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April 11, 2011

Honorable Antonio R. Villaraigosa, Mayor  
Honorable Carmen Trutanich, City Attorney  
Honorable Members of the City Council  
of the City of Los Angeles

Given the slow economic recovery that I projected in my March economic forecast and the continuing budget deficits facing the City, funds that the City receives through the American Recovery and Reinvestment Act (ARRA) are more important than ever. While many of the Recovery Act projects are focused more immediately on jumpstarting the economy, others, especially those involving infrastructure improvements, are expected to contribute to economic growth for many years.

Over the last several months, I have released a number of audits on the City's expenditure of ARRA funds, ensuring that the City is accountable for the funds that it has received, creating jobs, and that the City is transparent in the process. These audits have found that improvement is needed in all of these areas. As a follow-up, my Office was asked by the Audits and Governmental Efficiency Committee to perform a further evaluation on the information reported by the City Administrative Officer (CAO), for information related to expenditures, job creation and retention, and billing for reimbursement for two departments. This audit focused on a detailed review of the underlying records that supported the CAO's summarized results, as reported to Council.

In addition to stimulating the economy and job creation, accountability and transparency are among the top goals of the ARRA funds and should be a top priority in the City's reporting process. There was a clear lack of communication between departments receiving the grant awards and the CAO who serves as the information clearinghouse, raising questions about the accuracy of the expenditures reported and the number of jobs created. The CAO's reported expenditures were understated because fringe benefits were excluded even though the costs were reimbursable and cost adjustments were made by departments subsequent to submitting data to the CAO. In addition, the CAO requested departments to provide information on paid expenditures. As a result, incurred but not paid contracted costs were not reported and contributed to the expenditure understatement. Lastly, some costs incurred as early as August 2009 were still being reviewed by the departments to determine if they were reimbursable.

To compound the reporting challenges, job data was incorrectly reported as well. Some of the reasons that job data was not reported accurately was because departments used different cut-off dates for month-end reporting; labor hour adjustments were made subsequent to information submitted to the CAO; hours worked by other City departments were not included in the calculations; some hours were not correctly included for ARRA work orders; and labor hours are not always adjusted for compensatory time off.

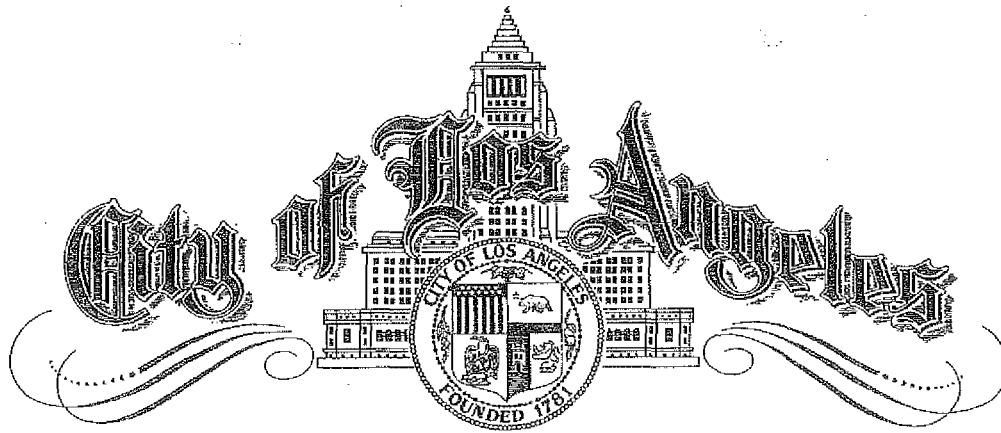
The City must accurately report these funds to ensure receipt of the remaining ARRA funds available. I know that the CAO will continue to work closely with recipient departments to ensure accuracy and consistency in its reporting process. Departments must comply with CAO requests and provide the most accurate information available. Especially during this time of staffing and budget challenges, the City cannot afford to compromise ARRA grant funds that have the potential to provide significant benefit to our local economy.

I encourage all City departments and programs benefitting from ARRA funds to examine this report and recommendations included in my previous ARRA audits to ensure that information is reported accurately and that funds are being spent effectively and efficiently. I will continue to monitor the expenditure of funds and the reporting to ensure that we can get as many Angelenos back to work and that we are in full compliance with the federal government's regulations.

Sincerely,

A handwritten signature in cursive script, appearing to read "Wendy Greuel".

WENDY GREUEL  
City Controller



WENDY GREUEL  
CONTROLLER

April 11, 2011

Miguel A. Santana, City Administrative Officer  
Office of the City Administrative Officer  
200 N. Main St.  
Los Angeles, CA 90012

Dear Mr. Santana:

Enclosed is a report entitled "Audit of CAO's Reported ARRA Results for the Departments of Public Works and Transportation." A draft of this report was provided to your Department on January 14, 2011. Comments provided by your Office and the Bureau of Sanitation, Bureau of Street Services and Department of Transportation at the exit conferences were evaluated and considered prior to finalizing this report.

If you have any questions or comments, please contact me at (213) 978-7392.

Sincerely,

FARID SAFFAR, CPA  
Director of Auditing

Enclosure

cc: Reverend Jeff Carr, Chief of Staff, Office of the Mayor  
Austin Beutner, First Deputy Mayor, Office of the Mayor  
Jaime de la Vega, Deputy Mayor, Office of the Mayor  
Romel Pascual, Deputy Mayor, Office of the Mayor  
Cynthia M. Ruiz, President, Board of Public Works  
Enrique C. Zaldivar, Director, Bureau of Sanitation, Dept. of Public Works  
Nazario Saucedo, Interim Director, Bureau of Street Svcs., Dept. of Public Works  
Amir Sedadi, Interim General Manager, Dept. of Transportation  
June Lagmay, City Clerk  
Gerry F. Miller, Chief Legislative Analyst  
Independent City Auditors



# **City of Los Angeles Office of the Controller**

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## **AUDIT OF CAO'S REPORTED ARRA RESULTS FOR THE DEPARTMENTS OF PUBLIC WORKS AND TRANSPORTATION**

**April 11, 2011**

**Wendy Greuel**  
City Controller

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## AUDIT OF CAO'S REPORTED ARRA RESULTS FOR THE DEPARTMENT OF PUBLIC WORKS AND DEPARTMENT OF TRANSPORTATION

### EXECUTIVE SUMMARY

On September 16, 2010, the Controller's Office issued reports on American Recovery and Reinvestment Act (ARRA or Recovery Act) Performance and Financial Audits of the Department of Public Works (DPW) and the Department of Transportation (DOT). The Departments and the Office of the City Administrative Officer (CAO) generally concurred with the results of the audits and the related recommendations.

