Item #3

THE PORT OF LOS ANGELES

AUDIT COMMITTEE

Report to the
Board of Harbor Commissioners

DATE: **MAY 15, 2015**

TO: **AUDIT COMMITTEE OF THE BOARD OF HARBOR COMMISSIONERS**

SUBJECT: RECREATION AND PARKS PERFORMANCE AUDIT REPORT

Please find enclosed a copy of the Recreation and Parks performance audit report. This audit was conducted by Moss Adams LLP under the direction of the Management Audit Divison. A PowerPoint slide presentation summarizing this audit will be presented by Moss Adams at the May 21, 2015 audit committee meeting.

EUGENE D. SEROKA
Executive Director

Attachment:

Transmittal 3: Performance Audit of the City of Los Angeles' Parks Billings from Its Recreation and Parks Department to Its Harbor Department Audit Report

Mb/jo/Management Audit Division Mark Blair
Author: J. H. Olds

Performance Audit of the City of Los Angeles' Parks Billings From Its Recreation and Parks Department to Its Harbor Department

MOSS ADAMS LLP
10960 Wilshire Blvd., Suite 1100
Los Angeles, CA 90024

MOSS-ADAMS LLP
Certified Public Accountants | Business Consultants

WWW.MOSSADAMS.COM

10960 Wilshire Boulevard, Suite 1100
Los Angeles, CA 90024

T (310) 477-0450 F (310) 477-0590

December 15, 2014

Mr. Jim Olds
Departmental Audit Manager
Port of Los Angeles
425 S. Palos Verdes Street
P.O. Box 151
San Pedro, CA 90733-0151

Subject: Performance Audit of the City of Los Angeles' Parks Billings from Its Recreation and Parks Department to Its Harbor Department

Dear Mr. Olds:

Moss Adams LLP is pleased to present the results of our performance audit of the City of Los Angeles' (City) Recreation and Parks (R&P) Department billings to the City's Harbor Department (Harbor) for the period fiscal year (FY) 2010 through June 30, 2014.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The performance audit objectives, scope, methodology, conclusions and a summary of the views of responsible officials are included in the report body.

The Harbor and the R&P Department remain responsible for the proper implementation and operation of an adequate internal control system. Due to inherent limitations in any internal control structure, errors or fraud may occur and not be detected. Also, projections of any evaluation of the internal control structure to future periods are subject to the risk that the internal control structure may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

This report is intended solely for the use of the Harbor. Moss Adams does not accept any responsibility to any other party to whom this report may be shown or into whose hands it may come.

We would like to express our appreciation to both the R&P Department and the Harbor for their cooperation throughout this audit. Please do not hesitate to contact Curtis Matthews at (503) 704-6943 if you have any questions or need further assistance regarding this important matter.

Moss Adams LLP

Moss Adams LLP

TABLE OF CONTENTS

EXECUTIVE SUMMARY 1

BACKGROUND INFORMATION 3

OBJECTIVE, SCOPE AND METHODOLOGY 4

RESULTS 11

PERFORMANCE AUDIT RESULTS 12

APPENDIX A – LIST OF DOCUMENTS REVIEWED 19

APPENDIX B – CALCULATION OF COST IMPACT OF POTENTIAL DUPLICATION OF LABOR COSTS 21

APPENDIX C – CALCULATION OF COST IMPACT OF SHIFT FROM PT TO FT PERSONNEL 22

APPENDIX D – RECONCILIATION OF LABOR COSTS 23

APPENDIX E – ADJUSTMENTS TO R&P BILLING AMOUNTS 24

EXECUTIVE SUMMARY

Our performance audit of billings from R&P to Harbor for the period FY 2010 through June 30, 2014, indicated a number of good controls on the part of both R&P and Harbor as follows:

Good Practices

- Significant review of quarterly billings from R&P is performed by Harbor.
- R&P does provide quarterly billings which include details on indirect rates applied and costs billed by Harbor location.
- Both R&P and Harbor are aware of the Tidelands Trust Memorandum of Understanding (MOU) that defines the relationship between R&P and Harbor with regards to the services to be provided to Harbor.

