which Caltrans was copied, to seek approval of sole source procurements via an email request not the PIF form. Three requests have been approved in this manner since that time and this procedure will be incorporated into SCAG's policies and procedures.

SCAG cites FTA Procurement Circular 4220.1F at Ch.VI, Section 3.i.(1)(b)2 (Rev. 4, March 18, 2013) (Attachment 6) which states that if a competitive solicitation results in one bid, the recipient should review the specifications used to determine if they were overly restrictive. If the recipient determines the specifications were not overly restrictive and that other companies could have met the specification but chose not to bid for other reasons, the procurement qualifies as a valid competitive award. SCAG conducted a survey of the firms solicited to determine why the response yielded only one bidder. A summary of their responses is in Attachment 7 and this information was reported to the RC on April 4, 2013 (Attachment 8, page 40). The main reason cited for not responding was that they were unable to team up with a prime consultant or were too busy with other work. This supports the idea that the scope of work was not too restrictive.

In light of the above, SCAG requests that this finding be removed.

II. Procurement Policies and Procedures Manuals Deficiencies.
SCAG is updating its policies and procedures to comply with all applicable requirements and will provide training to staff.

ANAYLSIS OF AUDITEE'S RESPONSE

FINDING 2 – Contract Management Deficiencies

SCAG's contract management system did not comply with state and federal regulations and Caltrans agreement provisions. We found that SCAG billed Caltrans for unsupported and unallowable consultant and sub-recipient costs. Furthermore, we found that SCAG improperly managed consultant and sub-recipient contracts, did not properly close-out consultant contracts, executed amendments on expired contracts, and could not support all local match requirements

were met. Additionally, SCAG lacked contract management policies and procedures detailing proper processes to manage consultant and sub-recipient contracts and detailed procedures for reviewing and approving invoices. SCAG billed and was reimbursed $590,537 in unsupported consultant costs, and $361,426 on an expired consultant contract. These costs are disallowed.

Specifically we found the following:

I. Consultant and Sub-recipient Invoice Deficiencies

We tested twenty-three consultant invoices (from ten consultants) and found that SCAG lacked documented support for consultant costs charged to projects/work elements, and they approved and paid consultant costs lacking adequate support. We tested three sub-recipient invoices and found that SCAG lacked documentation to support invoiced costs on one of the sub-recipient invoices tested.

- 10 of 23 consultant invoices were arbitrarily split and allocated to more than one project/work element with no source documentation to support the actual costs applicable to each project/work element. The unsupported consultant costs total $590,538 and are disallowed.
- 7 of 23 consultant progress reports submitted with the invoices did not include the percentage of work completed as required in the consultant contracts.
- 1 of 23 consultant invoices was approved without a required progress report.
- SCAG approved payment of a sub-recipient invoice with no supporting documentation to determine the reasonableness, allowability, and eligibility of the costs billed.

SCAG's review and approval process of consultant and sub-recipient invoices was performed by project managers, section managers, accountants, contract administrators (for consultants) and budgets and grants staff (for sub-recipients). SCAG's review and approval process was not documented and staff were unclear as to the roles and responsibilities of each area in the process. SCAG's accounting staff stated that based on the lack of detailed information included on the consultant invoices, there was no way to determine which project(s) the consultant costs related to. The practice of accepting and arbitrarily splitting consultant invoices that lack appropriate information detailing what tasks/activities the consultant performed work increases the risk of unallowable costs being charged to Caltrans.

SCAG's Budgets and Grants Management Policies and Procedures, were not clear and did not define the roles and responsibilities of project managers. Furthermore, SCAG did not have written policies and procedures for project managers and other staff reviewing and approving invoices of sub-recipients and consultants. SCAG staff acknowledged they had inadequate Project Management and Grant Management Policies and Procedures in place to provide staff guidance. SCAG stated that they are in the process of developing policies and procedures for staff that define staff roles and responsibilities and provide guidance to the project managers. The lack of policies and procedures and weak invoice approval processes increase the risk of unallowable costs being billed to Caltrans.

II. Consultant and Sub-recipient Contract Deficiencies

We tested three consultant contracts and found that SCAG billed costs incurred on an expired contract and did not perform and/or document required actions related to properly managing consultant contracts. We also tested three sub-recipient agreements and found all three lacked required language to comply with Caltrans agreement provisions. Specifically we found the following:

- SCAG executed an amendment on an expired contract for the consultant contract with Parsons and billed costs to Caltrans that were incurred after the contract expiration date. Additionally, work was amended into the contract for the LA County Express Lane Strategic Plan on behalf of another agency that was outside of the original scope of work. Parsons original contract of $1,859,803 was amended 12 times to add $195,500 to total $2,058,303. Amendment 5 was executed after the contract expiration date. Therefore, amendments 5 through 12 are invalid and subsequent costs billed to Caltrans totaling $361,426 are disallowed.
- The scope of work for the RFP and the AECOM consultant contract were not clearly defined as evidenced by the contract being amended 15 times. Nine amendments changed the scope of work and six amendments added additional funds. The original contract amount was $2,065,599. Amendments totaling $2,306,337 were added for a total contract amount of $4,371,936, an increase of 112 percent. In addition, the contract was executed even though the final contract Terms and Conditions did not appear to be finalized. One proposed sub-consultant was deleted from task 7 on the executed contract with no documented justification. Additionally, 5 amendments included changes to the scope, and additions of sub-consultants and dollars to task 7.
- The scope of work on the RFP for the SMG consultant procurement was not clearly defined as evidenced by the contract being amended 14 times. Three amendments added additional funds. The original contract amount was $1,839,422. Amendments totaling $622,900 were added for a total contract amount of $2,463,322, an increase of 34 percent.
- The project manager and contract administrator did not always perform an independent cost estimate, an analysis of the cost proposal, and cost negotiation when they amended the AECOM and SMG consultant contracts. In addition, not all cost estimates that were prepared for the AECOM, Parson's and SMG contracts were signed and dated to support they were prepared prior to cost negotiation and execution.
- SCAG extended the contract terms for the AECOM, Parson's, and SMG consultant contracts over thirty-six (36) months without re-solicitation in violation of SCAG's Procurement Policies and Procedures.
- Three sub-recipient Memorandums of Understanding (MOU) agreements tested lacked required language below:
  - Project related travel and subsistence expense of contractors should be in accordance with California Department of Personnel Administration rates.
  - Sub-contractor and third party compliance for applicable cost principles should be with 48 CFR Ch. 1 Part 31.
  - Requirement to specify the type of contract as required by the Caltrans Local Assistance Procedures Manual (LAPM), Chapter 10.

The MOUs also included inaccurate regulations. The MOUs cited sub-recipients were to comply with 48 CFR Chapter 1 Part 31 instead of 49 CFR Part 18 which was superseded by 2 CFR 200.

III. Consultant Contract Close-out Deficiencies

SCAG's contract close-out process was not in compliance with Caltrans agreement provisions and state requirements on both consultant contracts tested. The project managers for these contracts did not perform a contact performance evaluation or a post evaluation of the consultants as required by DLA's Local Assistance Procedures Manual (LAPM) Chapter 10.8 and the PCC §10369. Additionally, both contracts were closed out with no support to indicate all deliverables had been met or completed as required by the contract. Specifically, the first contract close-out lacked documentation of required summary memos for a workshop, and whether five meetings and presentations were held/given. The second lacked documentation of five meetings held, two presentations, a summary report, a catalog of public comment and a project completion plan.

The contract close-out procedures in SCAG's Procurement Policy and Procedures Manual were not developed in compliance with Caltrans LAPM and state regulations. One project manager was not aware of SCAG's contract close-out process and the departments involved. Lack of proper contract close-out processes impacts the ability of staff to understand and ensure compliance of the contracted work or services as specified in the contract.

IV. Local Match Deficiencies

During our testing of the AECOM consultant contract we found that SCAG inappropriately used two inconsistent federal funding sources to fund a consultant contract. One source of federal funds provided through DLA had a 20 percent local match and the second source provided through DOTP had an 11.47 percent local match. The AECOM contract did not segregate the tasks/activities by funding source to track work associated to the separate federal funding sources. We tested five AECOM consultant invoices and determined that SCAG arbitrarily allocated the costs between two separate work elements (one funded by DLA and one by DOTP) with no consultant documentation to support the allocation or split. Due to the lack of support for the allocation/split of costs the local match cannot be supported and verified as accurate.

Additionally, we noted that SCAG included a term in a Funding Agreement amendment that allowed for the contract completion date to be subject to the completion of a separate consultant agreement as opposed to a required specific end date in the Funding Agreement amendment.

Several SCAG staff stated that they did not think it was the consultant's responsibility to identify work they performed on each task and project on the consultant's invoices. SCAG accounting staff stated they were instructed by management to record local match costs to projects/work elements that were not supported by the consultant invoices. If SCAG is unable to support they are paying consultants for actual work performed on specific tasks separately from other funded work they run the risk of billing Caltrans for unallowable costs.

See Attachment III finding 2 for detailed criteria.

RECOMMENDATION

We recommend SCAG reimburse Caltrans a total of $951,963 for the unallowable costs identified above ($590,538 of consultant costs + $361,426 on expired contract).

We also recommend SCAG:

- Ensure consultants provide adequate invoice detail to support costs claimed in compliance with consultant contract terms and 2 CFR Part 200 (which superseded 49 CFR Part 18, and 2 CFR Part 225). Additionally, ensure consultants are required to submit invoices that identify the work performed by task/activity and work element so proper documentation is maintained to support consultant billings and local match.
- Ensure sub-recipients provide adequate invoice detail and/or support that dollars claimed are actually incurred and in compliance with 2 CFR Part 200.
- Withhold payment of invoices from sub-recipients who fail to provide adequate invoice detail and/or supporting documentation.
- Establish procedures that identify and define each staff's roles and responsibilities regarding consultant invoice reviews.
- Revise the Grants Management Policies and Procedures and develop a Project Management Policies and Procedures Manual to ensure compliance with all applicable state and federal regulations, and provide staff with detailed processes to follow.
- Ensure consultant contracts identify the funding sources and/or work elements of each task/activity when there are multiple funding sources and/or work elements.
- Ensure compliance with all state and federal regulations over the administration of consultant contracts and that the contracts contain language as required in the Caltrans' agreements.
- Ensure compliance with all state and federal regulations over the administration of sub-recipient (MOU) agreements, that agreements contain language as required in the Caltrans' agreements and include specific contract end dates.
- Ensure staff are properly trained on the administration and management of consultant and sub-recipient pass through funds.

AUDITEE'S RESPONSE

I. Consultant and Sub-recipient Invoice Deficiencies

SCAG concurs with the findings with the exception of: "SCAG approved payment of a sub-recipient invoice with no supporting documentation to determine the reasonableness, allowability, and eligibility of the costs billed." This is a reference to SCAG's files lacking the final cost estimate from the sub-recipient. However, the payment packet includes the MOU (Attachment 9) in which on page 4, both parties "agree and acknowledge that the total value of the project is $158,000…" ***This takes precedence over the cost estimate and SCAG requests that this finding be removed.***

II. Consultant and Sub-recipient Contract Deficiencies

SCAG requests that the finding for the Parson's Contract and associated disallowed costs note the following information and also eliminate the disallowed costs of $361,246.

a. Notwithstanding the requirements, SCAG relied on the retroactive language in Amendment No. 5 of the Parsons contract to keep the contract active despite it being executed after the contract's expiration date. Such language is an acceptable method for maintaining contracts, is legally binding, and is commonly used in expired commercial contracts.

b. The number of amendments to the AECOM contract are explained by the administrative needs of that contract and the fact that the outreach portion of the contract was put in abeyance and later restored when needed. Also, SCAG received a new grant in the amount of $916,000 to perform additional work and this was amended into the AECOM contract.

c. Twelve of the SMG contract amendments were for administrative purposes, e.g., annual fiscal year funding, term and schedule changes, and line-item budget revisions. Three amendments were the result of the additional work added to the underlying AECOM contracts related to the new grant of $916,000 mentioned above.

d. SCAG agrees that it could not produce all required records of independent cost estimates, analyses of cost proposals, and cost negotiations and is putting in place policies and procedures to ensure required procedures are followed and documentation kept.

e. SCAG received concurrence from Angela Jacobs, USDOT on September 14, 2015 (Attachment 10) to proceed with the AECOM, Parson's and SMG contracts without rebidding after 36 months.

f. SCAG will update the language in its MOUs to comply with all applicable requirements.

III. Consultant Contract Closeout Deficiencies

SCAG has updated its contract closeout procedures to comply with all applicable requirements.

IV. Local Match deficiencies

SCAG agrees that the consultant should indicate on the invoices which project/WE is being billed. This will ensure that the associated match is recorded correctly.

Regarding the Funding Agreement amendment that allowed for the contract completion date to be subject to the completion of a separate consultant agreement, this was done to allow the Funding Agreement to terminate without an amendment when the related consultant services were completed. This provided evidence of commitment to the project until completed and avoided an amendment to an agreement that had five parties, which can prove inefficient, slow, cumbersome and impact project delivery.

ANAYLSIS OF AUDITEE'S RESPONSE

FINDING 3 – Labor and Fringe Benefit Deficiencies

SCAG's labor and fringe benefit charging practices do not comply with Caltrans Agreement requirements, and state and federal regulations as noted below.

Labor Charges and Quarterly Reporting

Indirect and ineligible costs were charged to work element 120 which was established for direct costs related to Development and Administration of the Overall Work Program (OWP). Eligible tasks included the development of the OWP; preparation of the annual budget and amendments to the budget; and preparation of Quarterly Progress Reports.

Specifically we noted the following labor charging and reporting deficiencies:

- Accountants and contract administrators charged time for the review and approval of consultant invoices which were ineligible and indirect in nature.
- Thirteen project and section managers charged time for the review and approval of consultant invoices related to projects budgeted under work elements other than 120.
- Some project and section managers charged time related to managing other projects and activities to work element 120 when their budgets were depleted or underfunded.
- Ineligible labor for legal staff was charged to work element 120.
- Quarterly Progress Reports did not accurately represent the work that was actually performed and charged to work element 120.

SCAG staff acknowledged they miss-charged labor costs to work element 120 that were related to other projects and work elements when budgets were depleted or underfunded.

We determined SCAG billed and was reimbursed a total of $1,558,051 in ineligible direct labor charges to work element 120. These costs are disallowed. For a detail of the disallowed costs, see Attachment II,

In addition to the ineligible charges identified above, we noted instances where SCAG staff inconsistently charged time for staff meetings and an office holiday party.

Retroactive Pay and Merit Increases

SCAG's accounting for retroactive pay and merit increases occurred months after the increase was given, and the methodology used to allocate the increase did not accurately or equitably allocate to the month(s) and work element(s) worked by the employees. We found instances where accountants prepared or changed employee timesheets by adding hours (sometimes in excess of 20 hours in one day for a single employee) to adjust the ending pay to equal the total pay period. Additionally, there was no clear audit trail for charging and recording the pay increases.

Fringe Benefits

SCAG's methodology for billing fringe benefit costs was inaccurate and inconsistent with their Indirect Cost Allocation Plan (ICAP) calculation methodology which resulted in an inaccurate allocation of costs. SCAG did not allocate fringe benefit costs to intern and student assistant salaries. SCAG inappropriately allocated the intern and student assistant fringe benefit costs to all regular staff salaries (excluded intern and student assistant salaries). In addition, the ICAP calculation allocated the intern and student assistant fringe benefits to all staff salaries (included the interns and student assistants). The interns and student assistants have limited fringe benefit costs associated with their positions and require a separate fringe benefit allocation methodology to equitably allocate their costs.

SCAG does not have adequate policies and procedures related to labor charging practices, and no documented procedures to account for time sheet corrections or retroactive pay and merit increases. In addition to billing ineligible costs identified, the inappropriate charging practices result in SCAG lacking accurate historical information related to actual costs for future budget purposes, and overhead rate calculations.

See Attachment III finding 3 for detailed criteria.

RECOMMENDATION

We recommend SCAG:

- Reimburse Caltrans $1,558,051 for the disallowed costs identified above.
- Ensure billings to Caltrans are based on actual labor costs incurred.
- Ensure the accounting methodology for retroactive pay and merit increases provides for an audit trail for changes made to the employee time sheets and costs are allocated to the appropriate pay periods.
- Develop and implement written policies and procedures for proper and consistent labor charging practices. Ensure procedures define appropriate charging practices for staff meetings and other non-project or work element activities.
- Update the Accounting Manual to include procedures for time sheet corrections and retroactive pay and merit increases and train staff accordingly.
- Develop separate fringe benefit allocation methodologies for regular staff, and interns and student assistants.

AUDITEE'S RESPONSE

Labor Charges and Quarterly Reporting

The practice of charging time to WE 120 other than that of Budget & Grants staff was begun many years ago after consultation with District 7. Since the practice is no longer permissible, SCAG's FY18 actuals and FY19 budget will charge those hours to the Indirect Cost budget. SCAG requests that the costs disallowed from WE 120 in FY15 be charged to the Indirect Cost budget in that year.

Retroactive Pay and Merit increases

SCAG has implemented new practices and is actively documenting new policies and procedures to more accurately account for retroactive pay rate changes.

Fringe Benefits
SCAG has implemented new practices and is actively developing new policies and procedures to more accurately allocate fringe benefit charges.