The Controller's Office presented the reports to the Audits and Governmental Efficiency Committee (AGE/Committee) on September 21, 2010. The AGE noted that the audits analyzed data that was available in March 2010 and inquired about more recent information. The CAO and Controller's Office were requested to report back.

At the meeting, the CAO submitted a report with updated information related to ARRA expenditures, reimbursements and jobs created/retained by month for January through June 2010 for both departments.

To gain assurance that the CAO's updated information was accurately reported by the departments and supported, the Controller's Office audited the underlying data and source documents for six ARRA grant awards (two each from the Bureau of Sanitation and Bureau of Street Services and two from DOT). The ARRA grants selected were:

#### DPW

##### Sanitation:

- Bike Safe Grating Replacement
- Santa Monica Bay Low Flow Diversion Project

##### Street Services:

- City of Los Angeles Resurfacing Phase 1

- LAX Hospitality Zone Street and Sidewalk Rehabilitation Phase I

#### DOT

- Signal LED Retrofit Program
- New Traffic Signals Project

Our audit sought to answer questions raised by the Committee when the Chair asked for updated information related to ARRA expenditures, job creation and retention and billing for reimbursement for the two departments. In order to respond, we performed audit procedures to determine whether:

- The CAO's reported information was accurate and supported by appropriate source documents;
- DPW and DOT had adequate procedures for ensuring accurate and complete information was captured and reported to the CAO;
- For a sample of reported expenditures from January to June 2010, the information was supported by invoices, employee time sheets, cash receipt reports, etc.;
- Billings to grantors requesting reimbursements for eligible expenses were adequately supported;
- The reported number of jobs created/retained was accurate by tracing to source documents such as cost reports or employee time sheets; and
- DPW and DOT met reporting deadlines to grantor agencies and the reported information was accurate and complete for January to June 2010.

We conducted this audit in accordance with Generally Accepted Governmental Auditing Standards, which focused on reported ARRA-related activities from January through June 2010. The standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Fieldwork was conducted between July and October 2010. While our previous audits of the Departments' ARRA-related processes provided a basis for our assessment of the Departments' control activities surrounding their ARRA projects, this audit focused on a detailed review of the underlying records that supported the CAO's summarized results, as reported to Council.

## **Overall Assessment**

Based on the six ARRA projects reviewed, we noted that key information reported by the CAO did not reflect up-to-date information. The cumulative reimbursements reported by the CAO as received by the departments were in fact received and agreed with billings submitted by the departments. However, the reported expenditures and job counts did not agree with the departments' supporting documentation. Since DPW and DOT generally followed the same processes for recording and reporting ARRA information to the CAO, which in turn, reports at a summary level to the Council, we consider the issues noted from this audit to be applicable to the departments' other ARRA projects, and likely apply to the program as a whole.

As the City's ARRA coordinator, the CAO developed a Project Health Report for City departments to submit financial information (e.g., grant award amount, expenditures for current month, year-to-date expenditures, amount invoiced, amount reimbursed, etc.) and the number of public and/or private sector jobs created or retained.

The CAO's September 21, 2010 report reflected the information provided by the Bureaus of Sanitation and Street Services and DOT in the Project Health Reports submitted for each month from January through June 2010. These previously submitted reports were not updated for more current information and to reflect any subsequent adjustments that occurred after submission. We found that the Bureaus did not inform the CAO of any cost adjustments that were made; nor did they submit revised Project Health Reports to update prior period information. In addition, the CAO did not request updated information for its September report.

For our audit, we requested cost information for the audit period of January through June 30, 2010. Because this information was requested in October, the cost data included any adjustments that had been made subsequent to the initial Project Health Reports. In most cases, we found that more up-to-date cost information was available in August and could have been included in the CAO's report.

The specific differences noted as well as the underlying causes are summarized below, along with our assessment of the departments' billing accuracy, compliance with reporting requirements and challenges. Additional detail on these findings is noted in the body of the report.

## **Cumulative Grant Expenditures as of June 2010**

Our review of the Departments' cost reports and other supporting documentation disclosed the CAO's reported cumulative expenditures were not accurate, since the Departments did not include all costs.



We noted the CAO's reported expenditures were understated for several reasons:

- Fringe benefits costs were not included even though the costs are reimbursable and the departments had billed the grantor;
- Incurred but not paid contracted costs were not reported; yet the corresponding private sector labor hours were included in job counts;
- Cost adjustments were made subsequent to submitting monthly data to the CAO;
- Some incurred and unbilled costs from as early as August 2009 were still being reviewed as of November 2010, to determine if they were ARRA reimbursable.

Additionally, the CAO's reported expenditures did not include indirect costs such as departmental or central services administrative costs. Generally, indirect costs are not billed to the grantor until the last billing, if there are any grant funds remaining. However, it is not clear what information the City's leaders assume they are receiving from the CAO's report – direct, reimbursable expenditures, or the total costs of the ARRA projects (direct and indirect).