This performance audit also identified areas of improvement specific to R&P billings to Harbor as follows:

Areas for Improvement

Our audit indicated the following areas for improvement:

- We identified a potential duplication in the amount of $238,677 of management and accounting labor costs charged directly to Harbor with similar management and accounting costs allocated to Harbor through the application of the Departmental Overhead rate.
- We observed a significant increase in billings to Harbor with $794,779 resulting from a shift from part-time (PT) to full-time (FT) personnel due to the much higher fringe benefit costs associated with FT personnel.
- We attempted to reconcile R&P labor billings to Harbor to labor cost reports requested from R&P. In some cases, the reports were not provided, and in other cases the amounts billed did not reconcile to the report provided. In total, reported labor exceeded billed labor by $606,542.
- R&P indicated that revenues were earned related to Harbor properties that R&P did not use to offset amounts owed in the quarterly billings submitted to Harbor. R&P stated that, in accordance with the MOU, it is not required to offset billed amounts with these revenues. Despite at least three requests over several months, R&P declined to respond to our requests for additional information to enable us to ascertain the validity of R&P's position regarding the revenues.
- In order to evaluate compliance with the State Tidelands Trust Act (STTA) of labor costs billed to Harbor, we requested details related to the specific activities performed for labor hours billed to Harbor. R&P responded that the only documentation of

activities performed is that employees select job codes when charging their time. R&P indicated that specific documentation of activities performed does not exist and that the MOU between R&P and Harbor does not require R&P to maintain this documentation. This presents a problem with regards to Harbor meeting its responsibility to ensure that all Harbor expenditures are in compliance with the STTA. We recommend that an agreement be established that ensures that adequate documentation exists so that Harbor can evidence compliance with the STTA. R&P should be held accountable to document in sufficient detail why labor is being billed to Harbor.

- Article 17 of the MOU requires that at least once every five years the parties jointly fund an independent study to determine if the services provided under the MOU are complete, accurate and consistent with applicable STTA principles. It has been over ten years since the last study. We recommend that a study be conducted as soon as possible to bring the parties into compliance with the MOU requirement.
- Significant adjustments to R&P billings were made by Harbor in FY 2013 and FY 2014 to address issues such as inclusion costs related to non Harbor properties.

Please see the report body for further information on the above areas for improvement.

BACKGROUND INFORMATION

The Port of Los Angeles (POLA or Harbor) is the number-one port by container volume and cargo value in the United States. POLA generates 919,000 regional jobs and $39.1 billion in annual wages and tax revenues. A proprietary department of the City, POLA is self-supporting and does not receive taxpayer dollars. At POLA, high priority is placed on responsible and sustainable growth initiatives combined with high security, environmental stewardship and community outreach.

Under City Charter, the Harbor is to use services provided by other City departments. In obtaining such services, the Harbor and the relevant City department first negotiate an MOU that establishes the terms and conditions of such work. These services include legal, fiscal, fire support, park and grounds maintenance, personnel and information technology, among others. This arrangement is similar to that used for other City proprietary departments including the Los Angeles World Airports and the Department of Water and Power. In addition to direct-service costs, the Harbor also pays an indirect overhead cost allocation for those services using an annual Cost Allocation Plan (CAP) established by the City Controller. The MOU between the Harbor and R&P that covers park and grounds services expired on June 30, 2008, and is currently in carryover status.

Objective, Scope and Methodology

Objective

Moss Adams was engaged by the City's Harbor Department to execute an analysis of the City's R&P Department's billings paid by the Harbor for the FYs 2010-2014 to assess their reasonableness and accuracy. The review was to include an assessment of R&P's personnel and equipment billed over the last four years to measure to what extent such detailed data supports the costs billed to the Harbor. The audit was also to include specific recommendations related to unsupported or unreasonable services billed, if any.