ANAYLSIS OF AUDITEE'S RESPONSE

FINDING 4 – Billing and Reporting Deficiencies

SCAG did not submit required documentation with their requests for reimbursement to support costs billed, and did not submit Quarterly Progress Reports in accordance with the DOTP Master Fund Transfer Agreement (MFTA) and the DLA Master Agreement.

Specifically, we noted the following deficiencies:

- Three SCAG Consolidated Planning Grant billings did not include the CPG IT Reports, or comparable information, which would allow the Caltrans's district staff to reconcile and trace billed costs to supporting documentation. The Consolidated Planning Grant IT Reports provide a breakdown of the costs and funding sources by task associated to each respective work element, which provides a tie to the billings and SCAG's financial management system. By not providing all relevant information, Caltrans is not able to determine if costs are allowable, and that costs are charged to the appropriate work elements.

- SCAG did not submit the Quarterly Progress Reports to the district as required per the MFTA. Without the Quarterly Progress Reports, Caltrans is not able to determine if the costs billed are in line with the progress of the project, or that they relate to the appropriate work element.

- Two SCAG billings to DLA included a Funding Schedule with a column titled "Other Project" with no explanation. It was determined the "Other Project" column are costs related to consultant costs that are billed to another funding source. SCAG's billings should include schedules and support documentation that provide for transparency, full disclosure, and sufficient detail to support all activities performed that tie to SCAG's financial management system. The lack of adequate and relevant information included on schedules to support SCAG's billed costs increases the risk Caltrans will pay for unallowable costs.

The MFTA requires Metropolitan Planning Organizations to prepare and submit requests for reimbursement of actual allowable costs incurred consistent with work elements described in their Overall Work Plan.

See Attachment III finding 4 for detailed criteria.

RECOMMENDATION

We recommend SCAG take the following actions:

- Ensure all billings to Caltrans' include all applicable information and supporting documentation that trace to the billed costs and SCAGs financial management system. This includes ensuring the Consolidated Planning Grant IT Reports (or equivalent information) are provided and totaled by task associated to the respective work elements.
- Submit Quarterly Progress Reports to Caltrans in compliance with the MTFA.
- Ensure supporting schedules provided with the billings include appropriate descriptions detailing where costs are being charged.

AUDITEE'S RESPONSE

SCAG will be sure to include all applicable back up documentation in the future including items such as the CPG IT reports. Since the invoices were approved and reimbursed by CALTRANS, and SCAG commits to provide all applicable information in the future, ***SCAG requests that this finding be removed from the report.***

SCAG provided documentation after the exit interview for the Quarterly Progress reports and in return were informed that this item would be removed from the final report.

Regarding the column titled "Other Billing", SCAG will more fully describe its columns on the CPG invoice documentation.

ANAYLSIS OF AUDITEE'S RESPONSE

FINDING 5 – Possible Conflict of Interest with Sponsorship Program

SCAG's Sponsorship Program gives the appearance of a possible conflict of interest. SCAG created a Sponsorship Program to solicit donations from individuals, entities, and organizations with an interest in accessing participants of SCAG's General Assembly for networking, relationship building, business opportunities, and information sharing. We noted that SCAG solicits and receives donations from consultants for its Sponsorship Program that they also enter into consultant contracts with to perform work. SCAG lacks a documented process over the Sponsorship Program to ensure a conflict of interest does not occur. Additionally, SCAG does not have documented policies and procedures over the administration and management of the Sponsorship Program.

See Attachment III finding 5 for detailed criteria.

RECOMMENDATION

We recommend SCAG perform the following:

- Establish procedures over the Sponsorship program to ensure there is no real or appearance of a conflict of interest with consultants that provided donations to the Sponsorship Program and are awarded consultant contracts.
- Develop policies and procedures over the administration and management of the Sponsorship Program to ensure compliance with all state and federal regulations.

AUDITEE'S RESPONSE

SCAG is in the process of developing written policies and procedures for its sponsorships, in compliance with all requirements, to ensure there are no real or apparent conflicts of interest.

ANAYLSIS OF AUDITEE'S RESPONSE

State of California
DEPARTMENT OF TRANSPORTATION

California State Transportation Agency

Memorandum

Making Conservation a California Way of Life.

To: CHRIS SCHMIDT
Chief
Division of Transportation Planning

Date: January 9, 2019

File: P1580-0023

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

Subject: INDIRECT COST ALLOCATION PLAN AUDIT – SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS

We performed an Indirect Cost Allocation Plan (ICAP) audit of the Southern California Association of Governments (SCAG) to determine whether SCAG's FY 2016/17 ICAP was presented in accordance with Title 2 Code of Federal Regulations (CFR) Part 200 and Caltrans's Local Assistance Program Manual (LAPM) Chapter 5. It was also performed to determine whether SCAG had a financial management system capable of accumulating and segregating costs that are reasonable, allowable, and can be allocated to projects. This audit of the financial management system also included testing of procurement and contract management systems to ensure compliance with state and federal regulations. The final report, along with SCAG's full response, is attached.

Based on audit work performed, we determined that SCAG's ICAP for the FY 2016/17 is presented in accordance with 2 CFR Part 200 and LAPM Chapter 5. The approved indirect cost rate for 2016/17 is 83.71 percent of total direct salaries and wages, plus fringe benefits. During the course of the audit, we found that SCAG's procurement practices and charging practices (related to properly segregating direct and indirect costs) were not in compliance with state and federal regulations. The noncompliant practices resulted in unallowable costs billed direct to Caltrans in the amount of $2,617,813.

The FY 2016/17 ICAP audit was done in conjunction with the incurred cost audit of SCAG. Please refer to the Incurred Cost Audit report (P1580-0022) for further findings related to deficiencies in labor charging practices, procurement, and contract management.

Please provide our office with a corrective action plan addressing the recommendations in the report, including timelines, by March 11, 2019.

If you have questions or need additional information, contact MarSue Morrill, Chief, Planning and Modal Office, at (916) 323-7105.

c: Darin Chidsey, Acting Executive Director, Southern California Association of Governments
Debbie Dillon, Deputy Executive Director, Administration, Southern California Association of Governments
Basil Panas, Chief Financial Officer, Southern California Association of Governments
Rodney Whitfield, Director of Financial Services, Federal Highway Administration
Tashia Clemons, Director, Planning and Environment, Federal Highway Administration
Veneshia Smith, Financial Manager, Federal Highway Administration
John Bulinski, Director, District 7, Caltrans
Steve Novotny, District Local Assistance Engineer, District 7, Caltrans
Eraina Ortega, Inspector General, Independent Office of Audits and Investigations, Caltrans
William E. Lewis, Assistant Director, Independent Office of Audits and Investigations, Caltrans
MarSue Morrill, Chief, External Audits-Local Governments, Independent Office of Audits and Investigations, Caltrans
Erin Thompson, Chief, Regional Planning, Division of Transportation Planning, Caltrans
Rihui Zhang, Chief, Division of Local Assistance, Caltrans
Kamal Sah, Chief, Office of Guidance and Oversight, Division of Local Assistance, Caltrans
Daniel Burke, Civil Rights Program Manager, Division of Local Assistance, Caltrans
Paula Bersola, Audit Liaison, Division of Local Assistance, Caltrans
Gilbert Petrissans, Chief, Division of Accounting, Caltrans
Lisa Gore, Associate Accounting Analyst, Division of Accounting, Caltrans

Southern California Association of Governments
Indirect Cost Allocation Plan Audit

Audit Report

January 2019

Caltrans

Prepared By:

California Department of Transportation
Independent Office of Audits and Investigations – MS 2
Post Office Box 942874
Sacramento, California 94274-0001
ig.dot.ca.gov

Audit Team

MarSue Morrill, Chief, Planning and Modal Office
Teresa Greisen, Audit Manager
Carvin Seals Jr., Auditor in Charge
Vincent Miranda, Auditor

P1580-0023

TABLE OF CONTENTS

SUMMARY, OBJECTIVES, SCOPE, METHODOLOGY, BACKGROUND, AND CONCLUSION

SUMMARY

The Independent Office of Audits and Investigations (IOAI), California Department of Transportation (Caltrans), audited the Southern California Association of Governments' (SCAG) Indirect Cost Allocation Plan (ICAP) for fiscal year (FY) 2016/17. We found that SCAG's procurement practices and charging practices were not in compliance with state and federal regulations and SCAG's policies and procedures. The noncompliant practices resulted in unallowable costs billed direct to Caltrans in the amount of $2,617,813. Additionally, the noncompliant charging practices impacted the allowability of SCAG's proposed ICAP rate that was accepted by IOAI on October 26, 2016. The audited ICAP rate for FY 2016/17 is 83.71 percent of total direct salaries and wages, plus fringe benefits. The audited rate is a final rate based on actual costs for FY 2016/17, therefore, there is no carryforward adjustments to future periods.

OBJECTIVES

The audit was performed to determine whether SCAG's FY 2016/17 ICAP was presented in accordance with 2 Code of Federal Regulations (CFR) Part 200 and Caltrans' Local Assistance Procedure Manual (LAPM) Chapter 5. It was also performed to determine whether SCAG had a financial management system, which includes procurement and contract management, capable of accumulating and segregating costs that are reasonable, allowable, and can be allocated to projects in compliance with Caltrans agreement requirements and state and federal regulations.

SCOPE

The scope of the audit was limited to select financial and compliance activities. The audit included interviews of SCAG staff necessary to obtain an understanding of SCAG's financial management system and reviews of SCAG's policies and procedures. It also included tests of select accounts to the general ledger and supporting documentation to assess allowability, allocability, and reasonableness of costs based on a risk assessment. It also included an assessment of the internal control system as related to the ICAP for the carry-forward year 2014/15. Additionally, the audit included review and tests of transactions related to costs incurred and billed to Caltrans in FY 2014/15 to evaluate compliance with Title 2 CFR Part 200, Title 48 CFR Chapter 1 Part 31, Title 49 CFR Part 18, California Public Contract Code, Caltrans' LAPM, and requirements stipulated in the SCAG's agreements with Caltrans. The audit field work was completed on April 30, 2018. Financial management system changes and transactions occurring subsequent to this date were not tested and, accordingly, our conclusion does not pertain to changes arising after this date. We believe that our audit provides a reasonable basis for our conclusion.

SCAG's management is responsible for the fair presentation of the ICAP and for ensuring costs incurred and billed to Caltrans are in compliance with applicable agreement provisions, and state

and federal regulations. Further, SCAG is responsible for ensuring the adequacy of their financial management system.

Because of inherent limitations in any financial management system, misstatements due to error or fraud may occur and not be detected. Also, projections of any evaluation of the financial management system to future periods are subject to the risk that the financial management system may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

METHODOLOGY

IOAI conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that IOAI 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. IOAI believes that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The audit was less in scope than an audit performed for the purpose of expressing an opinion on the financial statements of SCAG. Therefore, IOAI did not audit and is not expressing an opinion on SCAG's financial statements.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the data and records selected. An audit also includes assessing the accounting principles used and significant estimates made by SCAG, as well as evaluating the overall presentation of the ICAP.

The accompanying ICAP was prepared on a basis of accounting practices prescribed in Title 2 CFR Part 200, and the Caltrans' LAPM Chapter 5, and is not intended to present the results of operations of SCAG in conformity with generally accepted accounting principles.

CONCLUSION

Based on audit work performed, we found that SCAG's procurement practices and charging practices (related to properly segregating direct and indirect costs) were not in compliance with state and federal regulations and SCAG's own policies and procedures. The noncompliant practices resulted in unallowable costs billed direct to Caltrans in the amount of $2,617,813.

Additionally, the noncompliant charging practices affected the allowability of costs included in the FY 2014/15 carryforward and FY 2016/17 actual costs. This resulted in the accepted FY 2016/17 ICAP rate of 79.54 percent to be noncompliant with 2 CFR 200 and LAPM Chapter 5.

At the request of IOAI, SCAG recalculated the FY 2016/17 ICAP using actual costs to report a final rate. The audited rate includes an adjustment to the carryforward and the FY 2016/17 actual costs to account for unallowable costs identified during the audit. The audited rate is 83.71 percent of total direct salaries and wages, plus fringe benefits (see calculation of the audited rate below). The audited rate is a final rate based on actual costs for FY 2016/17, therefore, there is no carryforward adjustment to future periods.

	Actuals FY 2016/17	
Beginning Carryforward (2014/15)	$(515,166)	
Indirect Costs	$12,516,900	
Total Indirect Costs	$12,001,825	(a)
Salaries & Fringe Benefits	$14,336,804	(b)
Audited Rate	**83.71%**	(a)/(b)

The findings in this report detail the unallowable costs identified in the carryforward year of FY 2014/15 that required adjustment to both the FY 2014/15 and FY 2016/17 actual costs.

The FY 2016/17 ICAP audit was done in conjunction with the incurred cost audit performed of SCAG. Please refer to the Incurred Cost Audit report (P1580-0022) for further findings related to deficiencies in labor charging practices, procurement, and contract management.

VIEWS OF RESPONSIBLE OFFICIALS

Our findings and recommendations considered SCAG's response dated October 24, 2018, to our September 6, 2018, draft report. Our findings and recommendations, SCAG's response, and our analysis of the response are set forth in the Findings and Recommendations section of this report. A copy of the SCAG's full written response is included as Attachment V.

This report is a matter of public record and will be placed on IOAI's website which can be viewed at: ig.dot.ca.gov.

If you have any questions, please contact Carvin Seals Jr., Auditor, at (916) 323-7965, or Teresa Greisen, Audit Manager at (916) 323-7910.

MarSue Morrill

MARSUE MORRILL, CPA
Chief
Planning and Modal Office
Independent Office of Audits and Investigations
January 9, 2019

FINDINGS AND RECOMMENDATIONS

FINDING 1 – Improper Procurement Practices

SCAG's procurement practices for ten IT consultant procurements tested did not support that fair and open competition was performed, or that proper procurement procedures were followed as required by Caltrans agreement provisions, state and federal procurement requirements, and SCAG's policies and procedures. The noncompliant procurement practices resulted in unallowable costs billed direct to Caltrans in the amount of $627,179 and unallowable indirect costs included in the FY 2014/15 actual indirect cost pool in the amount of $164,628. Specifically, we noted the following deficiencies:

1. SCAG did not comply with the Department of General Services Master Services Agreement (MSA) requirements to procure nine of the ten IT consultants. Specifically, SCAG did not maintain support or evidence that:
    a) Solicitations for a minimum of three offers or documentation of a minimum of three responses were received from IT consultants on six out of ten procurements tested.
    b) An evaluation was performed of the contractors' Scope of Work responses to the Request for Offers (RFO) and rationale for selection on all ten tested.
    c) Verification of the contractors' certifications or resumes was performed on all ten tested.
2. SCAG entered into a contract with an IT consultant (Acro Service Corporation) with no documentation to support that a competitive procurement process was performed. Costs totaling $57,596 are deemed unallowable.
3. SCAG amended nine of the IT consultant contracts 41 times, in excess of the original contract value (doubling to more than quadrupling the original contract value).
4. SCAG amended six out of the ten contracts after the contracts were expired. Costs incurred on two of the six were included in the FY 14/15 indirect cost pool ($107,032). In addition, costs totaling $627,179 on all six contracts were charged direct to several projects/work elements. These costs are disallowed.
5. SCAG did not obtain the required Regional Council approval on 23 contract amendments that exceeded either 30 percent of the original contract amount or $75,000.
6. SCAG entered into one IT consultant contract with a contract term in excess of 36 months and amended three IT consultant contracts beyond a 36-month period without re-soliciting contracts.
7. SCAG did not document the specific circumstance for increasing the contract value over $50,000 on 14 out of 41 amendments tested.

See Attachment I for detailed criteria.

See Attachment II for a summary of the IT consultant contracts tested.

The FY 2014/15 actual indirect cost pool will be adjusted by $164,628 in unallowable indirect consultant costs.

RECOMMENDATION

We recommend SCAG:

- Reimburse Caltrans $627,179 for the disallowed IT consultant contract costs identified above.
- Adjust the FY 2014/15 actual indirect cost pool by $164,628 ($57,596 + $107,032) for the unallowable IT consultant costs identified above.
- Determine the amount incurred and included in the FY 2016/17 indirect cost pool for the seven unallowable IT consultant contracts and adjust the FY 2016/17 indirect cost pool accordingly.
- Ensure costs that are not in compliance with the state and federal procurement regulations are excluded from the indirect cost pool.
- Revise SCAG's Procurement Policy & Procedures Manual to ensure they are current and comply with all applicable state and federal regulations.
- Ensure management and staff receive proper training in procurement procedures.
- Ensure all documentation is maintained to support that proper procurement procedures are followed in accordance with state and federal regulations.
- Take Caltrans, Division of Local Assistance (DLA), A&E consultant procurement training either in person or online at http://www.dot.ca.gov/hq/LocalPrograms/training.html

SUMMARY OF AUDITEE'S RESPONSE

Finding 1.1a and b - SCAG agrees their procurement documentation procedures and practices require improvement and indicated they have implemented a new Finance Database System that tracks their procurements.

Finding 1.1c - SCAG pointed out that the Department of General Services qualified each vendor on the list of selected candidates form. The essential part of their review process was to determine if a candidate was qualified to perform our scope of work. This effectively verified their resume.

Finding 1.2 - SCAG agrees they should have done a better job at documenting that they checked to ensure they were using a valid competitive procurement and that Contracts staff did check websites used by Maricopa County.