The differences in the cumulative expenditures as of June 2010 are noted in Table 1:

**Table 1**  
**Comparison of Cumulative Expenditures in CAO Report as of June 2010**

	Dept. of Transportation		Bureau of Sanitation		Bureau of Street Services	
	LED Retrofit	New Traffic Signals	Bike Safe Grating	Santa Monica Bay Low Flow	LAX Street & Sidewalk Rehab.	Resurfacing Phase I
Total Direct Costs Reported by CAO	\$3,933,107	\$358,020	\$89,714	\$2,661,608	\$1,793,620	\$6,686,431
Total Direct Costs Per Auditor's Analysis	4,502,848	431,851	397,521	2,937,554	2,356,870	7,260,753
<b>Difference – Over/(Under)statement</b>	<b>(\$569,741)</b>	<b>(\$73,831)</b>	<b>(\$307,807)</b>	<b>(\$275,946)</b>	<b>(\$563,250)</b>	<b>(\$574,322)</b>
<b>Difference Accounted for as follows:</b>						
Direct Costs not included in CAO report:						
Fringe Benefits	175,395	72,456	n/a	n/a	530,093	575,276
Accounting Difference (cash vs. accrual)			307,773			
Direct Material Costs	394,296					
Contracted costs	50					
Subsequent Adjustments to labor costs		1,375	34			
Reporting error by Bureau				78,106		
Escrow costs omitted from prior billings and pending eligibility determination				87,847		
Subsequent adjustments				109,993	33,157	(954)
<b>Additionally:</b>						
Incurring Costs under review by Dept.	n/a	1,275	n/a	n/a	n/a	n/a
Indirect Costs not included in CAO Report (dept'l admin., central services admin.)	324,939	134,232	54,810	114,292	1,528,726	2,425,854
Total Direct and Indirect Costs	\$4,827,787	\$567,358	\$452,331	\$3,051,846	\$3,885,596	\$9,686,607

Source: DOT/DPW Project Health Reports, FMIS, Cost Reports and Certified Payrolls

For the sample of ARRA projects reviewed, Table 1 demonstrates that the CAO's reported cumulative direct expenditures were understated by \$2,364,897 or 13%.

### **Cumulative Reimbursements**

The cumulative reimbursements reported by the CAO for both Departments matched the amounts actually received as reimbursements by the grantors, through June 30, 2010. However, since ARRA reimbursements are based on the amounts billed by the Departments, which are in turn based on expenditures, the billings are understated. This is due to billing grantors based on paid costs not for invoices received but not yet paid. In addition, indirect costs (departmental administrative and central services costs) have been incurred but not billed for transportation projects. We also noted that one of the reimbursements received by DOT in January 2010 was incorrectly reported by the CAO as part of the cumulative reimbursement in 2009. This timing difference does not impact the total cumulative amount as of June 30, 2010, which was correctly reported.

### **Job Counts for June 2010**

Our review of the Departments' Job Calculation Worksheets and other supporting documentation (e.g., cost reports and employee time sheets) disclosed the CAO's reported job data is not accurate for several reasons. Specifically,

- DOT uses an earlier cut-off date from month-end and deducts the cumulative labor hours from the prior month's cumulative total. As a result, all prior period corrections are reflected in the reporting month, distorting the FTE hours that are used to calculate the number of jobs created/retained;
- Labor hour adjustments to prior periods were made subsequent to the departments submitting the monthly reports to the CAO;
- Hours worked by other City departments were not included in FTE calculations, despite the lead departments billing the grantor for the associated labor charges;
- A sample of timesheets reviewed had some hours incorrectly scanned to a non-ARRA work order; as a result, the hours worked were not picked up in the cost report for the ARRA project;
- Labor hours used to calculate FTEs are not always adjusted for compensatory time off (CTO). Billings for reimbursement include labor costs adjusted for CTO rates. DOT adjusts its labor hours using the CTO rate; however, neither Street

Services nor Sanitation makes this adjustment. The CAO instructed departments to divide the total number of Recovery Act-funded hours worked for each created or retained job (including overtime, paid leave and other compensation) by the number of hours in that position's full-time schedule to determine the number of FTE's. CTO is paid leave and should be included in the FTE calculation to determine the number of jobs created/retained with ARRA funds. Neither Sanitation nor Street Services adjusts the base work hours by their CTO rates.

Because our review only included a small sample of timesheets, we cannot make a statistically valid conclusion as to whether the reported job counts are under- or overstated. However, the problems noted during our review do not support the CAO's job counts as being accurate.

### **Compliance with Reporting Requirements**

Generally, both DPW and DOT complied with reporting requirements for five of six projects reviewed. Sanitation did not submit reports for one project from January to May but we noted it has since been submitting the reports from June, forward.

### **Accurate Billings**

Both DPW's and DOT's billings were adequately supported. DPW appears to be billing accurately; however, we noted DOT's billings used an unapproved CAP rate and had not billed for some contractual costs (\$46K) and some materials costs (\$90K) that had been incurred and paid. DOT had not billed for some materials while awaiting documentation from GSD; however, our review found that DOT had sufficient supporting documentation to bill the grantor for those. Therefore, DOT's billings did not include all of the costs that could be reimbursed.

### **Challenges Faced by Departments**

As stated in our previous audit reports, although the federal agencies (e.g., FHWA, EPA, etc.) have grant requirements similar to ARRA, the Recovery Act included additional mandates. For example, it is critical that ARRA-funded expenditures can be readily identified to meet transparency and accountability requirements. In addition, ARRA-funded labor hours must be identified to ensure the number of jobs created/retained is accurately calculated.

Also, since two of the primary objectives of ARRA are to stimulate the economy and create/retain jobs, it is critical that contracting processes are streamlined or expedited to ensure projects are started as quickly as possible.

The remainder of the report discusses our observations and conclusions in more detail.

### **Review of Report**

On January 14, 2011, a draft report was provided to DPW, DOT management and the CAO. We held exit conferences on January 24, February 1, and February 23 with the respective departments. We considered the comments provided by the departments and CAO before finalizing this report. We would like to thank the department management and staff for their cooperation and assistance during this review.

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## OBSERVATIONS AND CONCLUSIONS

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### Section I: Cumulative Grant Reimbursements and Expenditures

#### **Department of Public Works Observations:**

Based on our review of cash receipt reports, the cumulative reimbursements as of June 30, 2010 reported by the CAO for the two Sanitation projects and two Street Services projects are accurate, based on the billings submitted to the grantor, which follow Public Works' policy to bill the grantor based on paid costs.