Finding 1.3 and 1.5 - SCAG indicates their Board authorized staff to annually fund the IT contracts for the life of each project up to a combined maximum of $940,000 each year. Given that approval, staff did not exceed Board-approved annual thresholds.

Finding 1.4 - SCAG makes note there were practical difficulties with meeting the amendment deadlines and SCAG relied on the retroactive language in the amendments. While this type of language is legally binding and commonly used in commercial contracts, SCAG now understands that the practice is not in compliance with state and federal requirements.

Finding 1.6 - SCAG stated that the 36-month rule was self-imposed in a version of their Procurement Manual prior to December of 2016 and proved to be impractical in cases such as this and thus revised the requirement.

Finding 1.7 - SCAG requests Caltrans to provide a citation as to what guidance is at issue so that they can respond or they can request Caltrans to remove this finding.

See Attachment V for SCAG's full response.

ANALYSIS OF AUDITEE'S RESPONSE

Finding 1.1 a and b - We appreciate SCAG's efforts to improve their processes. Any process changes subsequent to our fieldwork have not been reviewed or tested.

Finding 1.1c - Reviewing resumes does not support a competitive procurement. The list of vendors per the Department of General Services is to allow agencies to solicit consultants from the list and procure the consultants in accordance with state and federal procurement requirements.

Finding 1.2 – Staff checking several websites to ensure SCAG was using a valid competitive procurement does not address the finding. The finding was a lack of documentation to support competitive procurement.

Finding 1.3 and 1.5 – SCAG did request approval from their Board, however, the June 6, 2013, Board Report does not state for the "life of each project."

The June 6, 2013, Board Report states, "*For the budgeted FY14 IT work plan, staff seeks approval to enter into multiple contracts under this MSA up to a combined maximum of $940,000." It also states, "To meet dynamic resource needs, staff desires to use a State of California Master Service Agreement (MSA) that was competitively procured and established for this specific purpose, i.e. to obtain IT resources from qualified, pre-approved vendors. As the IT workload varies from year to year, staff requests the Regional Council's approval on an annual basis. For FY 2013-2014, staff seeks authorization to enter into IT contracts up to a combined maximum of $940,000.*"

Finding 1.7 - SCAG requested IOAI to provide a citation as to what guidance is at issue. SCAG's Procurement Policies & Procedures Section 8.3 (f) states, "*Note – Amendments may increase the contract's or PO's value over the informal procurement threshold ($50,000). However, this should be rare and the procurement file must document the specific circumstances. Such amendments must still be processed in accordance with this Policy Manual.*" There was no documentation for the specific circumstances for increasing the contract amount in excess of $50,000 on 14 amendments.

Based on the analysis of the responses, the finding remains as written.

FINDING 2 – Deficient Charging Practices

SCAG's charging practices related to billing indirect and direct costs to Caltrans were deficient and resulted in billings that were not in compliance with Caltrans agreement provisions and state and federal regulations. Specifically, SCAG billed an indirect rate for FY 2016/17 that included unallowable direct and indirect costs and billed indirect and ineligible direct labor costs to a direct project/work element. The charging practices implemented by SCAG did not ensure the proper segregation of direct, indirect, and unallowable costs in the accounting records and costs included on the billings to Caltrans. We identified the following unallowable costs that resulted from deficient charging practices:

Finding 2A - Unallowable Indirect Costs Included in the FY 2016/17 ICAP

In our testing of 41 transactions within 15 indirect cost accounts for the FY 2014/15 carryforward we found that SCAG included direct, unallowable, and unsupported costs in the indirect cost pool. Unallowable costs totaling $196,617 were due to weak internal controls, improper charging practices, and non-compliant vendor procurements. Specifically, we found the following:

Legal Services Account – SCAG did not treat costs consistently. SCAG included $82,494 of legal expenses from two vendors in the indirect cost pool that were direct legal expenses related to projects or other final cost objectives of SCAG. The legal costs for PC Law ($57,495) are unallowable as the costs included direct and indirect costs that were not properly segregated. SCAG miscoded costs on one invoice as indirect instead of direct for Nossaman LLP ($24,999).

Memberships – SCAG included $49,875 of membership costs from four vendors in the indirect cost pool that appeared to be related to lobbying or were not supported by proper documentation. The costs paid to California Contract Cities Association ($2,500) and National Association of the Regional Council ($30,000) are unallowable as the entities perform lobbying activities for members, and the invoices did not identify and segregate the lobbying costs. The invoices from Mobility Advancement Group ($12,500) and Coalition for America's Gateway & Trade Corridors ($4,875) did not properly support the costs charged to FY 2014/15.

Computer Maintenance – SCAG included $19,356 of computer maintenance costs from the consultant Granicus, Inc. that are unallowable as SCAG could not support that a competitive procurement was performed. SCAG used the City of San Jose's procurement of the consultant to contract with Granicus, Inc. and did not solicit their own bids for the work and did not maintain documentation supporting that a proper procurement was performed.

Travel – SCAG included $44,892 ($16,007 + $9,942 + 18,943) of unallowable travel costs in the indirect cost pool related to commute mileage, travel mileage, and other travel expenses of the SCAG Executive Director.

- Our testing of travel expense claims (TECs) during our audit period found unallowable reimbursement of mileage costs to the Executive Director for the use of his personal vehicle and travel expenses that were not supported. Per the Executive Director's employment agreement, a monthly car allowance of $1,035 was provided to cover all expenses related to

the employee's use of his personal vehicle for SCAG business related travel. As the car allowance provided compensation for the mileage related to business travel and the monthly car allowance was included in the fringe benefit costs billed to Caltrans, all mileage costs included on the Executive Director's TECs are unallowable as the cost was reimbursed through the fringe benefit rate. The unallowable mileage costs for FY 2014/15 totaled $16,007 and will be removed from the indirect cost pool.

- We also found on the TECs tested that the purpose was not identified, and there was no other documentation to support that the Executive Director's travel was for an allowable business related purpose. State travel regulations and SCAG's travel policies and procedures require that the purpose of the travel be documented on the TEC to support and ensure all travel is for allowable business purposes. The unsupported travel costs totaled $9,942.

- As part of our audit, we followed up on prior audit work performed and determined that SCAG did not adjust prior ICAPs for the Executive Director's reimbursement of commute mileage costs that were identified in a SCAG Internal Audit Report dated March 11, 2014. The report covered the period of July 2012 through June 2013. Commute mileage costs are unallowable. As SCAG did not adjust prior FY ICAP's for the commute costs of $18,943, the FY 2014/15 indirect cost pool will be adjusted.

- We also identified an internal weakness in the approval process of the Executive Director's TECs. We found that the Chief Financial Officer (CFO) and the Internal Auditor approved the TECs of the Executive Director that lacked supporting documentation. The CFO and internal auditor are subordinate to the Executive Director and should not be approving his TECs. Additionally, the internal auditor's independence is jeopardized when approving the Executive Director's TECs.

We noted from reports obtained from SCAG that the Executive Director was reimbursed unallowable mileage costs in the amount of $11,986 for FY 2016/17 that should be removed from the indirect cost pool of the FY 2016/17 ICAP.

See Attachment I for detailed criteria.

See Attachment III for summary of total unallowable indirect costs.

RECOMMENDATION

We recommend SCAG:

- Adjust the FY 2014/15 actual indirect cost pool by $196,617 ($82,494 + $49,875 + $19,356 + $44,892) for the unallowable costs identified above.
- Remove $11,986 from the indirect cost pool for FY 2016/17 for the unallowable travel costs identified above.
- Review all indirect accounts to ensure costs are in compliance with state and federal regulations; are properly segregated between direct, indirect and unallowable; and are supported by original source documentation.

- Adjust the FY 2016/17 indirect cost pool by all unallowable costs identified.
- Establish written policies and procedures for segregating direct and indirect legal costs in compliance with state and federal regulations.
- Establish written policies and procedures that prevent the Internal Auditor from reviewing and approving travel expense.
- Ensure staff provide adequate documentation supporting any and all travel expenses and comply with SCAG travel policies and procedures and Caltrans Agreement provisions related to travel. Also, report to the board monthly of all travel related expenses incurred by the Executive Director.

SUMMARY OF AUDITEE'S RESPONSE

Finding 2A

Legal Services - SCAG concurs with this finding with the exception of the RCS Investigations & Consulting LLC ($3,592). The firm was hired to perform an investigation into an employee complaint which is an allowable indirect cost as an element of an organization's human resource program.

Memberships - SCAG disagrees with the disallowance of membership dues associated to National Association of Regional Council (NARC). SCAG contends the NARC membership dues consists of two components and the invoice delineates $15,000 for Calendar Year Membership Dues and Transportation Dues of $15,000. Transportation Dues are not related to lobbying.

Computer Maintenance - SCAG concurs.

Travel - SCAG stated that it as the intent of the Board for the car allowance to cover expenses such as insurance, tolls, parking, and depreciation in addition to mileage reimbursement. Therefore, the reimbursement is not a double billing. SCAG additionally states that the contract language left the mileage issue open to interpretation and has clarified the issue in in the Executive Director's most recent contract.

ANALYSIS OF AUDITEE'S RESPONSE

Legal Services - Based on the analysis of the response regarding the legal costs for RCS Investigation & Consulting LLC that was hired to perform an investigation into an employee complaint that relates to the organization's human resource program, $3,592 for RCS Investigation & Consulting LLC costs have been removed from the finding.

Memberships - The National Association of Regional Council's website states, "Its primary mission is to assist Regional Councils and Metropolitan Planning Organizations (MPOs) to better serve their member local governments – and their regions – more effectively. NARC represents and advocates for and provides services to its member councils of government and metropolitan planning organizations." National Association of Regional Council's website is clear that it provides various services that includes lobbying. The invoice tested during the audit did not

specify what percentage of the dues related to lobbying related activities versus not lobbying related activities and SCAG did not provide support to dispute the finding.

Travel – Based on our review of, the Executive Director employment contract seeking additional reimbursement through travel expense claims for mileage and including the monthly car allowance as part of SCAG's fringe benefit calculation compensates SCAG twice for the same cost.

Based on the analysis of the responses, the finding remains as written except for the removal of the finding relating to RCS Investigation & Consulting LLC invoice.

Finding 2B – Unallowable Labor Costs

The Incurred Cost Audit (dated July 24, 2018) identified indirect and ineligible costs charged to Work Element 120 which was established for direct costs related to development and administration of the Overall Work Program. This will impact the FY 2016/17 ICAP. Eligible tasks included the development of the Overall Work Program, preparation of the annual budget and amendments to the budget, and preparation of Quarterly Progress Reports. In our incurred cost audit, we found that SCAG accountants and contract administrators charged time for the review and approval of consultant invoices which were inelegible and indirect in nature. SCAG's charging practices remained unchanged for FY 2016/17 and unallowable costs were billed to Work Element 120. Based on an analysis of SCAG's labor reports for FY 2016/17, $1,625,797 of indirect labor related to accountants, contract administrators, and an internal auditor were inappropriately charged direct to Work Element 120. See Attachment IV for a summary of the unallowable direct labor costs.

SCAG does not have adequate policies and procedures related to labor charging practices. In addition to billing ineligible costs identified, the inappropriate charging practices result in SCAG lacking accurate historical information related to actual costs for future budget purposes and overhead rate calculations.

See Attachment I for detailed criteria.

RECOMMENDATION

We recommend SCAG:

- Reimburse Caltrans $1,625,797 in unallowable labor costs.
- Ensure billings to Caltrans are based on actual labor costs incurred.
- Develop and implement written policies and procedures for proper and consistent labor charging practices. Ensure procedures define appropriate charging practices for staff meetings and other non-project or work element activities.

AUDITEE'S RESPONSE

The practice of charging time to WE 120 other than that of Budget & Grants staff was begun many years ago after consultation with District 7. Since the practice is no longer permissible, SCAG's

FY18 actuals and FY19 budget will charge those hours to the Indirect Cost budget. SCAG requests that the costs disallowed from WE 120 in FY15 be charged to the Indirect Cost budget in that year.

ANALYSIS OF AUDITEE'S RESPONSE

As SCAG has already been reimbursed directly for the finding amount, SCAG will need to repay Caltrans the full $1,625,797 as indicated in the finding. Once SCAG repays the disallowed costs, they can make a request to Caltrans Division of Transportation Planning and DLA to include the disallowed costs in the FY 2016/17 indirect cost pool. If the request is approved, SCAG will then be required to resubmit a revised FY 2016-17 ICAP to IOAI that includes the adjustments for review and approval prior to seeking reimbursement for any variance in the rate.

Based on the analysis of the response, the finding remains as written.

ATTACHMENT I
AUDIT CRITERIA

Finding 1 (Improper Procurement Practices)

1a. California Public Contract Code §10340 (a) states, in part, "State agencies shall secure at least three competitive bids or proposals for each contract."

1b. User Instruction for MSA 57175 specifies the ordering department's responsibilities as following:

- Solicitation of a minimum of three (3) offers and document responses;
- Evaluation of the contractors' Statement of Work (SOW) response(s) to the RFO and rationale for selection;
- Verification of contractor's certifications and resumes as defined on the SOW;

1c. 49 CFR Part 18.36 and 2 CFR 200.319 (a) states in part, "All procurement transactions must be conducted in a manner providing full and open competition consistent with the standards of this section. In order to ensure objective contractor performance and eliminate unfair competitive advantage, contractors that develop or draft specifications, requirements, statements of work, or invitations for bids or requests for proposals must be excluded from competing for such procurements…."

1d. State Contracting Manual 5.81 states in part, "Competitive bidding requirements and exemptions should be evaluated when contemplating an amendment (PCC 10355). A.1.b, the amendment does one, but not both, of the following and there is no change is the scope of work, i., adds time only to complete performance, not to exceed one year…**or** ii., the amendment adds not more than 30%) not to exceed $250,000) of the original contract…."

1e. Caltrans LAPM Chapter 10.8 states in part, "A consultant contract may be amended at any time. The most common amendment is to extend the ending date of the contract. All contract amendments must be fully executed before the ending date of the contract."

1f. SCAG's Procurement Policy and Procedures Manual:

a. 8.3.1 K. states, "Once the term of the contract has expired, no further amendments can be made (i.e., an amendment must be fully executed before the ending date of the contract)"
b. 3.5 states, in part, "while contract amendments are limited to no more than thirty (3) percent of the original total amount of the contract, any amendment(s) with an individual or aggregate amount of $75,000 or greater requires Regional Council Approval."
c. 7.11 states, "Consistent with the State of California Contract Manual, Section 7.8, each consultant agreement should be re-solicited after a total of thirty-six (36) months consecutive with the same consultant (including any amendment to extend the contract's term), unless Caltrans or the Federal government gives SCAG statutory authority or a written exemption."

1g. 8.3.1 F. states, in part, "Amendment may increase the contract's or PO's value over the informal procurement threshold. ($50,000) However, this should be rare and the procurement file must document the specific circumstance."

1h. Public Contract Code Part 2, Chapter 2, Article 4, Section 10371 (c) states, "Each state agency shall, prior to signing a consulting services contract totaling five thousand dollars ($5,000) or more, prepare detailed criteria and a mandatory progress schedule for the performance of the contract and shall require each selected contractor to provide a detailed analysis of the costs of performing the contract."

1i. Caltrans LAPM Chapter 10.8 states, in part, "Contract amendments are required to modify the terms of the original agreement for changes such as extra time, added work, or increased costs."

Finding 2 (Deficient Charging Practices)
2A (Unallowable Indirect Costs included in the FY 2016/17 ICAP)

2a. 2 CFR Part 200.413 (a) states, "Costs incurred for the same purpose in like circumstances must be treated consistently as either direct or indirect (F&A) costs."

2b. 2 CFR 200.403 (d) states, "Costs must meet the following general criteria in order to be allowable under federal awards: be accorded consistent treatment. A cost may not be assigned to a federal award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the Federal award as an indirect cost."

2c. 2 CFR 200.450 (a) states, "Lobbying. The cost of certain influencing activities associated with obtaining grants, contracts, cooperative agreements, or loans is an unallowable cost."

2d. 49 CFR Part 18.36 and 2 CFR 200.319 (a) states, in part, "All procurement transactions must be conducted in a manner providing full and open competition consistent with the standards of this section."

2e. Executive Director's Employment Agreement states, in part, "Subsection (f) Section 3.06 (Employee Benefits) of Article 3 (Obligations of Employer) is hereby amended to read in it's entirely as follows: (f) Employee shall receive an allowance of $1,035 per month to cover the Employee's use of his personal vehicle for SCAG business,...and reasonable travel-related expenses...."

2f. SCAG's Travel Policy Section VI states, in part, "Prior to approving the reimbursement request, the manager or director should review the expenditures..... Travel Expense Reimbursement Form Requirements: (1) dates and times when expenses occurred.... (2) Location of each trip and any additional justification required....."

Finding 2B (Unallowable Labor Costs)

2a. 2 CFR Part 200.404 (c) states, "Any costs allocable to a particular Federal award under the principles provided for in this part may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by Federal statutes, regulations, or terms and conditions of the Federal awards, or for other reasons."