However, our review of the Bureaus' cost reports and other supporting documentation disclosed differences in the CAO's reported cumulative expenditures. We noted the reported cumulative expenditures as of June 30, 2010 do not include incurred but unpaid costs and were not updated to reflect subsequent adjustments. The CAO's September 21, 2010 report reflected the information provided by the Bureaus of Sanitation and Street Services in the Project Health Reports submitted for each month from January through June 2010. These previously submitted reports were not updated for more current information and to reflect any subsequent adjustments that occurred after submission. The Bureaus did not inform the CAO of any cost adjustments that were made nor did they submit revised Project Health Reports to update prior period information. In addition, the CAO did not request updated information for its September report.

For our audit, we requested cost information for the audit period January through June 30, 2010. Because this information was requested in October, the cost data included any adjustments made subsequent to the initial Project Health Reports. In most cases, we found that more up-to-date cost information was available in August and could have been included in the CAO's report.

- Direct costs that were incurred but not paid were not included. Sanitation did not report incurred contracted construction costs in the Project Health Reports. Additionally, Sanitation did not report any expenditures from January through April for the Bike Safe Grating project, despite reporting jobs as created/retained for the same period. As noted in our previous report, DPW's policy is to bill the grantor based on paid costs, not incurred costs. Although Sanitation had received contractor invoices for the construction costs (in one case as early as March), payment did not occur until July. There is a difference of opinion on how costs should be presented – accrual basis or cash basis. The CAO requests departments to provide information on paid expenditures.

The Controller's Office contends that accounting principles dictate that accrued expenditures (i.e., incurred costs) be reported as they are a more accurate representation of accumulated project costs and may be more closely aligned with the progress of the project.

- Some internal labor costs were not included in Project Health Reports. Additionally, some costs, including labor costs, were adjusted subsequent to the submission of the Project Health Reports to the CAO. The CAO indicated that these adjustments were reported by the Bureau in November 2010.
- The CAO requests departments to report the "total dollar amount of cash expenditures" for the reporting month and cumulative expenditures on the Project Health Reports. Street Services did not include fringe benefit costs in its reported expenditures; but Sanitation did include its fringe benefit costs in its reported expenditures.

Additionally, the CAO's reported expenditures do not include indirect costs such as departmental administrative or central services administrative costs. Generally, the Department's practice is to bill indirect costs to the grantor on the last billing and if there are any grant funds remaining. However, it is not clear what information the City's leaders assume they are getting with the CAO's report – only direct expenditures, incurred and intended for reimbursement, or the total costs of the ARRA projects (direct and indirect). As stated in the Controller's previous audit report, the City's decision makers should be aware of all costs (direct and indirect) associated with grant-funded programs/projects, especially if full cost recovery may not be achievable.

For the projects reviewed, we noted the following:

Sanitation – Bike Safe Grating Project

Sanitation was awarded \$1,555,275 ARRA funds for this project. As of June 30, 2010, cumulative direct expenditures were \$397,521 (26% of total award) and cumulative reimbursements were \$47,211 (3% of total award). The cumulative direct expenditures reported by the CAO were understated by \$307,807, as shown in Table 2. This is primarily construction costs of \$307,773 that were incurred but not paid as of June 30, 2010. Based on OMB guidelines, jobs created/retained should be calculated and reported to the extent of ARRA funding/expenditures incurred. Since the private sector jobs created/retained by the construction contractor were included in job estimates, the corresponding project costs, totaling \$307,773, incurred by the contractor for April through June 2010 should have also been included in the Bureau's reported expenditures.

Table 2  
Comparison of Cumulative Expenditures in CAO's Report  
Sanitation's RSTP Bike Safe Grating Project

	June 2010
Total Reported by CAO	\$89,714
Total Per Auditor's Analysis-	\$397,521
<b>Difference – Over/(Under)statement</b>	<b>(\$307,807)</b>
<b>Difference Accounted for as follows:</b>	
Direct Costs not included in CAO Report:	
Fringe Benefits	n/a
Accounting Difference (cash vs. accrual)	\$307,773
Subsequent Adjustments to labor costs	\$34
<b>Additionally:</b>	
Indirect Costs not included in CAO Report (dept'l admin & central services admin)	\$54,810
Total Direct and Indirect Costs	\$452,331

(Source: DPW Project Health Reports, FMIS and Merlin)

We also noted that the CAO reported all City labor incurred from July 2009 to May 2010, in the month of May 2010. Costs should be reported according to the months they were incurred.

The CAO's reported cumulative expenditures also do not include indirect costs which total \$54,810. Direct and indirect costs through June 2010 totaled \$452,331.

Sanitation - Santa Monica Bay Low Flow Diversion Project

Sanitation was awarded \$4,361,106 ARRA funds for this project. As of June 30, 2010, cumulative direct expenditures were \$2,937,554 (67% of total award) and cumulative reimbursements were \$95,086 (2% of total award). The cumulative direct expenditures reported by the CAO were understated by \$275,946. This includes a reporting error by the Bureau for internal labor costs of \$78,106 and escrow costs totaling \$87,847 that were pending determination from the grantor as to eligibility. The remaining \$109,993 were adjustments to costs that were made subsequent to the submission of the Project Health Reports, as shown in Table 3.



Table 3  
Comparison of Cumulative Expenditures in CAO's Report  
Sanitation's Santa Monica Low Flow Diversion

	June 2010
Total Reported by CAO	\$2,661,608
Total Per Auditor's Analysis-	\$2,937,554
<b>Difference – Over/(Under)statement</b>	<b>(\$275,946)</b>
Direct Costs not included in CAO Report:	
Fringe Benefits	n/a
Reporting error by Bureau	\$78,106
Escrow costs omitted from prior billings and pending eligibility determination	\$87,847
Subsequent adjustments	\$109,993
<b>Additionally:</b>	
Indirect Costs not included in CAO Report (dept'l admin and central svcs. admin)	\$114,292
Total Direct and Indirect Costs	\$3,051,846

(Source: DPW Project Health Reports, FMIS and Merlin)

The CAO's cumulative expenditures do not include indirect costs which total \$114,292. Direct and indirect costs through June 2010 totaled \$3,051,846.

Street Services – LAX Hospitality Zone Street & Sidewalk Rehabilitation Project

Street Services was awarded \$7 million ARRA funds for this project. As of June 30, 2010, cumulative direct expenditures were \$2,356,870 (34% of total award) and cumulative reimbursements were \$1,506,106 (21% of total award). The cumulative direct expenditures reported by the CAO were understated by \$563,250. This includes fringe benefit costs of \$530,093 and adjustments to labor costs, materials and other costs of \$33,157 that were made subsequent to the submission of the Project Health Reports, as shown in Table 4. The subsequent adjustments were included in the August billing to Caltrans and therefore would have been known to the Bureau and available to the CAO for inclusion in the CAO's September report.

Table 4  
Comparison of Cumulative Expenditures in CAO's Report  
Street Services LAX Street & Sidewalk Rehab

	June 2010
Total Reported by CAO	\$1,793,620
Total Per Auditor's Analysis-	\$2,356,870
<b>Difference -- Over/(Under)statement</b>	<b>(\$563,250)</b>
Direct Costs not included in CAO Report:	
Fringe Benefits	\$530,093
Subsequent adjustments	\$33,157
<b>Additionally:</b>	
Indirect Costs not included in CAO Report (dept'l admin & central svcs. admin)	\$1,528,726
Total Direct and Indirect Costs	\$3,885,596

(Source: DPW Project Health Reports, FMIS and Merlin)

The CAO's cumulative expenditures do not include indirect costs which total \$1,528,726. Total direct and indirect costs through June 2010 are \$3,885,596.

According to Bureau staff, indirect costs will be billed as part of the last billing if there are grant funds remaining.

#### Street Services - Resurfacing Phase 1 Project

Street Services was awarded \$15,588,000 ARRA funds for this project. As of June 30, 2010, cumulative direct expenditures were \$7,260,753 (47% of total award) and cumulative reimbursements were \$6,048,443 (39% of total award). The cumulative direct expenditures reported by the CAO were understated by \$574,322. This includes fringe benefit costs of \$575,276 and adjustments to labor costs, materials and other costs that resulted in a net effect of (\$954) that were made subsequent to the submission of the Project Health Reports, as shown in Table 5. The subsequent adjustments were accounted for in the Bureau's August billing to Caltrans and therefore would have been known to the Bureau and available to the CAO for inclusion in the CAO's September report.

Table 5  
Comparison of Cumulative Expenditures in CAO's Report  
Street Services Resurfacing Phase I

	June 2010
Total Reported by CAO	\$6,686,431
Total Per Auditor's Analysis –	\$7,260,753
<b>Difference – Over/(Under)statement</b>	<b>(\$574,322)</b>
Direct Costs not included in CAO Report:	
Fringe Benefits	\$575,276
Subsequent adjustments	(\$954)
<b>Additionally:</b>	
Indirect Costs not included in CAO Report (dept'l admin & central svcs admin)	\$2,425,854
Total Direct and Indirect Costs	\$9,686,607

(Source: DPW Project Health Reports, FMIS and Merlin)

The CAO's cumulative expenditures do not include indirect costs which total \$2,425,854. Total direct and indirect costs through June 2010 are \$9,686,607.

#### Department of Transportation Observations:

Based on our review of cash receipt reports, the cumulative reimbursements as of June 30, 2010 reported by the CAO for the two DOT projects are accurate.

However, the reported cumulative expenditures as of June 30, 2010 are not accurate. Our review of the Department's cost reports and other supporting documentation, disclosed the CAO's reported cumulative expenditures did not include all costs, and therefore, is understated. The understatements are due to several reasons.

- The CAO requests departments to report the "total dollar amount of cash expenditures" for the reporting month and cumulative expenditures on the Project Health Reports. However, the total expenditures represent direct labor costs only and do not include costs for fringe benefits. Yet, fringe benefit costs are reimbursable and have been billed by the Department.
- Other direct costs were not included in the Project Health Reports. Direct materials totaling \$394,296 related to the LED project were not reported in the Project Health reports. DOT does not follow a consistent process for

reporting expenditures to the CAO and billing Caltrans for reimbursement. DOT bills Caltrans based on the actual usage of the LED light bulbs, which accounts for the materials' costs, regardless of when the materials were purchased. However, the reported expenditures to the CAO are based on encumbrances incurred for the reporting period. Expenditures billed and reimbursed by Caltrans will not match the CAO's reported expenditures until the completion of the LED Retrofit Program and only if DOT replenishes the LED inventory level at the amount currently not reported (i.e. \$394,296).

Additionally, the CAO's reported expenditures do not include indirect costs such as departmental administrative or central services administrative costs. Generally, the Department's practice is to bill indirect costs to the grantor on the last billing and if there are any grant funds remaining. However, it is not clear what information the City's leaders assume they are getting with the CAO's report – only direct expenditures, incurred and intended for reimbursement or total costs of the ARRA projects (direct and indirect). As stated in the Controller's audit report, the City's decision makers should be aware of all costs (direct and indirect) associated with grant-funded programs/projects, especially if full cost recovery may not be achievable.

Also, we noted additional differences between the CAO's reported expenditures and our analysis of costs incurred and classified as project-related but not included in the CAO's figures, as they were still being reviewed by the Department to determine whether they are ARRA reimbursable or are direct or indirect costs.

For the two grants reviewed, we noted the following:

#### LED Retrofit Program

DOT was awarded a \$9 million ARRA grant for the LED Retrofit Program. We noted the CAO mistakenly reported a Caltrans reimbursement of \$354,116 in 2009 when it was actually received in January 2010. However, the CAO's reported cumulative reimbursements as of June 2010 were correct.

Based on our review, as of June 30, 2010, cumulative direct expenditures were \$4,502,848 (50% of total award) and cumulative reimbursements were \$2,342,373 (26% of total award). We found the cumulative direct expenditures reported by the CAO were understated by \$569,741, as shown in Table 6.