ATTACHMENT II
INDIRECT COST ALLOCATION PLAN AUDIT
OF
SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS

UNALLOWABLE INDIRECT AND DIRECT IT CONSULTANT COSTS

Consultant	Contract Number	Original Contract Amount	Final Contract Amount	Contract Execution Date	Contract Expiration Date	Number of Amendments	Number of Amendments on Expired Contracts	Number of Amendments with no Documentation	Consultant Contracts with Unallowable Costs	Unallowable Amounts in the FY 2014/15 ICAP	Unallowable Costs Billed Direct FY 2014/15 thru 2016/17
AgreeYa Solutions, Inc.	13-034-C1	$ 34,000	$ 243,000	3/12/2013	7/31/2013	6	2	1	X	$ 101,018	-
Allied Network Solutions, Inc.	14-004-C1	$ 124,000	$ 503,000	8/6/2013	6/30/2015	6	3	4	X	-	$ 185,629
Celer Systems, Inc.	15-025-C1	$ 90,000	$ 260,000	2/5/2015	6/30/2015	2	2	1	X	-	-
22nd Century Technologies, Inc.	15-018-C1	$ 75,000	$ 292,110	2/2/2015	6/30/2015	3	2	1	X	-	$ 188,104
22nd Century Technologies, Inc.	15-018-C2	$ 75,000	-	2/5/2015	-	-	N/A	-	-	-	-
Logic House Ltd. Corp.	14-005-C1	$ 170,000	$ 478,896	10/15/2013	6/30/2015	3	2	2	X	-	$ 78,485
Acro Service Corp.	13-017-C1	$ 100,000	$ 373,600	11/15/2012	-	4	N/A	2	1	$ 57,596	-
RADgov, Inc.	13-016-C1	$ 175,000	$ 627,632	9/24/2012	12/19/2013	5	3	3	X	$ 6,014	$ 174,961
AgreeYa Solutions, Inc.	14-021-C1	$ 156,000	$ 255,201	6/3/2014	-	7	N/A	-	-	-	-
Civic Resource Group, LLC	14-021-C1	$ 162,181	$ 204,293	6/5/2015	-	5	N/A	-	-	-	-
TOTAL						41	14	14		$ 164,628	$ 627,179

Note:
1 - Lack of documentation supporting competitive procurement as SCAG piggybacked off of the Arizona County of Maricopa's contract.
X - Amendment on an Expired Contract

ATTACHMENT III
INDIRECT COST ALLOCATION PLAN AUDIT
OF
SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS

TOTAL UNALLOWABLE INDIRECT COSTS

Account Description	Vendor	Unallowable Amounts in the FY 2014/15 ICAP
Consultant	AgreeYa Solutions, Inc.	$101,018
	Acro Services Corp	$57,596
	Radgov, Inc.,	$6,014
		$164,628
Legal Services	PC Law	$57,495
	Nossaman, LLP	$24,999
		$82,494
Equipment Repairs & Maintenance	Granicus, Inc.	$19,356
Memberships	Mobility Advancement Group	$12,500
	Coalition for America's Gateway	$4,875
	California Contract Cities Assoc.	$2,500
	NARC	$30,000
		$49,875
Travel	E.D	$44,892
	TOTAL	$361,245

ATTACHMENT IV
INDIRECT COST ALLOCATION PLAN AUDIT
OF
SOUTHERN CALIFORNIA ASSOCIATION OF GOVERNMENTS

UNALLOWABLE DIRECT LABOR COSTS - FY 2016-17

	A	B	C =AxB	D =A+C	E = D X 79.54%	F =D+E	
	Labor less TDA Labor charged to PL & 5303	Fringe Benfit Percentage	Total Fringe Benefits	Total Labor plus FB	Indirect Costs	Total Disallowed Direct Labor, FB & IC Costs	
Accountants	$ 173,152	78.87%	$ 136,565	$ 309,716	$ 246,348	$ 556,065	
Internal Auditor	$ 37,877	78.87%	$ 29,873	$ 67,750	$ 53,889	$ 121,639	
Contracts Administration	$ 360,815	78.87%	$ 284,575	$ 645,390	$ 513,343	$ 1,158,733	
Totals	$ 571,843		$ 451,013	$ 1,022,856	$ 813,580	$ 1,836,436	(1)
					Federal Reimburement Rate	88.53%	(2)
					Total Disallowed Amount	$ 1,625,797	(3) = 1 X 2

ATTACHMENT V

October 24, 2018

Mr. William E. Lewis, Assistant Director
California Department of Transportation
Independent Office of Audits and Investigations
1304 O Street Suite 200
Sacramento, CA 95814
Sent via email to william.lewis@dot.ca.gov

Subject: SCAG Response to Draft Audit Report of Incurred Cost Audit

Dear Mr. Lewis:

This letter is to officially transmit SCAG's written responses to the draft Indirect Cost Allocation Plan audit report.

First, I want to express my appreciation on behalf of the SCAG staff and Regional Council for the thorough and diligent work effort that your team has put into conducting the Incurred Cost Audit and preparing the draft report.

We all truly appreciate that conducting audits is to ensure that SCAG has sound business practices and is in compliance with Caltrans agreement provisions and state and federal regulations. Which is critically important to carrying out the mission of SCAG, its federal, state and local partners.

As we've discussed, SCAG had not been audited by Caltrans for more than ten years at the inception of this audit. Therefore, we sincerely appreciate the opportunity to take the findings and improve our organization and business practices in a timely manner.

Attached to this letter, SCAG has included its written responses as part of the draft report provided for ease of Caltrans reference. Additionally, SCAG has attached relevant documentation referred to in the responses for ease of reference.

As noted in the responses, SCAG has already begun to implement recommendations and findings that it is in agreement with and will work quickly to implement others after the final disposition of this Audit is confirmed.

Thank you again for the opportunity to work together on this important effort.

Sincerely,

Darin Chidsey, Interim Executive Director

FINDINGS AND RECOMMENDATIONS

FINDING 1 – Improper Procurement Practices

SCAG's procurement practices on the 10 Information Technology (IT) consultant procurements tested did not support that fair and open competition was performed, or that proper procurement procedures were followed as required by Caltrans Agreement provisions, state and federal procurement requirements and SCAG's policies and procedures. The noncompliant procurement practices resulted in unallowable costs billed direct to Caltrans in the amount of $627,179 and unallowable indirect costs to be included in the FY 2014/15 actual indirect cost pool in the amount of $164,628. Based on our review of the 10 IT consultant procurements we noted the following noncompliant actions:

1) SCAG did not comply with the Department of General Services Master Services Agreement (MSA) requirements to procure 9 of the 10 IT consultants. Specifically, SCAG did not maintain support or evidence that:
   a) Solicitations for a minimum of 3 offers or documentation of a minimum of 3 responses were received from IT consultants on 6 out of 9 procurements tested.

   b) An evaluation was performed of the contractors' Scope of Work responses to the Request for Offers (RFO) and rationale for selection on all 9 tested.

   c) Verification of the contractor's certifications or resumes was performed on all 9 tested.

2) SCAG entered into a contract with an IT consultant (Acro Service Corporation) with no documentation to support a competitive procurement process was performed. SCAG stated they relied on the procurement performed by the Maricopa County of Arizona.

3) SCAG amended nine of the IT consultant contracts 41 times, in excess of the original contract value (doubling to more than quadrupling the contracts).

4) SCAG amended 6 out of 10 contracts after the contracts were expired.

5) SCAG did not obtain the required Regional Council approval on twenty-three contract amendments that exceeded either 30 percent of the original contract amount or $75,000.

6) SCAG entered into 1 IT consultant contract with a contract term in excess of 36 months and amended 3 IT consultant contracts beyond a 36 month period without re-soliciting contracts.

7) SCAG did not document the specific circumstance for increasing the contract value over $50,000 on 14 out of 41 amendments.

See Attachment II for a summary of the IT consultant contracts tested. SCAG's procurement actions demonstrate a lack of understanding of state and federal procurement regulations and a lack of proper oversight to ensure staff comply with its own policies and procedures.

Based on our testing of the 10 non-compliant IT consultant procurements, 6 were amended on expired contracts. Costs incurred on all 6 are unallowable. Costs incurred on 2 of the 6 were included in the FY 14/15 indirect cost pool ($107,032) and additional costs on all 6 were charged direct to several projects/work elements (627,179). One of the 10 consultant contracts is unallowable due to a lack of documentation that fair and open competition was achieved ($57,596). The FY 2014/15 actual indirect cost pool will be adjusted by $164,628 in unallowable indirect consultant costs.

See Attachment I finding 1 for detailed criteria.

RECOMMENDATION

We recommend SCAG perform the following:

- Reimburse Caltrans $627,179 in unallowable IT consultant contract costs directly billed.
- Adjust the FY 2014/15 actual indirect cost pool by $164,628 for the unallowable IT consultant costs.
- Determine the amount incurred and included in the FY 2016/17 indirect cost pool for the seven unallowable IT consultant contracts. Adjust the FY 2016/17 indirect cost pool by this amount.
- Ensure costs that are not in compliance with the state and federal procurement regulations are excluded from the indirect cost pool.
- Revise SCAG's Procurement Policy & Procedures Manual to ensure they are current and comply with all applicable state and federal regulations.
- Ensure management and staff receive proper training in procurement procedures
- Ensure all documentation is maintained to support that proper procurement procedures are followed in accordance with state and federal regulations.

AUDITEE'S RESPONSE

Finding 1.1 (a) and (b):

SCAG agrees that our procurement documentation procedures and practices require improvement. As we explained to the auditors, much of the required procurement documentation was inadvertently purged due to a change in our electronic file storage policy. During the course of the audit, we provided the auditors with supplementary evidence and documentation that we believe demonstrates that SCAG competitively procured these contracts in accordance with the Department of General Services Master Service Agreement requirements. (Please see Exhibit 1)

It should also be noted that in a report to our board about these contracts we specifically state, "To gain even greater cost reductions, unlike most MSA, this MSA would require staff to compete

each of the projects among at least 3 of the 120 approved vendors on the MSA." This is an indication that competition was performed.

Further, to help ensure that we maintain proper file documentation we have implemented a new Finance Database System that tracks our procurements, Contracts staff revised its Checklist procedure for processing procurements to clarify how and where documents are to be maintained, and the Contracts Manager reviews the file at five (5) key stages (creation of the solicitation, consultant selection, contract issuance, any amendment and close out) to ensure all required parts of the file are properly stored, are accurate and complete.

Finding 1.1 (c):
We would like to point out that the Department of General Services qualified each vendor to the list we selected candidates from. The essential part of our review process was to determine if a candidate was qualified to perform our scope of work. This effectively verified their resume.

Finding 1.2:

While we agree we should have done a better job at documenting that we checked to insure we were using a valid competitive procurement, Contracts staff did verify this by checking the following websites:

- **https://www.bidsync.com/bidsync-app-web/vendor/links/BidDetail.xhtml?bidid=1903849&roundId=null.**
  This is a link to Bid #11143-RFP - TEMPORARY STAFFING AND RELATED SERVICES issued by Maricopa County which closed on January 19, 2012. This is proof there was a competitive procurement.

- **www.seattle.gov/purchasing/docs/bids/RFP1400.pdf** shows this MSA listed on the U.S. Communities Purchasing Alliance website which is proof it was valid.

This documentation was and still is available at the links shown above.

Finding 1.3:
At the June 6, 2013 SCAG Board meeting, the Board authorized staff to annually fund these contracts for the life of each project up to a combined maximum of typically $940,000 each year. Given that approval, staff did not exceed Board-approved annual thresholds. The majority of the amendments were administrative in nature and all amendments were consistent with Board approval.

Finding 1.4:
There were practical difficulties with meeting the amendment deadlines and SCAG relied on the retroactive language in the amendments. While this type of language is legally binding and commonly used in commercial contracts, we now understand that the practice is not in compliance with state and federal requirements. SCAG has developed a more effective way to process amendments and notify executive management of potential bottlenecks in processing amendments through the implementation on of its Finance Database System,

Finding 1.5:
At the June 6, 2013 SCAG Board meeting, the Board authorized staff to annually fund these contracts for the life of each project up to a combined maximum of typically $940,000 each year. We did not exceed this threshold.

Finding 1.6:
The 36-month rule was self-imposed in a version of our Procurement Manual prior to December of 2016 and proved to be impractical in some cases, this being one. In the December 2016 Procurement Manual we include a more effective procedure to extend a contract beyond 36-months (i.e., the SCAG project manager must provide written justification for the extension to the Chief Financial Officer for approval).

Finding 1.7:
SCAG requests Caltrans to provide a citation as to what guidance is at issue so that we can respond or we request Caltrans to remove this finding.

ANAYLSIS OF AUDITEE'S RESPONSE

FINDING 2 – Deficient Charging Practices

SCAG's charging practices related to billing indirect and direct costs to Caltrans were deficient and resulted in billings that were not in compliance with Caltrans Agreement provisions and state and federal regulations. Specifically, SCAG billed an indirect rate for FY 2016/17 that included unallowable direct and indirect costs and billed indirect and ineligible labor costs as direct to a direct project/work element. SCAG is responsible for developing and implementing charging practices that ensure compliance with state and federal regulations when state and federal funds are expended. The charging practices implemented by SCAG did not ensure the proper segregation of direct, indirect and unallowable costs in the accounting records and costs included on the billings to Caltrans. We identified the following unallowable costs that resulted from deficient charging practices:

Finding 2A - Unallowable Indirect Costs included in the FY 2016/17 ICAP

SCAG included costs in the indirect cost pool of the FY 2014/15 carryforward that were not in compliance with Caltrans ICAP Submission requirements, and state and federal regulations. The 2 CFR 200 requires that unallowable costs be segregated and excluded from the indirect cost pool. Our testing of 41 transactions within 15 indirect cost accounts found that SCAG included direct, unallowable and unsupported costs in the indirect cost pool. Unallowable costs of $200,209 were due to weak internal controls, improper charging practices and non-compliant vendor procurements. Specifically, we found the following:

Legal Services Account - SCAG included $86,086 of legal expenses from 3 vendors in the indirect cost pool that were direct legal expenses related to projects or other final cost objectives of SCAG. The legal costs for PC Law ($57,495) are unallowable as the costs included direct and indirect

costs that were not properly segregated. SCAG miscoded costs on 2 invoices as indirect instead of direct for RCS Investigations & Consulting LLC ($3,592) and Nossaman LLP ($24,999).

Memberships – SCAG included $49,875 of membership costs from 4 vendors in the indirect cost pool that were related to lobbying or not supported by proper documentation. The costs paid to California Contract Cities Association ($2,500) and National Association of the Regional Council ($30,000) are unallowable as the entities perform lobbying activities for members and the invoices did not identify and segregate the lobbying costs. The invoices from Mobility Advancement Group ($12,500) and Coalition for America's Gateway & Trade Corridors ($4,875) did not properly support the costs charged to FY 2014/15.

Computer Maintenance – SCAG included $19,356 of computer maintenance costs from the consultant Granicus, Inc. that are unallowable as SCAG could not support that a competitive procurement was performed. SCAG used the City of San Jose's procurement of the consultant to contract with Granicus, Inc., and did not solicit their own bids for the work or maintain documentation supporting a proper procurement was performed.

Travel – SCAG included $44,892 of unallowable travel costs in the indirect cost pool related to commute mileage, travel mileage and other travel expenses of the SCAG Executive Director.

Our testing of travel expense claims (TECs) during our audit period found unallowable reimbursement of mileage costs to the Executive Director for the use of his personal vehicle and travel expenses that were not supported. Per the Executive Director's employment agreement, a monthly car allowance of $1,035 was provided to cover all expenses related to the employees' use of his personal vehicle for SCAG business related travel. As the car allowance provided compensation for the mileage related to business travel and the monthly car allowance was included in the fringe benefit costs billed to Caltrans, all mileage costs included on the Executive Director's TECs are unallowable as the reimbursement was a double billing. The unallowable mileage costs for FY 2014/15 total $16,007 and will be removed from the indirect cost pool.

We also found on the TEC's tested, the purpose was not identified and there was no other documentation to support that the Executive Director's travel was for an allowable business related purpose. State travel regulations and SCAG's travel policies and procedures require that the purpose of the travel be documented on the TEC to support and ensure all travel is for allowable business purposes. The unsupported travel costs total $9,942.

As part of our audit, we followed up on prior audit work performed and determined that SCAG did not adjust prior ICAPs for the Executive Director's reimbursement of commute mileage costs that were identified in a SCAG Internal Audit Report dated March 11, 2014. The report covered the period of July 2012 through June 2013. Commute mileage costs are unallowable. As SCAG did not adjust prior FY ICAP's for the commute costs of $18,942, the FY 2014/15 indirect cost pool will be adjusted.

We also identified an internal weakness exists in the approval process of the Executive Director's TECs. We found that the Chief Financial Officer (CFO) and the Internal Auditor approved the TEC's of the Executive Director. The CFO and internal auditor are subordinate to the Executive

Director and should not be approving his TEC's. Additionally, the internal auditor's independence is jeopardized when he is required to approve the Executive Director's TECs.

Federal cost principles as noted in Attachment I, require that unallowable costs be segregated and excluded from the indirect cost pool. The FY 2014/15 indirect cost pool will be adjusted by the total unallowable costs identified in the audit. See Attachment III for summary of unallowable costs.

We noted from reports obtained from SCAG, that the Executive Director was reimbursed unallowable mileage costs in the amount of $11,986 for FY 2016/17 that should be removed from the indirect cost pool of the FY 2016/17 ICAP.

See Attachment I finding 2A for detailed criteria.