Table 6  
Comparison of Cumulative Expenditures in CAO's Report  
LED Retrofit Program

	<b>June 2010</b>
Total Reported by CAO	\$3,933,107
Total Per Auditor's Analysis	\$4,502,848
<b>Difference – Over/(Under)statement</b>	<b>(\$569,741)</b>
Direct Costs not included in CAO Report:	
Fringe Benefits	\$175,395
Direct Material Costs	\$394,296
Contracted costs	\$50
<b>Additionally:</b>	
Indirect Costs not included in CAO Report (dept'l admin & central svcs admin)	\$324,939
Total Direct and Indirect Costs	\$4,827,787

(Source: DOT Project Health Reports and FMIS)

The understatement is due to the CAO's exclusion of fringe benefit costs, and some direct costs (primarily materials costs) not reported by the DOT. The DOT indicates that it is awaiting clarification from the CAO regarding how to report costs previously paid with General Fund monies.

Also, as stated in the Controller's previous audit report<sup>1</sup>, the Department plans to claim indirect costs (central services and department administrative costs) on the last billing, when the most recent CAP rate is approved and if there are remaining funds available on the grant. The CAO's report did not include indirect costs which totaled \$324,939 as of June 30, 2010. Direct and indirect costs for the LED Retrofit Program totaled \$4,827,787.

#### New Traffic Signals

The DOT was awarded a \$3.5 million ARRA grant for the New Traffic Signals Project. As of June 30, 2010, cumulative direct expenditures were \$431,851 (12% of total award) and cumulative reimbursements were \$175,955 (5% of total award). The cumulative expenditures reported by the CAO were understated by

<sup>1</sup> ARRA Performance and Financial Audit of the Department of Transportation issued September 16, 2010.

\$73,831. This includes fringe benefits of \$72,456 not captured by the CAO, and direct expenditures of \$1,375 not reported by the Department, as shown in Table 7 below.

Table 7  
Comparison of Cumulative Expenditures in CAO's Report  
New Traffic Signals

	June 2010
Total Reported by CAO	\$358,020
Total Per Auditor's Analysis	\$431,851
<b>Difference – Over/(Under)statement</b>	<b>(\$73,831)</b>
Direct Costs not included in CAO Report:	
Fringe Benefits	\$72,456
Subsequent Adjustments to labor costs	\$1,375
<b>Additionally:</b>	
Incurred Costs being reviewed by Dept.	\$1,275
Indirect Costs not included in CAO Report	\$134,232
Total Direct and Indirect Costs	\$567,358

(Source: DOT Project Health Reports and FMIS)

The non-reported expenditures include subsequent adjustments of \$1,375 made after the Project Health Reports were submitted to the CAO.

The CAO's report also did not include indirect costs which totaled \$134,232 as of June 30, 2010. In addition, DOT did not report incurred labor costs totaling \$1,275 because the Project Manager was reviewing the costs to determine if the field supervisor's time is administrative and not billable for reimbursement. The Department should clearly define and instruct field supervisors what labor costs will be considered billable to ensure the costs are accurately captured at the initial time sheet recording. Direct and indirect costs for the New Traffic Signals Project totaled \$567,358. Subsequent to our audit fieldwork, the Department determined that labor costs of \$1,275 were administrative and not billable.

## **Section II: Job Creation and Retention**

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### **Department of Public Works Observations:**

The number of jobs created/retained as reported by the CAO in their September 21, 2010 report was not accurate for the ARRA projects we reviewed, for several reasons:

- Hours worked by other departments/bureaus were not included in the FTE calculations despite billing for the associated labor charges to the applicable ARRA grant.
- Some ARRA work hours were misapplied to a non-ARRA work order due to a scanner misread of employee timesheets.
- Some timesheet corrections were made subsequent to submitting the Job Calculator Worksheets to the CAO. Although the timesheets have supervisory approval, we did not see evidence of the employees' signatures nor written justification, and therefore, cannot determine whether the changes are valid.
- Base work hours were not adjusted by CTO rates. The CAO's Project Health Report Guide describes the FTE calculation as dividing the total number of Recovery Act-funded hours worked for each created or retained job (including overtime, paid leave and other compensation) by the number of hours in that position's full-time schedule. Neither Sanitation nor Street Services adjusts the base work hours by their CTO rates.

For the four ARRA projects reviewed, we noted the following:

#### Sanitation- Bike Safe Grating Project

We noted Sanitation used the CAO's Jobs Calculation Worksheet and the number of jobs created/retained reported for the month of June 2010 is correct for this project. However, Sanitation did not report the correct number of jobs created/retained for January 2010. The Bureau combined all 2009 work hours with January 2010 hours. In doing so, the full-time equivalent (FTE) was overstated for January because the number of available work hours that was used as the denominator for determining FTEs did not include the applicable 2009 hours.

#### Sanitation - Santa Monica Bay Low Flow Diversion Project

We noted the CAO's reported number of jobs created/retained was not accurate. We recalculated the number of jobs created/retained each month from January to June 2010, based on the Bureau's cost report and the contractors' submitted

certified payrolls and noted differences with the CAO's report for each month, as shown in Table 8 below.

Table 8  
Comparison of FTEs  
Santa Monica Bay Low Flow Diversion Project

	FTEs Reported by CAO	FTEs Per Auditor's Analysis	Over/(Under)statement
Jan-10	9.12	10.01	(.89)
Feb-10	11.65	12.27	(.62)
Mar-10	5.08	10.57	(5.49)
Apr-10	7.26	10.50	(3.24)
May-10	7.09	10.32	(3.23)
Jun-10	7.68	12.93	(5.25)

Source: DOT Job Calculator Worksheets, and FMIS

According to Sanitation, the difference can be attributed to subsequent adjustments to labor hours made by the Bureau for a number of reasons. For example, work order corrections, input errors, and the fact that some hours worked were not yet in FMIS when the Job Calculation Worksheets were submitted to the CAO.

#### Street Services – LAX Hospitality Street & Sidewalk Rehabilitation

The reported number of jobs created/retained was not accurate since it did not include work hours incurred by the General Services Department (GSD) and the Bureau of Engineering (BOE). GSD and BOE provided support to Street Services for material testing and survey work. As of June 30, 2010, GSD and BOE had charged Street Services a total of \$145,779<sup>2</sup> for labor costs for this project. Street Services billed Caltrans for GSD's and BOE's costs; therefore, the related work hours by GSD and BOE should be included in the computation of jobs created/retained. We were not able to determine the work hours by GSD and BOE staff since cost statements did not include this information.

In addition, we noted that some staff hours were not included in the Bureau's cost reports. We selected a sample of employee timesheets for June 2010 and attempted to confirm if the hours worked were accurately captured in the cost report. We noted hours were either missing or did not match the hours shown in the cost report, see Table 9 below:

<sup>2</sup> Charged to Street Services' project called LAX Hospitality with ARRA work order no. M0013986



**Table 9**  
**Timesheet/Cost Report Testwork for WO 0013986**

Employee Name	Date & Hours Worked Per Time Sheet	Matched Cost Report?	Impact on Cost Report Hours
V., Jose	06/29/10- 9 hrs	No	under by 9 hours
S., Adelio	06/29/10- 9 hrs	No	under by 9 hours
H., Bruce	06/01/10- 7.5 hrs	No	over by 0.5 hour
T., La Tatia	06/01/10- 7.5 hrs	No	over by 0.5 hour
A., James	06/01/10- 7.5 hrs	No	over by 0.5 hour

Street Services staff explained that when the timesheets were scanned, the scanner read a different work order number. Although the employee time sheets recorded Work Order number **M013986**, the scanner read the Work Order number as **M013966**. As a result, 18 hours were recorded to the wrong work order. According to the Bureau, the necessary corrections were made in October 2010.

For hours that were different from the actual time sheets, time sheet corrections had been submitted on June 4, 2010. Although the correction forms were signed and approved by supervisory staff, we saw no indication of employee signatures or written justification for the adjustments. As a result, we cannot conclude as to whether these adjustments were appropriate nor conclude whether the reported number of jobs created/retained was under- or overstated.

#### Street Services - Resurfacing Phase 1 Project

The reported number of jobs created/retained is not accurate since it does not include work hours incurred by the General Services Department (GSD), Department of Transportation (DOT) and Bureau of Engineering (BOE). As of June 30, 2010, GSD, DOT and BOE had charged Street Services a total of \$613,164 for labor costs for this project. Street Services billed Caltrans for these costs; therefore, the related work hours by GSD, DOT and BOE should be included in the computation of jobs created/retained. Although DOT and BOE provided a summary of hours worked on their cost statements (1,103.6 and 172 hours, respectively), GSD did not provide this level of detail. Therefore, we cannot determine the number of FTEs that should have been reported.

#### Adjusting Work Hours for CTO

We noted an inconsistency between the Department of Transportation (DOT) and Sanitation and Street Services in how work hours are determined for calculating FTEs. DOT adjusts its base work hours by its Compensated Time Off (CTO) rate. However, neither Sanitation nor Street Services adjusts the base work hours by their CTO rates.

The OMB's guidance for estimating the number of jobs created or retained is based on calculating the Full-Time Equivalent of hours worked and funded by ARRA funds. The FTE formula is:

$$\frac{\text{Total Number of Hours Worked and Funded by Recovery Act within Reptg. Qtr.}}{\text{Quarterly Hours in a Full-Time Schedule}}$$

The CAO's Project Health Report Guide describes FTEs as calculated by dividing the total number of Recovery Act-funded hours worked for each created or retained job (including overtime, paid leave and other compensation) by the number of hours in that position's full-time schedule.

CTO rates are to be used when sick, vacation, and other CTO hours are not directly charged to a grant project. Our review of employee time sheets and cost reports for DOT, Sanitation and Street Services disclosed that only hours worked (regular and overtime) are recorded on the ARRA work orders. Other compensated time off (e.g., sick leave, vacation, holiday, etc.) is separately recorded.

Labor costs charged to ARRA grants include CTO rates; therefore, to be consistent, the corresponding hours worked should be adjusted to include the CTO rate for the FTE calculation.

#### **Department of Transportation Observations:**

The FTEs reported by the CAO were not accurate due to the DOT's use of different cut-off periods from the CAO's Job Calculator Worksheet, and not using the current month's work hours but instead, using a calculated difference between current and prior cumulative hours. As a result, we noted discrepancies between the CAO's reported FTEs and our analysis.

We noted the DOT did not report the correct ARRA-funded hours during a work-month in the Job Calculation Worksheet. In order to meet the CAO's monthly deadline, the DOT chooses to establish a cut-off date for the month which does not always coincide with month-end. For example, the April Job Calculation Worksheet included labor hours worked from April 1 to 24, and the May Job Calculation Worksheet included labor hours worked from April 25 to May 22. Despite having 30 days after month-end to complete the Worksheet, DOT stated that the latest payroll information may not be available by the deadline to submit it to the CAO. Since the CAO's Worksheet is based on the number of actual work hours available in a month, using a different cut-off period to calculate jobs will result in discrepancies, as shown in Table 10.

Table 10  
Comparison of FTEs

ESPL5006 (586) -- LED Retrofit Program	FTEs Reported by CAO	FTEs Per Auditor's Analysis	Over/(Under)statement
Jan-10	6.84	6.84	0.00
Feb-10	6.35	6.53	(0.18)
Mar-10	7.11	7.11	0.00
Apr-10	5.51	7.31	(1.80)
May-10	7.09	7.26	(0.17)
Jun-10	10.63	5.26	5.37

Source: DOT Job Calculator Worksheets, and FMIS

We also noted that the DOT does not calculate the actual hours worked, but rather deducts the cumulative labor hours from the prior month's cumulative total. By doing so, all corrections relating to a prior month(s) will be reflected in the reporting month, distorting the FTE hours. While we noted the difference in FTEs was generally minimal, the effect of reporting all adjustments in the reporting month would have resulted in negative labor hours for February, if overtime hours had not been incurred for the New Traffic Signals Project, as shown in Table 11.