RECOMMENDATION

We recommend SCAG do the following:

- Adjust the FY 2014/15 actual indirect cost pool by $200,209 for the unallowable the unallowable costs identified above.
- Determine the amount incurred and included in the FY 2016/17 indirect cost pool for the unallowable Granicus consultant contract and travel costs related to the Executive Director (audit noted $11,986).
- Review all indirect accounts to ensure costs are in compliance with state and federal regulations; are properly segregated between direct, indirect and unallowable; and are supported by original source documentation.
- Adjust the FY 2016/17 indirect cost pool by all unallowable costs identified.
- Establish written policies and procedures for segregating direct and indirect legal costs in compliance with state and federal regulations.
- Establish written policies and procedures that prevent the Internal Auditor from reviewing and approving travel expense forms as a conflict exists when that position also performs audits of SCAG's TECs.
- Ensure staff provide adequate documentation supporting any and all travel expenses and comply with SCAG travel policies and procedures and Caltrans Agreement provisions related to travel.

AUDITEE'S RESPONSE

Finding 2A

Legal Services

We concur with this finding with the exception of the RCS Investigations & Consulting LLC ($3,592). The firm was hired to perform an investigation into an employee complaint which is an allowable indirect cost as an element of an organization's human resource program.

Memberships
The National Association of Regional Council's membership consists of two components. The invoice delineates $15,000 for Calendar Year Membership Dues and Transportation Dues of $15,000. Transportation Dues are not related to lobbying. The NARC website describes its activities in the Transportation arena as follows: The National Association of Regional Councils (NARC) supports Councils of Government (COGs), Metropolitan Planning Organizations (MPOs), and Rural Planning Organizations (RPOs) – large, small, urban, and rural – in transportation planning and programming to promote regional solutions to national transportation needs that support economic growth, environmental sustainability, and enhanced mobility.

Computer Maintenance
We concur with this finding.

Travel
We concur with the travel findings related to documentation of trip purpose in the Executive Director's travel expense claims, the reimbursement of commute mileage and with the finding concerning the approval of the Executive Director's travel expense claims by the Chief Financial Officer and the Internal Auditor. The approval by the Internal Auditor was ended as a result of the Internal Audit Peer Review of 2015.

In regard to the reimbursement of the Executive Director's car expenses, SCAG wants to clarify that it was the intent of the Board to pay the Executive Director a monthly car allowance of $1,035.00 to cover expenses such as insurance, tolls, parking and depreciation in addition to mileage reimbursement. Therefore, the reimbursement of the Executive Director's mileage costs are not a double billing. The basis of this agreement reflects the extensive number of miles the Executive Director was required to drive for business purposes. SCAG acknowledges that the Executive Director's contract language left the mileage issue open to interpretation. This issue was clarified in the Executive Director's most recent contract as follows:

"Employee shall receive an allowance of $2135.00 per month to cover all costs of Employee's use of his personal vehicle for SCAG business including, but not limited to, mileage costs, toll road fees, parking costs, and fuel expenses. This supplemental expense allowance will be paid monthly as part of a non-accountable plan in accordance with applicable regulations of the United States Treasury Department, Internal Revenue Service, and all such payments shall be reported as income."

ANAYLSIS OF AUDITEE'S RESPONSE

Finding 2B – Unallowable Labor Costs

The Incurred Cost Audit (dated July 24, 2018) identified indirect and ineligible costs were charged to work element 120 which was established for direct costs related to Development and Administration of the Overall Work Program (OWP). Eligible tasks included the development of the OWP; preparation of the annual budget and amendments to the budget; and preparation of Quarterly Progress Reports. Our incurred cost audit found that SCAG accountants and contract administrators charged time for the review and approval of consultant invoices which were

inelegible and indirect in nature. SCAG's charging practices remained unchanged for FY 2016/17 and unallowable costs were billed to WE 120. Based on an analysis of SCAG's labor reports for FY 2016/17, $1,625,797 of indirect labor related to accountants, contract administrators and an internal auditor were inappropriately charged direct to WE 120. See Attachment IIIA for a summary of the unallowable direct labor costs.

SCAG does not have adequate policies and procedures related to labor charging practices. In addition to billing ineligible costs identified, the inappropriate charging practices result in SCAG lacking accurate historical information related to actual costs for future budget purposes, and overhead rate calculations.

See Attachment I finding 2B for detailed criteria.

RECOMMENDATION

We recommend SCAG do the following:

- Reimburse Caltrans for $1,625,797 in unallowable labor costs.
- Ensure billings to Caltrans are based on actual labor costs incurred.
- Develop and implement written policies and procedures for proper and consistent labor charging practices. Ensure procedures define appropriate charging practices for staff meetings and other non-project or work element activities.

AUDITEE'S RESPONSE

The practice of charging time to WE 120 other than that of Budget & Grants staff was begun many years ago after consultation with District 7. Since the practice is no longer permissible, SCAG's FY18 actuals and FY19 budget will charge those hours to the Indirect Cost budget. SCAG requests that the costs disallowed from WE 120 in FY15 be charged to the Indirect Cost budget in that year.

ANAYLSIS OF AUDITEE'S RESPONSE

Exhibit 1

As the audit noted, 3 of the 9 files tested (contracts 14-021-C1, 14-021-C2 and 14-005-C1) did contain documentation of a minimum of 3 responses were solicited or received from IT consultants. Further, SCAG submits the following table showing the documents we previously provided to the Caltrans auditors, listed by contract:

SCAG Contract No	Supporting Documentation
15-025-C1	List showing the 3 vendors we contacted, the names of the 11 resumes we received and the 5 candidates that we evaluated and interviewed. The list summarizes the results of the process. We basically were conducting a job interview to select an individual from a vendor to provide as needed Information Technology expertise on various projects. Further, the file named "RFP Response from Spruce Tech" shows the Request for Offer (RFO) and that we solicited as well as received an offer from Spruce Technology. This demonstrates that we solicited and evaluated offers from at least Spruce Technology and Celer Systems, given we selected Celer Systems. Per the RFO (pg. 1, 2nd paragraph, last sentence) our selection was based on Celer Systems' candidate being the most qualified, after what amount to a job interview.
15-018-C2	List showing the 3 vendors we contacted, the names of the 9 resumes we received and the 4 candidates that we interviewed. The list summarizes the results of the process. Further, the file named "FW Interview for the EGIS Consultants and PM Recommendation," demonstrates that we evaluated and interviewed candidates from RadGov and 22nd Century Technologies. Like all the other candidate interviews, our selection was based on 22nd Century Technologies' candidate being the most qualified.
15-018-C1	A list showing the 3 vendors we contacted, the names of the 9 resumes we received and the 4 candidates that we interviewed. The list summarizes the results of the process. Further, a document in the contract file named "FW Interview for the EGIS Consultants and PM Recommendation," demonstrates that we evaluated and interviewed candidates from RadGov and 22nd Century Technologies. Like all the other candidate interviews, our selection was based on 22nd Century Technologies' candidate being the most qualified

SCAG Contract No	Supporting Documentation
14-021-C1	RFO we issued to 9 vendors. Section J1 of the contract file also lists the 9 vendors we contacted as well as the 1 offer we received and evaluated (from Civic Resource Group – in Section G of the contract file). The offer contained sufficient information to make an award and an interview was not held. Section J1 in the contract file states why we selected Civic Resources Group
14-021-C2	RFO we issued to 9 vendors (same list as 14-021-C1). Section J1 of the contract file also lists the 9 vendors we contacted and the 2 offers we received (both in Section G of the contract file). The offers contained sufficient information to make an award (to a different vendor than 14-021-C1) and interviews were not held. Section J1 in the contract file states why we selected AgreeYa Solutions.
14-005-C1.	File named "For Caltrans 9-26-17 Contract 14-005-C1" in the contract file contains documents to support our evaluation and interview of vendors. File section J in the contract file states why we selected Logic House.
14-004-C1	File named "Solicitation e-mail and response from Cambria Solutions" in the contract file shows we solicited an offer from Allied Network Solutions (pg. 1 – also discusses our evaluation of the candidates interviewed and recommends hiring Abhishek Sharma, Allied Network Solutions. This email also shows we solicited an offer from Cambria Solutions (pg. 2 and 3) as well. The 4th pg. shows the RFO. The vendors it was emailed to are blind copied. Like all the other candidate interviews, our selection was based on Allied Network Solutions' candidate being the most qualified.
13-034-C1	File named "SCAG Solicitation and Resume Submission from RadGov", on the bottom of the email thread shows the RFO email (the vendors it was emailed to are blind copied), and RadGov's offer. The contract file also contains a file named "Three Vendor Selected" containing the names of the 3 vendors we solicited (yellow highlighted). Given we selected AgreeYa, our customary practice would be to evaluate at least AgreeYa and RadGov. Further, the contract file contains the following documents to support that we evaluated/interviewed vendors. 1. "Email Regarding Solicitation for Candidates" – to document our intent to solicit offers from 10 vendors; 2 "Web Content editor interview questions-arlg" – to document the interview questions we asked; and 3. "Web content Editor SOW" – to document the project's work scope.

SCAG Contract No	Supporting Documentation
	Like all the other candidate interviews, our selection was based on the AgreeYa Solutions' candidate being the most qualified.
13-030-C1	File named "FW AV Technician - Call for Resumes for SCAG IT Services Division" shows the work scope, and states we emailed the offers to 7 vendors Robert Half, (RHI) AgreeYa, Radgov, Modis, LogicHouse, Acro, and Sierra. The email thread also shows a separate email to RHI. Like all the other candidate interviews, our selection was based on RadGov's candidate being the most qualified.
13-030-C1	File named "Three Vendors Selected" contains the 3 vendors that we evaluated and interviewed. The file also contains a document named "Candidate Solicitation and Vendor Response E-mail" and it shows the 4 resumes we received from RadGov. The file summarizes the results of the process, but not the actual evaluations or interviews. Like all the other candidate interviews, our selection was based on RadGov's candidate being the most qualified

DEPARTMENT OF TRANSPORTATION
OFFICE OF THE DIRECTOR
P.O. BOX 942873, MS-49
SACRAMENTO, CA 94273-0001
PHONE (916) 654-5368
FAX (916) 653-5776
TTY 711
www.dot.ca.gov

Making Conservation a California Way of Life.

May 7, 2019

Mr. Kome Ajise
Executive Director
Southern California Association of Governments
900 Wilshire Blvd, Suite 1700
Los Angeles, CA 90017

Dear Mr. Ajise:

This letter is to notify the Southern California Association of Governments (SCAG) of the California Department of Transportation's (Caltrans) determination of the corrective actions regarding findings identified in the SCAG Incurred Cost Audit, dated September 21, 2018. The audit was performed to determine whether costs claimed by and reimbursed to SCAG were allowable, adequately supported, and in compliance with the Caltrans agreement provisions and federal and State regulations.

Caltrans Final Incurred Cost Audit Report for SCAG examined costs claimed and reimbursed to SCAG totaling $12,458,538 for work performed under Master Agreement 53-6049R relating to the Value Pricing Pilot Program (VPPP-6049(010)) and Federal Overall Work Program Agreement number 74A0822 with Caltrans. The audit period covered April 1, 2014, through June 30, 2015. The audit also included testing of three consultant contracts procured prior to April 1, 2014, with costs incurred through March 30, 2018. Based on the audit, the reimbursed costs totaling $2,510,015 were not in compliance with Caltrans agreement provisions, and federal and State regulations. Specifically, deficiencies were found in labor charges, consultant procurements, contract management, billing and reporting, and SCAG's policies and procedures.

In response to the audit findings, Caltrans Division of Transportation Planning (DOTP) and Division of Local Assistance (DLA) have developed the corrective action plan below. SCAG must develop a plan to implement all corrective actions listed below by June 25, 2019, to ensure the continued allocation and authorization of federal and State transportation funds.

Caltrans Final Incurred Cost Audit Report Corrective Actions:

Finding # 1–Improper Procurement Practices

SCAG did not ensure that fair and open competition was performed or that proper procurement procedures were followed as required by federal and State regulations and the Caltrans agreement provisions. Additionally, SCAG's Procurement Policy and Procedures Manual that

was in effect during the period of procurements tested did not fully comply with federal and State procurement regulations and Caltrans agreement provisions. Specifically, we found the following procurement deficiencies:

Corrective Actions:

SCAG must revise their Procurement Policies and Procedures manual and train staff accordingly, to ensure:

- Compliance with all applicable Caltrans requirements and federal and State procurement regulations. This includes revising Section 6.6.2 to describe the different competitive procurement processes available and when each should be used in compliance with federal and State regulations.
- Proper management decisions are made when preparing Request for Proposals that include tasks or sub-tasks that require an Architectural and Engineering (A&E) consultant to perform the work for compliance with federal and State procurement regulations.
- Management and staff receive proper training in procurement procedures.
- Staff that are involved in the consultant procurement process perform all required actions and comply with SCAG policies and procedures, Caltrans requirements, and federal and State procurement regulations.
- All documentation is maintained to support that proper procedures are followed in accordance with federal and State regulations.
- SCAG must also take the DLA A&E consultant procurement training either in person or online. A training webinar is tentatively scheduled to be posted in late May.
    - If SCAG elects to take the online training, they must provide a list to the DLA Audits Coordinator for those staff who have completed the online training when available. The list shall contain staff names, phone numbers, e-mail addresses, date(s) of completion, and a verification signature by the staffs' supervisor.

SCAG may reference Chapter 10 of the Local Assistance Procedures Manual (LAPM).

Finding # 2–Contract Management Deficiencies

SCAG's contract management system did not comply with federal and State regulations and Caltrans agreement provisions. We found that SCAG billed Caltrans for unsupported and unallowable consultant costs. Furthermore, we found that SCAG improperly managed consultant contracts, did not properly close-out consultant contracts, executed amendments on expired contracts, and could not support that all local match requirements were met. Additionally, SCAG lacked contract management policies and procedures detailing proper processes to manage consultant and sub-recipient contracts and detailed procedures for reviewing and approving invoices. SCAG billed and was reimbursed $590,537 in unsupported consultant costs, and $361,426 on an expired consultant contract. These costs are disallowed.

Corrective Actions:

Please see the following regarding the $951,963 in disallowed costs:

1) DLA will not require reimbursement of the $361,426 disallowed for time extensions incurred after the initial expiration date for the Parsons Brinkerhoff, Inc. contract. Instead, DLA will address this finding with a programmatic solution that will require SCAG to update procurement and contract management procedures (see below), and to take training as prescribed in the corrective actions to Finding 1.
2) SCAG must reimburse Caltrans DLA $338,986 in disallowed costs for the contract with AECOM Technical Services, Inc. The removal of sub-consultants and task 7 (Consensus) at contract execution, and then reinstating Task 7 at an increase of $619,940 over the initial budget bear significant noncompliance to warrant reimbursement of the costs disallowed in the audit.
3) SCAG must reimburse Caltrans DOTP $251,552 of disallowed costs to Caltrans. Caltrans DOTP will coordinate with SCAG on the method and schedule of repayment.

In addition, SCAG must also strengthen procurement and contract management procedures to address the below deficiencies.

- Ensure consultants provide adequate invoice detail to support costs claimed in compliance with consultant contract terms and 2 CFR Part 200 (which superseded 49 CFR Part 18, and 2 CFR Part 225). Additionally, ensure consultants are required to submit invoices that identify the work performed by task/activity and work element so proper documentation is maintained to support consultant billings. Ensure compliance with all federal and State regulations over the administration of consultant contracts.
- Establish procedures that identify and define each staff's roles and responsibilities regarding consultant invoice reviews.
- Revise the Grants Management Policies and Procedures and develop a Project Management Policies and Procedures Manual to ensure compliance with all applicable federal and State regulations and provide staff with detailed processes to follow.
- Ensure consultant contracts identify the funding sources and/or work elements of each task/activity when there are multiple funding sources and/or work elements.
- Ensure compliance with all federal and State regulations over the administration of consultant contracts and that the contracts contain language as required in the Caltrans' agreements.
- Ensure compliance with all federal and State regulations over the administration of sub-recipient (MOU) agreements, that agreements contain language as required in the Caltrans' agreements, and include specific contract end dates.
- Ensure staff are properly trained on the administration and management of consultant and sub-recipient pass through funds.

SCAG may reference Chapter 10 of the LAPM.

Finding # 3–Labor and Fringe Benefit Deficiencies

SCAG's labor and fringe benefit charging practices do not comply with Caltrans Agreement requirements, and federal and State regulations. SCAG does not have adequate policies and procedures related to labor charging practices, no documented procedures to account for time sheet corrections or retroactive pay and merit increases. In addition to billing ineligible costs, the inappropriate charging practices result in SCAG lacking accurate historical information related to actual costs for future budget purposes and overhead rate calculations. SCAG billed and was reimbursed a total of $1,558,051 in ineligible labor charges to Overall Work Program (OWP) work element 120.

Corrective Actions:

SCAG must reimburse the $1,558,051 of disallowed costs to Caltrans DOTP. Caltrans DOTP will coordinate with SCAG on the method and schedule of repayment. After the method of repayment is agreed upon, SCAG may make a request to DOTP to include the disallowed costs in the Fiscal Year (FY) 2014–15 indirect cost allocation pool (ICAP). If the request is approved, SCAG will then need to submit a revised FY 2016–17 ICAP to the Independent Office of Audits and Investigation that includes the adjustments to the carry forward year for review and approval prior to seeking reimbursement for any variance in the rate. Additionally, SCAG must:

- Ensure billings to Caltrans are based on actual labor costs incurred.
- Ensure the accounting methodology for retroactive pay and merit increases provides for an audit trail for changes made to the employee time sheets and costs are allocated to the appropriate pay periods.
- Develop and implement written policies and procedures for proper and consistent labor charging practices. Ensure procedures define appropriate charging practices for staff meetings and other non-project or work element activities.
- Update the Accounting Manual to include procedures for time sheet corrections and retroactive pay and merit increases and train staff accordingly.
- Develop separate fringe benefit allocation methodologies for regular staff, interns, and student assistants.