Table 11  
Comparison of FTEs

ESPL5006 (589) -- New Traffic Signals	FTEs Reported by CAO	FTEs Per Auditor's Analysis	Over/(Under)statement
Jan-10	1.01	1.01	0.00
Feb-10	1.00	1.79	(0.79)
Mar-10	0.42	0.42	0.00
Apr-10	2.30	4.33	(2.03)
May-10	6.21	6.69	(0.48)
Jun-10	8.34	6.19	2.15

### **Section III: Compliance with Reporting Requirements**

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#### **Department of Public Works Observations:**

Except for some early period submission problems, both Bureaus appear to be meeting reporting requirements.

##### Sanitation

Caltrans requires monthly reports for ARRA projects. We noted Sanitation did not submit monthly reports for the Bike Safe Grating project from January to May 2010; however from June through September, the reports have been consistently submitted. We could not determine whether the reports were submitted timely, however, since Sanitation did not retain copies of the monthly reports.

The quarterly reports required for the Santa Monica Bay Low Flow Diversion project were submitted on time.

##### Street Services

Street Services submitted monthly reports for both projects to Caltrans on time.

#### **Department of Transportation Observations:**

Generally, the DOT is in compliance with reporting requirements from the primary recipient, Caltrans<sup>3</sup> and has met the reporting deadlines, except for February 2010, when the reports were one day late.

We also noted that, in some instances, overtime hours were not included in the job calculation and not all costs were reported to the primary recipient. For the LED Retrofit project, 152 overtime hours were omitted in June 2010, which caused the reported number of FTEs to be understated by one. For the New Traffic Signals Project, 54 overtime hours were omitted in April 2010. The effect on FTEs was insignificant. These monthly Caltrans reports are not used for billing and reimbursement purposes. We noted the overtime hours for the New Traffic Signals Project were billed to Caltrans. The overtime hours of the LED Retrofit Project had not been billed as of our fieldwork date (the latest billing was for costs incurred for April).

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<sup>3</sup> Starting September 2010, departments must also submit a monthly report to the U.S. Census Bureau for construction projects funded by the Recovery Act.

## **Section IV: Accurate Billings**

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### **Department of Public Works Observations:**

Sanitation's and Street Services' billings for the four projects reviewed are understated since Public Works' policy is to bill grantors based on paid costs, not for invoices that have been received but not yet paid. In addition, as previously mentioned, indirect costs (departmental administrative and central services administrative costs) have been incurred but not billed for transportation projects since the projects are still in progress (indirect costs are not billable for Sanitation's Santa Monica Low Flow Project).

As of June 30, 2010, indirect costs for the four projects reviewed totaled \$4,123,682.

### **Department of Transportation Observations:**

DOT's billings for ARRA projects may not be accurate.

We noted that some direct material costs incurred during the period have not been billed and billings subsequent to January 2010 are based on a Cost Allocation Plan that has not yet been approved by Caltrans.

For the LED Retrofit Program, the June 2010 billing used an unapproved CAP rate<sup>4</sup> (CAP 32) for calculating fringe benefits, resulting in an increase in fringe benefits totaling \$1,500 over the last approved CAP rate.

For the New Traffic Signals Project, materials and contractual costs of \$135,859 from July 2009 to June 2010 were not included in the billing to Caltrans. The Project Manager indicates that he intends to review the cost reports to make sure that there are no ineligible costs. DOT's practice is to make sure that all the over-the-counter materials are used exclusively for the ARRA project. Based on our review of the Department's material requisition process, all materials requested and received by DOT were verified by staff. It appears that the DOT has sufficient supporting documentation for the materials costs.

As stated in the Controller's previous audit report for transportation projects, Caltrans only allows billing of indirect costs through approved CAP rates. Departments claim the indirect costs (central services and department administration costs) when the most recent CAP rate is approved and if there are remaining funds available on the grant. Accordingly, the current billing only captures direct costs (salaries, fringe benefits, etc.) but not indirect costs (central services and departmental administrative costs).

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<sup>4</sup> DOT used CAP 32 in the January to June 2010 billings to Caltrans for requesting reimbursement of direct costs.

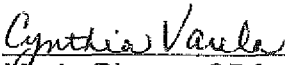
As of June 30, 2010, indirect costs of \$324,939 for the LED Retrofit Project and \$134,232 indirect costs for the New Traffic Signals Project have been incurred but not billed.

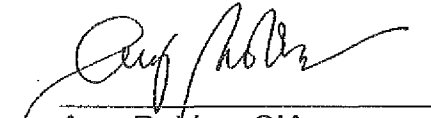
## Section V: Challenges Faced by Departments

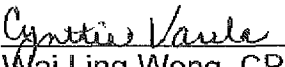
As stated in the Controller's previous reports, although the Federal Highway (FHWA) and EPA have similar grant requirements as ARRA, the Recovery Act has additional mandates. For example, it is critical that ARRA-funded expenditures can be readily identified to meet transparency and accountability requirements. In addition, ARRA-funded labor costs must be identified to ensure the number of jobs created/retained is accurately calculated.

Also, since the primary objectives of ARRA are to stimulate the economy and create/retain jobs, it is critical that contracting processes are streamlined or expedited to ensure projects are started as quickly as possible.

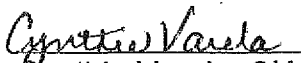
Respectfully submitted,

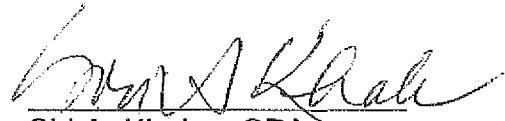
  
for Maria Pheng, CPA  
Internal Auditor II

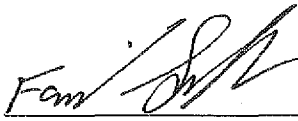
  
Amy Robles, CIA  
Internal Auditor II

  
for Wai Ling Wong, CPA, CIA  
Internal Auditor III

  
for Melani Rejuso, CPA  
Internal Auditor III

  
Cynthia Varela, CIA  
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Director of Auditing

February 23, 2011