Finding #4–Billing and Reporting Deficiencies

SCAG did not submit required documentation with their requests for reimbursement to support costs billed and did not submit Quarterly Progress Reports in accordance with the DOTP Master Fund Transfer Agreement and the DLA Master Agreement.

Corrective Actions:

SCAG must revise their billing and reporting procedures to ensure the following:

- Billings to Caltrans include all applicable information and supporting documentation that trace to the billed costs and SCAG's financial management system. This includes ensuring

the Consolidated Planning Grant IT Reports (or equivalent information) are provided and totaled by task associated to the respective work elements that are approved in the current OWP by the Federal Highway Administration (FHWA) and the Federal Transit Administration (FTA).
- Supporting schedules provided with the billings include appropriate descriptions detailing where costs are being charged.

SCAG may reference Chapter 5 of the LAPM for guidance on reviewing consultant invoices for DLA contracts.

Finding #5–Possible Conflict of Interest with Sponsorship Program

SCAG's Sponsorship Program gives the appearance of a possible conflict of interest. SCAG created a Sponsorship Program to solicit donations from individuals, entities, and organizations with an interest in accessing participants of SCAG's General Assembly for networking, relationship building, business opportunities, and information sharing. We noted that SCAG solicits and receives donations from consultants for its Sponsorship Program with whom they also enter into consultant contracts to perform work. SCAG lacks a documented process over the Sponsorship Program to ensure a conflict of interest does not occur. Additionally, SCAG does not have documented policies and procedures over the administration and management of the Sponsorship Program.

Corrective Actions:

In order to avoid the appearance of a possible conflict of interest, SCAG must:

- Establish procedures over the Sponsorship Program to ensure there is no real or appearance of a conflict of interest with consultants that provided donations to the Sponsorship Program and are awarded consultant contracts.
- Develop policies and procedures over the administration and management of the Sponsorship Program to ensure compliance with all federal and State regulations.
- Create a Conflict of Interest Statement Certification form to document compliance with SCAG's own policies and procedures referenced above.

Conclusion:

Please prepare a corrective action plan that outlines the actions SCAG will take to resolve the audit findings and provide it to Erin Thompson, Chief, Office of Regional Planning, and Kamal Sah, Chief, Office of Guidance and Oversight within 60 days of this letter. After the proper course of action has been decided upon, SCAG must repay Caltrans for the disallowed costs according to a mutually-determined repayment method and schedule.

All of the products listed above or a plan to address findings must be forwarded to Caltrans upon completion, by June 25, 2019. Failure by SCAG to make the required corrective actions will result in Caltrans not recommending approving SCAG's FY 2019–20 OWP and an increase

in the potential for future disallowed costs. No future federal and State expenditures will be approved by Caltrans, FHWA, or FTA unless a satisfactory resolution to all findings has been made. A final report detailing how and when all corrective actions were resolved will be due to the Caltrans DOTP upon the satisfactory fulfillment of all corrective actions. Caltrans has consulted with FHWA and FTA regarding the above course of action.

The Independent Office of Audits and Investigations may perform a follow-up audit after all corrective actions have been made to determine if SCAG has implemented adequate corrective measures for each audit finding and to ensure compliance with Caltrans agreements and federal and State rules and regulations. SCAG's progress with regards to the corrective actions and final resolutions will be closely monitored by Caltrans staff, including any follow-up audit work that may be performed. Additionally, all support documentation and corrective actions provided by SCAG will be reviewed by Caltrans staff.

We appreciate SCAG's cooperation and coordination during this process. If you have any questions, please contact Erin Thompson, Chief, Caltrans Office of Regional Planning, at (916) 654-2596 or by email sent to erin.thompson@dot.ca.gov or Kamal Sah, Office of Guidance and Support, at (916) 653-4336 or by email sent to kamal.sah@dot.ca.gov.

Sincerely,

COCO BRISEÑO
Deputy Director
Planning and Modal Programs

c: Debbie Dillon, Deputy Executive Director, Administration, SCAG
Basil Panas, Chief Financial Officer, SCAG
Rodney Whitfield, Director of Financial Services, FHWA
Tashia Clemons, Director, Planning and Environment, FHWA
Veneshia Smith, Financial Manager, FHWA
John Bulinski, District Director, District 7, Caltrans
Steve Novotny, DLA Engineer, District 7, Caltrans
MarSue Morrill, Chief, External Audits-Local Governments, Independent Office of Audits and Investigations, Caltrans
Ryan A. Dermody, Acting Division Chief, DOTP, Caltrans
Erin Thompson, Chief, Regional Planning, DOTP, Caltrans
Rihui Zhang, Chief, DLA, Caltrans
Kamal Sah, Chief, Office of Guidance and Oversight, DLA, Caltrans
Gilbert Petrissans, Chief, Division of Accounting

DEPARTMENT OF TRANSPORTATION
OFFICE OF THE DIRECTOR
P.O. BOX 942873, MS-49
SACRAMENTO, CA 94273-0001
PHONE (916) 654-5368
FAX (916) 653-5776
TTY 711
www.dot.ca.gov

Making Conservation a California Way of Life.

May 7, 2019

Mr. Kome Ajise
Executive Director
Southern California Association of Governments
900 Wilshire Blvd, Suite 1700
Los Angeles, CA 90017

Dear Mr. Ajise:

This letter is to notify the Southern California Association of Governments (SCAG) of the California Department of Transportation's (Caltrans) determination of the corrective actions regarding findings identified in the *SCAG Fiscal Year 2016–17 Indirect Cost Allocation Plan Audit,* dated January 9, 2019. The audit was performed to determine whether SCAG's Fiscal Year (FY) 2016–17 Indirect Cost Allocation Plan (ICAP) was presented in accordance with Title 2 Code of Federal Regulations (CFR) Part 200 and Caltrans' Local Assistance Program Manual (LAPM) Chapter 5. It was also performed to determine whether SCAG had a financial management system capable of accumulating and segregating costs that are reasonable, allowable, and can be allocated to projects.

Caltrans determined that SCAG's ICAP for the FY 2016–17 is presented in accordance with 2CFR 200 and LAPM Chapter 5. The approved indirect cost rate for 2016–17 is 83.71 percent of total direct salaries and wages, plus fringe benefits. During the course of the audit, we found that SCAG's procurement practices and charging practices (related to properly segregating direct and indirect costs) were not in compliance with federal and State regulations. The noncompliant practices resulted in unallowable costs billed direct to Caltrans in the amount of $2,617,813.

The FY 2016–17 ICAP audit was done in conjunction with the incurred cost audit of SCAG. Please refer to the Incurred Cost Audit report (P1580-0022) for further findings related to deficiencies in labor charging practices, procurement, and contract management.

In response to the audit findings, Caltrans Division of Transportation Planning (DOTP) has developed the corrective action plan below. SCAG must develop a plan to implement all corrective actions listed below by July 1, 2019, to ensure the continued allocation and authorization of federal and State transportation funds.

Caltrans Final Indirect Cost Allocation Plan Audit Report Corrective Actions:

Finding # 1–Improper Procurement Practices

SCAG's procurement practices for ten IT consultant procurements tested did not support that fair and open competition was performed, or that proper procurement procedures were followed as required by Caltrans agreement provisions, federal and State procurement requirements, and SCAG's policies and procedures. The noncompliant procurement practices resulted in unallowable costs billed direct to Caltrans in the amount of $627,179 and unallowable indirect costs included in the FY 2014–15 actual indirect cost pool in the amount of $164,628.

Corrective Actions:

SCAG must revise their Procurement Policies and Procedures manual and train staff accordingly, to:

- Ensure costs that are not in compliance with the federal and State procurement regulations are excluded from the indirect cost pool.
- Revise SCAG's Procurement Policy and Procedures Manual to ensure they are current and comply with all applicable federal and State regulations.
- Ensure management and staff receive proper training in procurement procedures.
- Ensure all documentation is maintained to support that proper procurement procedures are followed in accordance with federal and State regulations.
- Take Caltrans, Division of Local Assistance (DLA), Audits and Engineering (A&E) consultant procurement training either in person or online at http://www.dot.ca.gov/hq/LocalPrograms/training.html

In addition, SCAG must:

- Reimburse Caltrans $627,179 for the disallowed IT consultant contract costs identified in the audit report. Caltrans DOTP will coordinate with SCAG on the method and schedule of repayment.
- Adjust the FY 2014–15 actual indirect cost pool by $164,628 for the unallowable IT consultant costs identified in the audit report.
- Determine the amount incurred and included in the FY 2016–17 indirect cost pool for the seven unallowable IT consultant contracts and adjust the FY 2016–17 indirect cost pool accordingly.

Finding # 2–Deficient Charging Practices

SCAG's charging practices related to billing indirect and direct costs to Caltrans were deficient and resulted in billings that were not in compliance with Caltrans agreement provisions and federal and State regulations. Specifically, SCAG billed an indirect rate for FY 2016-17 that included unallowable direct and indirect costs and billed indirect and ineligible direct labor costs

to a direct project/work element. The charging practices implemented by SCAG did not ensure the proper segregation of direct, indirect, and unallowable costs in the accounting records and costs included on the billings to Caltrans.

Finding 2A–Unallowable Indirect Costs Included in the FY 2016–17 ICAP

In testing 41 transactions within 15 indirect cost accounts for the FY 2014–15 carryforward, Caltrans found that SCAG included direct, unallowable, and unsupported costs in the indirect cost pool. Unallowable costs totaling $196,617 were due to weak internal controls, improper charging practices, and non-compliant vendor procurements. Unallowable mileage costs totaling $11,986 were also included in the indirect cost pool of SCAG's FY 16–17 ICAP.

Corrective Actions:

- Adjust the FY 2014–15 actual indirect cost pool by $196,617 for the unallowable costs identified in the audit report.
- Remove $11,986 from the indirect cost pool for FY 2016–17 for the unallowable travel costs.
- Review all indirect accounts to ensure costs are in compliance with federal and State regulations; are properly segregated between direct, indirect and unallowable; and are supported by original source documentation.
- Adjust the FY 2016–17 indirect cost pool by all unallowable costs identified.
- Establish written policies and procedures for segregating direct and indirect legal costs in compliance with federal and State regulations.
- Establish written policies and procedures that prevent the Internal Auditor from reviewing and approving travel expense.
- Ensure staff provide adequate documentation supporting any and all travel expenses and comply with SCAG travel policies and procedures and Caltrans Agreement provisions related to travel. Also, report to the board monthly of all travel related expenses incurred by the Executive Director.

Finding 2B–Unallowable Labor Costs

The Incurred Cost Audit (dated July 24, 2018) identified indirect and ineligible costs charged to Work Element 120 which was established for direct costs related to development and administration of the Overall Work Program (OWP). This will impact the FY 2016–17 ICAP. Eligible tasks included the development of the OWP, preparation of the annual budget and amendments to the budget, and preparation of Quarterly Progress Reports. In the Incurred Cost Audit, Caltrans found that SCAG accountants and contract administrators charged time for the review and approval of consultant invoices which were ineligible and indirect in nature. SCAG's charging practices remained unchanged for FY 2016–17 and unallowable costs were billed to Work Element 120. Based on an analysis of SCAG's labor reports for FY 2016–17, $1,625,797 of indirect labor related to accountants, contract administrators, and an internal auditor were inappropriately charged direct to Work Element 120.

SCAG does not have adequate policies and procedures related to labor charging practices. In addition to billing ineligible costs identified, the inappropriate charging practices result in SCAG lacking accurate historical information related to actual costs for future budget purposes and overhead rate calculations.

Corrective Actions:

- Reimburse Caltrans $1,625,797 in unallowable labor costs. Caltrans DOTP will coordinate with SCAG on the method and schedule of repayment.
- Ensure billings to Caltrans are based on actual labor costs incurred.
- Develop and implement written policies and procedures for proper and consistent labor charging practices. Ensure procedures define appropriate charging practices for staff meetings and other non-project or work element activities.

Once SCAG repays Caltrans the full $1,625,797 in disallowed costs, they can request to include the disallowed costs in the FY 2016–17 indirect cost pool. If approved, SCAG will then be required to resubmit a revised FY 2016–17 ICAP including the adjustments.

Conclusion:

Please prepare a corrective action plan that outlines the actions SCAG will take to resolve the audit findings and provide the plan to Erin Thompson, Chief, Office of Regional Planning within 60 days of this letter. After the proper course of action has been decided upon, SCAG must repay Caltrans for the disallowed costs totaling $2,617,813 according to a mutually-determined repayment schedule.

All of the products listed above or a plan to address findings must be forwarded to Caltrans upon completion, no later than July 1, 2019. Failure by SCAG to make the required corrective actions will result in Caltrans not recommending approving SCAG's FY 2019–20 OWP and an increase in the potential for future disallowed costs. No future federal and state expenditures will be approved by Caltrans, Federal Highway Administration (FHWA), or Federal Transit Administration (FTA) unless a satisfactory resolution to all findings has been made. A final report detailing how and when all corrective actions were resolved will be due to the Caltrans DOTP upon the satisfactory fulfillment of all corrective actions. Caltrans has consulted with FHWA and FTA regarding the above course of action.

The Independent Office of Audits and Investigations may perform a follow-up audit after all corrective actions have been made to determine if SCAG has implemented adequate corrective measures for each audit finding and to ensure compliance with Caltrans agreements and federal and State rules and regulations. SCAG's progress with regards to the corrective actions and final resolutions will be closely monitored by Caltrans staff, including any follow-up audit work that may be performed. Additionally, all support documentation and corrective actions provided by SCAG will be reviewed by Caltrans staff.

We appreciate SCAG's cooperation and coordination during this process. If you have any questions, please contact Erin Thompson, Chief, Caltrans Office of Regional Planning, at (916) 654-2596 or by email sent to erin.thompson@dot.ca.gov.

Sincerely,

COCO BRISEÑO
Deputy Director
Planning and Modal Programs

c: Debbie Dillon, Deputy Executive Director, Administration, SCAG
Basil Panas, Chief Financial Officer, SCAG
Rodney Whitfield, Director of Financial Services, FHWA
Tashia Clemons, Director, Planning and Environment, FHWA
Veneshia Smith, Financial Manager, FHWA
John Bulinski, District Director, District 7, Caltrans
Steve Novotny, DLA Engineer, District 7, Caltrans
MarSue Morrill, Chief, External Audits-Local Governments, Independent Office of Audits and Investigations, Caltrans
Ryan A. Dermody, Acting Division Chief, DOTP, Caltrans
Rihui Zhang, Chief, DLA, Caltrans
Kamal Sah, Chief, Office of Guidance and Oversight, DLA, Caltrans
Gilbert Petrissans, Chief, Division of Accounting

SCAG
INCURRED COST AUDIT
CORRECTIVE ACTION PLAN

FINDINGS	REQUIRED CORRECTIVE ACTION		STATUS	% COMPLETE
FINDING #1- Improper Procurement Procedures	**SCAG must revise their Procurement Policies and Procedures manual and train staff accordingly, to ensure:**	A. Compliance with all applicable Caltrans requirements and federal and State and federal procurement regulations. This includes revising section 6.6.2 to describe the different competitive procurement processes available and when each should be used in compliance with federal and State regulations.	In Process	70%
		B. Proper management decisions are made when preparing Requests for Proposal that include tasks or sub-tasks that require an Architectural & Engineering (A&E) consultant to perform the work for compliance with federal and State procurement regulations.	Completed and ongoing	100%
		C. Management and staff receive proper training in procurement procedures.	In Process	75%
		D. Staff that are involved in the consultant procurement process perform all required actions and comply with SCAG policies and procedures, Caltrans requirements, and federal and State procurement regulations.	Completed and ongoing	100%
		E. All documentation is maintained to support that proper procurement procedures are followed in accordance with federal and State regulations.	Completed and ongoing	100%
		F. SCAG must also take the DLA A&E consultant procurement training either in person or online. A training webinar is tentatively scheduled to be posted in lat May. If SCAG elects to take the online training, they must provide a list to the DLA Audits Coordinator for those staff who have completed the online training when available. The list shall contain staff names, phone numbers, e-mail addresses, date(s) of completion, and a verification by the staff's supervisor.	In Process	25%
FINDING #2 – Contract Management Deficiencies		SCAG must reimburse Caltrans DLA $338,986 in disallowed costs for the contract with AECOM Technical Services, Inc. The removal of sub-consultants and Task 7 (Consensus) at contract execution, and then reinstating Task 7 at an increase of $619,940 over the initial budget, bear significant noncompliance to warrant reimbursement of the costs disallowed in the audit.	SCAG in discussion with Caltrans	
		SCAG must reimburse Caltrans DOTP $251,552 of disallowed costs to Caltrans. Caltrans DOTP will coordinate with SCAG on the method and schedule of repyament.	SCAG in discussion with Caltrans	

FINDINGS	REQUIRED CORRECTIVE ACTION		STATUS	% COMPLETE
	SCAG must strengthen procurement and contract management procedures to address the following deficiencies:	A. Ensure consultants provide adequate invoice detail to support costs claimed in compliance with consultant contract terms and 2 CFR Part 200 (which superseded 49 CFR Part 18, and 2 CFR Part 225). Additionally, ensure consultants are required to submit invoices that identify the work performed by task/activity and work element so proper documentation is maintained to support consultant billings. Ensure compliance with all federal and State regulations over the administration of consultant contracts.	Completed and ongoing	100%
		B. Establish procedures that identify and define each staff's roles and responsibilities regarding consultant invoice reviews.	In Process	25%
		C. Revise the Grants Management Policies and Procedures and develop a Project Management Policies and Procedures Manual to ensure compliance with all applicable federal and State regulations and provide staff with detailed processes to follow.	In Process	25%
		D. Ensure consultant contracts identify the funding sources and/or work elements of each task/activity when there are multiple funding sources and/or work elements.	Completed and ongoing	100%
		E. Ensure compliance with all federal and State regulations over the administration of consultant contracts and that the contracts contain language as required in the Caltrans' agreements.	In process	95%
		F. Ensure compliance with all federal and State regulations over the administration of sub-recipient (MOU) agreements, that agreements contain language as required in the Caltrans' agreements and include specific contract end dates.	Completed and ongoing	100%
		G. Ensure staff are properly trained on the administration and management of consultant and sub-recipient pass through funds.	In Process	80%

FINDINGS	REQUIRED CORRECTIVE ACTION		STATUS	% COMPLETE
FINDING #3 - Labor and Fringe Benefit Deficiencies	**SCAG must:**	Reimburse the $1,558,051 of disallowed costs to Caltrans DOTP.	SCAG in discussion with Caltrans	
	Additionally SCAG must:	A. Ensure billings to Caltrans are based on actual labor costs incurred.	Completed and ongoing	100%
		B. Ensure the accounting methodology for retroactive pay and merit increases provides for an audit trail for changes made to the employee time sheets and costs are allocated to the appropriate pay periods.	Completed and ongoing	100%
		C. Develop and implement written policies and procedures for proper and consistent labor charging practices. Ensure procedures define appropriate charging practices for staff meetings and other non-project or work element activities.	In Process	75%
		D. Update the Accounting Manual to include procedures for time sheet corrections and retroactive pay and merit increases and train staff accordingly.	In Process	95%
		E. Develop separate fringe benefit allocation methodologies for regular staff, and interns and student assistants.	Completed	100%
FINDING #4 – Billing and Reporting Deficiencies	**SCAG must revise their billing and reporting procedures to ensure the following:**	A. Billings to Caltrans include all applicable information and supporting documentation that trace to the billed costs and SCAG's financial management system. This includes ensuring the Consolidated Planning Grant IT Reports (or equivalent information) are provided and totaled by task associated to the respective work elements that are approved in the current OWP by the Federal Highway Administration (FHWA) and the Federal Transit Administration (FTA).	Completed and ongoing	100%
		B. Supporting schedules provided with the billings include appropriate descriptions detailing where costs are being charged.	Completed and ongoing	100%
FINDING #5 – Possible Conflict of Interest with Sponsorship Program	**In order to avoid the appearance of a possible conflict of interest, SCAG must:**	A. Establish procedures over the Sponsorship Program to ensure there is no real or appearance of a conflict of interest with consultants that provided donations to the Sponsorship Program and are awarded consultant contracts.	In Process	90%

SCAG
INCURRED COST AUDIT
CORRECTIVE ACTION PLAN

FINDINGS	REQUIRED CORRECTIVE ACTION		STATUS	% COMPLETE
		B. Develop policies and procedures over the administration and management of the Sponsorship Program to ensure compliance with all federal and State regulations.	In Process	90%
		C. Create a Conflict of Interest Statement of Certification form to document compliance with SCAG's own policies and procedures referenced above.	In Process	0%

SCAG
INDIRECT COST ALLOCATION PLAN AUDIT
CORRECTIVE ACTION PLAN

FINDING	REQUIRED CORRECTIVE ACTION		STATUS	% COMPLETE	CORRECTIVE ACTIONS
FINDING 1- Improper Procurement Procedures	**SCAG must revise their Procurement Policies and Procedures manual and train staff accordingly to:**	A. Ensure costs that are not in compliance with federal and State procurement regulations are excluded from the indirect cost pool.	Completed and ongoing	100%	SCAG's Manager of Contracts reviews its procurements to ensure they comply with federal and State requirements. If any do not comply, they are funded with local funds.
		B. Revise SCAG's Procurement Policy & Procedures Manual to ensure they are current and comply with all applicable federal and State regulations.	In process	70%	SCAG's Procurement Policies & Procedures Manual will be amended and staff will be trained by October 31, 2019. The CFO will issue written guidance to all staff addressing all changes made and implemented up to the issuance of the new manual detailing incremental revisions.
		C. Ensure management and staff receive proper training in procurement procedures.	In process	80%	On February 11, 2019, Julie Wiley, SANDAG Special Counsel and Manager of Contracts and Procurement, conducted training at SCAG. Since then SCAG has also been actively collecting best practices, updating practices and communicating regularly at All Staff meetings and management meetings. SCAG will continue to conduct periodic training to ensure education and updated information is shared on a continuous basis.
		D. Ensure all documentation is maintained to support that proper procurement procedures are followed in accordance with federal and State regulations.	Completed and ongoing	100%	SCAG has restructured the work assignments in the Contracts Department to shift daily procurement activities away from the Manager and to the Contract Administrators. This now enables the Manager of Contracts to spend more time on oversight to ensure that all documentation is maintained to support that proper procurement procedures are followed in accordance with state and federal regulations. Particular attention is being paid to documenting the preparation and receipt of the independent cost estimates. The Manager of Contracts now uses a more detailed sign-off sheet to review and approve procurement actions.
		E. Take Caltrans, Division of Local Assistance (DLA) A&E consultant procurement training either in person or online at http://www.dot.ca.gov/hq/LocalPrograms/training.html	In process	25%	SCAG will take the A&E training currently being organized by Felicia Haslem, Caltrans A&E Oversight Program Manager in June 2019. To help prepare for this training and better identify A&E type projects and how to procure and administer them, on May 22, 2019, procurement staff attended "Using the AASHTO Audit Guide for the Procurement and Administration of A/E Contracts." Procurement staff will disseminate the information at SCAG's June All Staff Meeting to further support ongoing procurement training efforts. Staff attempted to take the online training but the link would fail during the training. That link has now been removed.
	In addition, SCAG must:	Reimburse Caltrans $627,179 for the disallowed IT consultant contract costs identified in the audit report.	SCAG in discussion with Caltrans		SCAG proposes to substitute other allowable project costs in the amount of the audit finding of $627,179.
		Adjust the FY2014-15 actual indirect cost pool by $164,628 for the unallowable IT consultant costs identified in the audit report.	Completed	100%	Submitted to IOAI on November 19, 2018. Changes to the certification were submitted on November 27, 2018.
		Determine the amount incurred and included in the FY2016-17 indirect cost pool for the seven unallowable IT consultant contracts and adjust the FY2016-17 indirect cost pool accordingly.	Completed	100%	Submitted to IOAI on November 19, 2018. Changes to the certification were submitted on November 27, 2018.
FINDING 2A – Unallowable Indirect Costs Included in the FY2016/17 ICAP		A. Adjust the FY 2014/15 actual indirect cost pool by $196,617 for the unallowable costs identified in the audit report.	Completed	100%	Submitted to IOAI on November 19, 2018. Changes to the certification were submitted on November 27, 2018.
		B. Remove $11,986 from the indirect cost pool for FY 2016/17 for the unallowable travel costs.	Completed	100%	Submitted to IOAI on November 19, 2018. Changes to the certification were submitted on November 27, 2018.
		C. Review all indirect accounts to ensure costs are in compliance with federal and State regulations; are properly segregated between direct, indirect and allowable; and are supported by original source documentation.	Completed and ongoing	100%	Accounting staff review the charges to Indirect Cost accounts for propriety and this procedure has been added to the Accounting Manual in draft form. SCAG will review and finalize the Manual and train staff by October 31, 2019.
		D. Adjust the FY 2016/17 indirect cost pool by all unallowable costs identified.	Completed	100%	Submitted to IOAI on November 19, 2018. Changes to the certification were submitted on November 27, 2018.
		E. Establish written policies and procedures for segregating direct and indirect legal costs in compliance with federal and State regulations.	In process	70%	Changes to the Accounting Manual have been drafted. They will be reviewed and finalized and staff will be trained by October 31, 2019. The CFO has met with the Chief Counsel to convey the needs of this finding with respect to invoices for legal services.
		F. Establish written policies and procedures that prevent the Internal Auditor from reviewing and approving travel expense.	In process	70%	Changes to the Accounting Manual have been drafted to specifically exclude Internal Audit from the travel expense review process. SCAG will review and finalize the Manual and train staff by October 31, 2019.
		G. Ensure staff provide adequate documentation supporting any and all travel expenses and comply with SCAG travel policies and procedures and Caltrans Agreement provisions related to travel. Also, report to the board monthly all travel related expenses incurred by the Executive Director.	Completed with the exception of reporting Executive Director travel to the board monthly. SCAG respectfully disagrees that this is required by Caltrans and therefore should it be requested by the Board, it will be provided.	100%	SCAG has developed a new travel policy to be compliant with all federal and State regulations regarding travel. Staff will be trained on the new policy by July 31, 2019
Finding 2B - Unallowable Labor Costs		A. Reimburse Caltrans $1,625,797 in unallowable labor costs	SCAG in discussion with Caltrans		SCAG requests that Caltrans DOTP address this finding with a programmatic solution recognizing that SCAG has made the necessary internal control and procedural changes to address the finding and prevent a future recurrence.
		B. Ensure billings to Caltrans are based on actual labor costs incurred.	Completed and ongoing	100%	SCAG is actively monitoring labor charges to ensure that staff charge time to the correct work element or non-project activities. New policies and procedures for labor charging practices including monitoring available labor hours for direct and indirect projects, and amending the labor budget as required, will be developed and included in the Finance manuals and in the new project management manual. Finance will provide training to all staff by October 31, 2019.

FINDING	REQUIRED CORRECTIVE ACTION		STATUS	% COMPLETE	CORRECTIVE ACTIONS
		C. Develop and implement written policies and procedures for proper and consistent labor charging practices. Ensure procedures define appropriate chargin practices for staff meetings and other non-project or work element activities.	In process	70%	Starting with FY 2017-18, no time is charged to Work Element 120 except for Budget and Grants staff. Staff meetings and other non-project or work element activities are charged to the Indirect Cost fund in a new indirect cost activity (810-0120.06). New policies and procedures for labor charging practices including monitoring available labor hours for direct and indirect projects, and amending the labor budget as required, will be developed and included in the Finance manuals and in the new project management manual. Finance will provide training to all staff b October 31, 2019.

This Page Intentionally Left Blank

Southern California Association of Governments
900 Wilshire Boulevard, Suite 1700, Los Angeles, California 90017
June 27, 2019

To: Audit Committee (AC)

EXECUTIVE DIRECTOR'S APPROVAL

Kome Ajise

From: Joshua Margraf, Internal Auditor, AC - Audit Committee, (213) 236-1890, margraf@scag.ca.gov

Subject: Internal Audit Status Report (June 2019)

RECOMMENDED ACTION:
For Information Only – No Action Required.

STRATEGIC PLAN:
This item supports the following Strategic Plan Goal 7: Secure funding to support agency priorities to effectively and efficiently deliver work products.

EXECUTIVE SUMMARY:
The Internal Auditor will describe work performed since the last Audit Committee meeting.

BACKGROUND:
Since the last Audit Committee meeting, Internal Audit has assisted the Contracts Department with pre-award reviews, developed a draft annual audit plan, followed-up on prior reports, researched audit standards used by government agencies, and monitored SCAG's Ethics Hotline.

A. Pre-award Reviews
Internal Audit has performed pre-award review work for the proposals listed in Table 1.

Table 1: Pre-award Reviews performed by Internal Audit

Contract Number (Consultant)	Proposal Amount	Questioned Costs	Final Contract Amount[a]
19-021 (Toole Design)	$317,847	$39,553	$0 [c]
19-029 (IBI Group)	$269,554	$5,097	$267,659
19-037 (Iteris)	$325,296	$10,061	$295,035
19-040 (Chen Ryan Associates)	$300,000	$12,253	$299,975
19-043 (JKH Consulting)	$921,664	$662,707	$777,605
19-050 (Alta Planning + Design)	$397,981	$16,805	$374,994
Totals	$2,532,342	$746,476	$2,015,268

[a]Questioned costs are not always sustained for various reasons, such as removal of subconsultants, shifting work to the prime consultant, and consultants providing additional information following the pre-award review, among other things. Contract negotiations can also reduce proposed costs.
[b]Internal Audit completed pre-award reviews for four contracts (19-030, 19-034, 19-038, and 19-039), but final contract amounts are still under negotiation. These will be included in a later report.
[c]SCAG cancelled the negotiation, and has been working with stakeholders to re-scope the project.

Pre-award reviews are non-audit services performed at the request of Contracts Department staff. A request for a pre-award is typically based on an amount: (1) if an overall proposal is $250,000 or more, (2) if a direct labor rate is $100 per hour or more, (3) if an overhead rate exceeds 150 percent, or (4) if a fringe rate is 50 percent or higher. Internal Audit performs pre-award reviews after SCAG selects a consultant proposal, but prior to contract negotiation and execution. Pre-award reviews inform and help Contracts Department staff with cost negotiations by identifying whether consultants' proposed rates are reasonable, allocable, and allowable as well as highlighting potential risks that may be posed by a consultant (e.g. inability to provide requested support for proposed costs, cannot meet contracting requirements, etc.).

B. Follow-up to Prior Reports

At the March meeting, Internal Audit reported that SCAG independent cost estimates (ICE) for potential contracted work varied greatly from selected consultant proposals, specifically with underlying cost categories (e.g. direct labor, indirect labor, profit/fee, and other direct costs).[1] Further, there is a lack of guidance on how staff can develop an ICE (e.g. market research, past experience with similar types of projects, comparable projects at similarly-sized public agencies, etc.) that is clearly linked to the scope of proposed work. SCAG is currently updating its project management processes and procedures as well as other process improvements, to include guidance on how to develop an ICE. Internal Audit can inform the Committee about results at a future meeting.

At the January meeting, Internal Audit reported that SCAG has not always received invoices regularly per contract terms. As per the January meeting, the Committee requested that an action plan regarding vendor invoicing and receipts management be added as a future agenda item. Finance Division staff have developed a survey for vendors that includes questions related to SCAG's invoicing process and procedures, among other things. Survey results are expected to inform any changes to processes and procedures related to consultant monitoring and invoicing. SCAG has received the survey results, which will inform process improvements, including consultant invoicing. More specific information about the survey results will be shared when SCAG staff completes its update of current policies and procedures.

C. Audit Standards

To gain insight on the types of audit standards used by local/government auditors, Internal Audit researched audit standards as well as reached out to other auditors and representatives from the Association of Local Government Auditors (ALGA). These standards are *Generally Accepted Government Auditing Standards* (i.e. "Yellow Book" standards) or the *International Standards for the Professional Practice of Internal Auditing* (i.e. "Red Book" standards) promulgated by the Institute of Internal Auditors (IIA).[2] Given the type of work performed by Internal Audit (in particular

[1]SCAG requires project managers to develop an ICE prior to soliciting work from consultants. The cost estimate is a tool to assist SCAG staff in determining the reasonableness of a consultant bid or proposal. Staff use the estimates to evaluate bids and proposals based on scope and cost.

[2]Government Accountability Office (GAO), *Government Auditing Standards 2018 Revision*, GAO-18-568G, (July, 2018). IIA, International Standards for the Professional Practice of Internal Auditing (Standards) (Jan. 2017).

non-audit services such as pre-award reviews) and the size of the internal audit function, Red Book standards may be more suitable. A report describing key differences between the standards is included as part of this package.

D. External Audits

SCAG has undergone multiple external audits over the past year. Vavrinek, Trine, Day, and Company, LLP (VTD) has started audit work on SCAG's FY 2018-19 financial statements. Caltrans completed an incurred cost audit as well as an audit of SCAG's indirect cost allocation plan (ICAP). The California Department of Finance (DOF) finished an audit of California Office of Traffic and Safety (OTS) grant PS1725 awarded to SCAG.

- Financial Statement Audit
  SCAG's external independent financial auditors have started preliminary audit work on SCAG's FY 2018-2019 financial statements. VTD plan to complete the audit and report the results to the committee later this fall. They will present their audit plan during the committee meeting. A copy of their presentation is provided in this agenda package.

- Incurred Cost and ICAP Audits
  Caltrans completed an incurred cost audit of SCAG in September 2018.[3] SCAG management briefed the Committee about the findings during a special meeting in October 2018. On May 7, 2019 SCAG received a corrective action plan (CAP) letter related to the incurred cost audit that disallowed approximately $2.15 million. SCAG is required to develop its own CAP to address audit findings and recommendations. The due date for this CAP is August 1, 2019.

  Caltrans completed its audit on SCAG's indirect costs allocation plan (ICAP) in January 2019.[4] On May 7, 2019 SCAG received a corrective action plan (CAP) letter related to the ICAP audit that disallowed approximately $2.62 million. SCAG is required to develop its own CAP to address audit findings and recommendations. The due date for this CAP is August 1, 2019.

  SCAG provided a copy of the Caltrans CAP letters to the Regional Council on June 6, 2019 as part of the CFO's board report. SCAG has started developing actions to address the findings and recommendations stemming from both Caltrans audits. After Caltrans reviews and concurs with SCAG's proposed actions, SCAG will repay any disallowed costs according to a mutually-determined repayment schedule. A separate report on SCAG's corrective actions related to the Caltrans audits has been included in this agenda package.

- OTS grant PS1725 Audit
  DOF completed its audit OTS grant PS1725 awarded to SCAG and issued a report in April 8, 2019. The overall grant amount was $480,111. DOF's audit focused on whether grant expenditures claimed were in compliance with grant requirements as well as whether grant objectives were completed per grant requirements. DOF had no findings and indicated

[3]Caltrans, *Southern California Association of Governments Incurred Cost Audit*, (Sacramento, CA: Sept. 21, 2018).
[4]Caltrans, *Southern California Association of Governments Indirect Cost Allocation Plan Audit*, (Sacramento, CA: Jan. 9, 2019).

reasonable assurance that claimed grant expenditures complied with the grant agreement requirements and the grant objectives were completed as required by the grant agreement.

E. Ethics Hotline Monitoring

SCAG received three anonymous reports via the Ethics Hotline since the March meeting (two in April and one in May). The first two reports were closed due to lack of sufficient information for further review. The remaining report contained sufficient information and SCAG's Chief Counsel is in the process of conducting an internal review of the matter.

AGENDA ITEM 5

REPORT

Southern California Association of Governments
900 Wilshire Boulevard, Suite 1700, Los Angeles, California 90017
June 27, 2019

To: Audit Committee (AC)

EXECUTIVE DIRECTOR'S APPROVAL

Kome Ajise

From: Joshua Margraf, Internal Auditor, AC - Audit Committee, (213) 236-1890, margraf@scag.ca.gov

Subject: Annual Audit Workplan

RECOMMENDED ACTION:
Review and approve the fiscal year (FY) 2019-2020 audit plan.

STRATEGIC PLAN:
This item supports the following Strategic Plan Goal 7: Secure funding to support agency priorities to effectively and efficiently deliver work products.

EXECUTIVE SUMMARY:
The internal audit function developed the annual audit plan for presentation to the Audit Committee.

BACKGROUND:
SCAG's Internal Audit department develops an annual audit plan to outline work for the upcoming fiscal year. The plan is presented to the Audit Committee for review and approval. Work listed in the plan takes into account risks identified by staff as well as from audit findings (from both external and internal audit work). It also includes follow-up items from prior internal audit reports. The plan assumes annual total hours to be 2,080 (i.e. 40-hour workweek * 52 weeks per annum) given that the Internal Audit department consists of a single staff. The internal audit plan (including allocation of hours) is flexible, and can change based on Audit Committee and agency priorities, as well as from risks that arise from previous and ongoing audit work.

Pre-award reviews of consultant cost proposals are a key component of Internal Audit's workload given that SCAG relies considerably on consultants to help carry out its planning responsibilities.[1] Work performed as part of pre-award reviews has identified areas of improvement, such as better documentation of cost estimates as well as errors in budget materials supporting consultant proposals.

[1]Pre-award reviews are a non-audit service performed at the request of SCAG Contracts Department staff. Internal Audit performs the reviews after SCAG has selected a consultant's proposal, but prior to executing a contract. They help identify whether costs in a consultant's proposal are supportable as well as identify potential risks that may be posed by a consultant. Results from these reviews help inform contract negotiations.

Project management remains a risk area, and SCAG is working to improve its project management guidance and processes. The California Department of Transportation (Caltrans) released the results of two audits performed on SCAG: (1) an incurred cost (IC) audit, and (2) an indirect cost allocation plan (ICAP) audit.[2] Caltrans found SCAG to be non-compliant with federal and state regulations as well as with its own policies and procedures. Both audits identified areas of improvement related to project managements (such as project managers not performing an evaluation of consultant performance and including unallowable costs in the indirect cost pool, among other things).

SCAG received corrective action plan (CAP) letters for both Caltrans audits on May 7. According to the letters, SCAG is required to develop a plans that addresses audit findings and recommendations for both the IC audit and ICAP audit, and submit them to Caltrans (both plans must be submitted by August 1, 2019). After Caltrans reviews and concurs with SCAG's proposed plans, SCAG will repay any disallowed costs according to a mutually-determined repayment schedule. As per the letters, disallowed costs total approximately $4.77 million ($2.15 million related to the IC audit and $2.62 related to the ICAP audit).[3] Internal Audit would like to look at SCAG's ability to implement the corrective actions as well as the extent to which SCAG has addressed them, to include a repayment schedule. This can include specific procedures such as checking whether staff have received required training as well as whether contract files are properly documented. It can also include a review of updated policies and procedures. In addition, Internal Audit would like to continue to perform reviews on different areas of project management, such as contract monitoring, while also assisting staff as needed with input into updating and revising policies and procedures to address CAP requirements.

Internal Audit has performed reviews of various controls, such as travel expenses and vendor/consultant addresses, because they are relatively straightforward and require little audit hours as well as provide some assurance over how funds are used at a lower level (e.g. staff expenses). Time and resources permitting, Internal Audit can continue to perform reviews on lower level controls.

Table 1 provides the estimated hour breakdown for the proposed plan, followed by a brief description of the topic areas.

Table 1: Proposed Internal Audit Plan FY 2019-20

#	Topic Area	Hours[a]
1.	Pre-awards	530
2.	Project Management	530
3.	Assist – Policies and Procedures	200
4.	IT Controls	130

[2]Caltrans, *Southern California Association of Governments Incurred Cost Audit*, (Sacramento, CA: Sept. 21, 2018), and *Southern California Association of Governments Indirect Cost Allocation Plan Audit*, (Sacramento, CA: Jan. 9, 2019).

[3]Caltrans CAP letters state that an amount of approximately $4.77 million has been disallowed. SCAG's Finance Division indicated that the disallowed amount is approximately $4.4 million ($2.15 million related to the IC audit and $2.25 million related to the ICAP audit) after reviewing the CAP letters.

5.	Audit Committee Meetings	120
6.	Non-work Time	120
7.	Various Controls – Payroll Rates, Travel Expenses, etc.	110
8.	Assist - External Audits	90
9.	Ethics Hotline Monitoring	90
10.	Staff Functions (Staff and Regional Council Meetings)	80
11.	Training to Maintain Certifications	80
	Total	2,080

[a]Internal audit function hours are indirect–all hours are charged to 810-0120.14. Non-work time includes holidays, vacations, etc.

Planned Audit Work (#s 2, 4, 7)

Project Management

Project management is an area that SCAG is working to improve. It is a general term that can include managing staff as well as consultant effort. Last year, SCAG hired a consultant to review and provide training on its project management practices related to procurement. Although these efforts to improve project management were undertaken outside of the Caltrans audits, they can also help address corrective actions identified in the CAP letters. Below are some areas under project management that Internal Audit would like to review/look at.

- *Review and Implementation of Corrective Action Plans* – as noted above, SCAG must submit plans to address corrective actions stemming from the Caltrans audits. SCAG has started to address the audits' findings by undertaking a variety of actions, such as hiring a consultant to help respond to audit findings as well as updating its labor charging practices and procurement procedures, among other things. Internal Audit would like to compare the actions SCAG has underway with the requirements from the CAP letters to determine the extent to which SCAG has addressed the requirements as well as identify any areas where SCAG may need assistance. Additionally, corrective action requirements can help guide audit work with regard to areas to review and test (e.g. consultant monitoring, proper labor charging, etc.).

- *Consultant Monitoring Procedures and Processes* – continue reviews on how SCAG monitors contracts to ensure consultant compliance with contract terms and that consultant performance is tracked. Last year, we found that consultant invoices were not always received in a timely manner. Staff have indicated that invoices have not always been paid in a timely manner. Caltrans' IC CAP letter requires SCAG to establish procedures that identify and define staff roles and responsibilities related to invoicing, among other things. Internal Audit would like to follow-up on prior work with regard to how SCAG reviews consultant invoices and tracks issues with consultant invoicing to ensure efficient and effective use of funds.

- *How SCAG Manages Staff Effort* – review how SCAG develops staff hours for projects listed in the agency's Overall Work Plan (OWP). [4] The ICAP CAP letter requires SCAG to develop and

[4]The OWP is fundamentally a statement of proposed work and estimated costs that tie specific transportation planning activities to specific available funding sources. See http://www.scag.ca.gov/about/Pages/Overall%20Work%20Program.aspx for a copy of SCAG's most recent OWP.

implement policies and procedures for proper and consistent labor charging, among other things. Internal Audit wants to understand the process staff use to determine staff budgets (hours) for OWP projects, to include any official SCAG guidance and how SCAG ensures compliance with funding source requirements.

- *Proposals under Pre-award Threshold* – SCAG relies heavily on consultants to help carry out its planning responsibilities. Internal Audit reviews proposals based on certain dollar thresholds (e.g. $250,000 or more), and has identified issues with proposal estimates. Internal Audit would like to identify and review what processes SCAG has in place for review of consultant proposals that do not undergo a pre-award review.

IT Controls

Accounting System Controls – Internal Audit would like to identify IT controls SCAG has in place for various accounting system modules, to include how access is administered and transactions are monitored, among other things.

Various Controls

Payroll Rates – determine if employee current pay rates are in agreement with Human Resources (HR) files, and the extent to which any variances exist.

Employee Travel Expenses – determine how SCAG ensures travel expenses incurred and funds spent are processed in compliance with agency policies and procedures, as well as ascertain any risks associated with employee travel expenses.

Other Services (#s 1, 3, 5, 8, 9)

Pre-award Reviews

Internal Audit assists the Contracts Department by performing pre-award reviews of consultant proposals after a proposal is selected but prior to executing a contract. They help identify whether consultants' proposed rates are reasonable, allocable, and allowable, as well as any risks that may be posed by a consultant. The number of pre-award reviews requested can vary depending on the amount of proposals that come in.

External Audits

Caltrans completed two audits of SCAG—an IC audit and an ICAP audit.[5] The only current external audit being performed is the annual financial audit performed by Vavrinek, Trine, and Day (VTD). As a result, the number of hours set aside to assist with audits (e.g. responding to information requests and meeting with auditors) is reduced. SCAG's Finance Division has typically been SCAG's point of contact for external audits.

[5]Caltrans, *Southern California Association of Governments Incurred Cost Audit*, (Sacramento, CA: Sept. 21, 2018), and *Southern California Association of Governments Indirect Cost Allocation Plan Audit*, (Sacramento, CA: Jan. 9, 2019).

Hotline Monitoring

Monitor and summarize any reports made to SCAG's Ethics Hotline. Includes performing preliminary fact-finding and investigations as necessary. Estimated hours are based on number of reports made during the prior fiscal year.

Audit Committee Meetings

Preparation for Audit Committee meetings (typically one meeting every quarter) that includes drafting audit reports, soliciting feedback from management and staff, and meeting with the Audit Committee chair prior to the meetings. In cases when individuals outside the agency (e.g. external auditors) present information, coordinate with them. Of specific interest this year are (1) determining which audit standards to follow based on the work Internal Audit is expected to provide and updating the charter accordingly; (2) reviewing composition of the committee to see how it aligns with best practices.

Policies and Procedures Updates

Assist as needed with any updates to SCAG policies and procedures. Past audit findings have indicated that SCAG lacks updated policies and procedures in some areas, such as project management. Although an internal audit function cannot draft agency policies and procedures due to independence impairments, it can suggest areas of consideration as well as best practices based on criteria such as federal internal control standards.

Personnel (#s 6, 10, 11)

Includes time related to (1) staff functions such as RC and staff meetings; (2) training required to maintain audit certifications; and (3) any holidays, vacation, or non-work time.

RECOMMENDATION:

We respectfully request that you review and approve the proposed Internal Audit Plan**.**

FISCAL IMPACT:

None

This Page Intentionally Left Blank

AGENDA ITEM 6

REPORT

Southern California Association of Governments
900 Wilshire Boulevard, Suite 1700, Los Angeles, California 90017
June 27, 2019

To: Audit Committee (AC)

EXECUTIVE DIRECTOR'S APPROVAL

Kome Ajise

From: Joshua Margraf, Internal Auditor, Internal Auditor, (213) 236-1890, margraf@scag.ca.gov

Subject: Audit Standards

RECOMMENDED ACTION:
Approve adoption and use of Red Book audit standards by the internal audit function.

STRATEGIC PLAN:
This item supports the following Strategic Plan Goal 7: Secure funding to support agency priorities to effectively and efficiently deliver work products.

EXECUTIVE SUMMARY:
Internal Audit highlights differences between two sets of audit standards acceptable for local government employees conducting audits, and suggests one set be used by SCAG's internal audit function.

BACKGROUND:
California Government Code requires city/county/district employees conducting audits to follow certain standards.[1] Acceptable audit standards as per California Government Code are (1) Generally Accepted Auditing Standards (GAGAS) (also referred to as "Yellow Book" standards) or (2) International Standards for the Professional Practice of Internal Auditing (i.e. "Red Book" standards).[2] SCAG's internal audit function chose to use Yellow Book standards prior to requesting a peer review that the Association of Local Government Auditors (ALGA) performed in 2015. SCAG's internal audit function passed the peer review with major deficiency related to independence.[3] Other areas for improvement included developing a quality control system and maintaining auditor independence given the type of work performed by the internal audit function (e.g. pre-award reviews). Following the peer review and discussions with ALGA representatives, Red Book standards may better suit SCAG's internal audit function given the type of work it performs.

[1]California Government Code § 1236.
[2]U.S. Government Accountability Office (GAO), *Government Auditing Standards 2011 Revision*, GAO-18-568G, (July 2018), and Institute of Internal Auditors (IIA), *International Standards for the Professional Practice of Internal Auditing (Standards)* (Jan. 2017)
[3]The internal audit function reported to the Chief Financial Officer (CFO) and performed audit work that fell within the CFO's line of responsibility. Other areas for improvement included: developing a quality control system and maintaining auditor independence given the type of work performed by the internal audit function (e.g. pre-award reviews).

SCAG's internal audit function regularly performs non-audit services, such as pre-award reviews. Red Book standards are geared specifically towards the practice of internal audit, and clearly define internal auditing as an independent assurance and consulting activity designed to add value to an organization's operations. The standards are written in such a way that shows an internal audit function can provide more value than simply performing assurance type activities, whereas Yellow Book standards view multiple activities as non-audit services that can jeopardize auditor independence. Further, SCAG's internal audit function does not render an opinion on financial statements as SCAG outsources its annual financial statement audit.

Adopting Red Book standards will not impact work quality as these standards are internationally recognized.[4] Moreover, the internal audit function already consults Red Book standards, and ALGA performs peer reviews using either Yellow Book or Red Book standards.[5] ALGA representatives noted that SCAG can decide which standards to use, and that once it makes a decision, the Audit Charter would should be updated accordingly.

To show where Red Book and Yellow Book standards contrast, some key differences between the standards are highlighted in Table 1 below.

[4]Red Book standards are promulgated by the IIA, the same organization that offers the certified internal auditor (CIA) qualification. The CIA qualification is a globally recognized certification for internal auditors, and SCAG requires internal audit staff to maintain either a CIA or Certified Public Accountant (CPA) qualification.
[5]SCAG's *Internal Audit Charter* (approved March 2018) notes that the internal function will consult Red Book standards in addition to Yellow Book standards. The internal audit function develops an annual audit plan, not required by Yellow Book standards.

Table 1: Differences between Red Book Audit Standards and Yellow Book Audit Standards

Red Book Standards	Yellow Book Standards
Ethics Program	
Require periodic evaluation of ethics program. The evaluation should be documented.	Do not require review of ethics program. Discusses ethics in relation to performance of audit work at auditor level.
External Review	
Require external assessment every 5 years.	Require external peer review every 3 years.
Follow-up on Previous Audits	
Require process to monitor and ensure management actions have been effectively implemented or senior management has accepted risk of not taking action.	Require consideration of previous findings or recommendations in individual audit planning. Do not require auditor to monitor subsequent management actions on audit findings.
Non-audit Services/Independence	
Clearly identify consulting services in definition of internal auditing. Must clearly indicate in any work provided that the auditor is not assuming any management responsibility. Performance of non-audit work must be disclosed to the board.	Categorize any service that is not an audit or attestation engagement as a non-audit service.
Quality Assurance	
Require quality assurance and improvement program.	Require quality assurance program that addresses multiple issues, to include performance monitoring, independence, and staffing, among other things.
Risk Assessment	
Require overall risk assessment and establishment of risk-based annual audit plan to determine internal audit priorities.	Do not require risk-based annual audit plans. Focus on planning of individual audits, including risks specific to the audits.

Source: IIA, *Supplemental Guidance: Government Accountability Office GAGAS: A Comparison 2nd Edition*.

RECOMMENDATION:

Internal Audit is recommending that the Audit Committee recommend to the Regional Council adopt Red Book standards because it better mirrors the type of work an internal audit function can perform while helping ensure audit work is performed to high standards. Moreover, an internal audit function can still maintain understanding of Yellow Book standards and consult them while performing audit work. If work performed by the internal audit function changes or if the function adds capacity at a later date, the discussion as to which standards to follow can be re-visited.

FISCAL IMPACT:

None