Scope

This project was conducted in two phases, beginning with a preliminary review of the monthly billings and internal controls. Based on this review we developed a detailed work program. Based on the results of the risk assessment performed in Phase I described below, we performed Phase II fieldwork and reporting. Once the preliminary review was complete, our audit program was approved by the Departmental Audit Manager and our fieldwork began. Upon completion of fieldwork, a draft report was submitted to the Departmental Audit Manager for review and comment prior to preparing the final report. We also kept the Departmental Audit Manager informed of all significant issues as they arose.

Methodology

Phase I – Preliminary Review

Conduct Entrance Conference

An entrance conference was conducted with the key personnel responsible for R&P billings and MOU compliance. We worked with the Departmental Audit Manager to identify the key personnel and sources of documentation needed to perform our analysis. During this entrance conference, we reviewed the scope of the project and the information required to conduct our analysis. Project effort and access to key personnel was discussed and coordinated.

Request Documentation

This review began with a request for available documentation needed to perform our analysis. The initial documentation request included:

- Monthly billings for services from the City's R&P Department to the Harbor Department from FY 2010 through FY 2013.
- Billing support to assess causes for any changes in billings over time.

- Cost details and descriptions covering the City services component cost descriptions, including personnel costs for all staff providing services by cost center and the calculations of all administrative, overhead and benefit charges, as well as the cost allocation methodologies governing each cost component.
- Cost allocation plan rates and supporting detail from FY 2010 through FY 2013.
- A summary of all R&P personnel assigned and billed to the Harbor, including sufficient detail to identify specific employees and functions to cost allocation plans and billing supporting schedules such as total headcount, position classifications, names and payroll numbers.
- The Nexus MOU, MOU cost charges and related supporting documentation.
- Policies, procedures and guidelines used by R&P to identify and exclude unallowable and unallocable cost from billings to the Harbor Department (as available). Specific emphasis will be placed on controls designed to ensure billings are current, accurate and complete.
- Prior consultant reports covering R&P billings to the Harbor (as available).
- Other data as determined necessary to complete the Phase I preliminary review.

Once this initial documentation was received, we performed a preliminary review to ensure that the documentation received corresponded to the requested information in terms of completeness, nature and timing. Reconciliation of billings to cost support was performed. Mathematical accuracy was verified. The nature of cost charges and methods used for charging costs were given specific focus and attention. Additional detail on documents reviewed during the analysis is presented in Appendix A.

<u>Perform Interviews</u>

We conducted interviews to validate our understanding of the information reviewed and to verify that the methods used to prepare billings and related controls applied to ensure amounts billed are current, accurate and complete. Specific emphasis was placed on assessment of cost compliance risks.

Prepare Detailed Work Plan

After obtaining the requested information, we performed a risk assessment that ranks risks identified and determines planned steps for detailed testing of risk areas in Phase II of the project. The assessment included summarizing and analyzing the historical context of the City charges paid by Harbor for park and grounds services for the period of FY 2010 through FY 2013, including a summary of trends over the period reviewed.

A detailed draft work program was developed that was utilized in Phase II. The draft program was submitted to the Departmental Audit Manager for review and mutual agreement on the detailed fieldwork steps to be performed.

PHASE II – FIELDWORK AND REPORTING

The Phase II work plan and general program addressed risks identified in the Phase I preliminary review as indicated below. To the maximum extent possible, information from R&P's accounting system was used to determine total expenditures (direct and indirect) applicable to the cost allocation review. Total costs, regardless of the funding source, were identified for each function and expenditure type.

We performed testing of R&P's indirect expenditures based on an assessment of risk related to the inclusion of unallowable and/or otherwise inappropriate costs included in cost allocation pools. We also determined whether the base utilized to determine the cost allocation rates included all applicable unallowable costs.

We determined whether all direct costs are supported by indirect activities, including unallowable costs. We identified and excluded unallowable costs from the indirect cost rate calculation and application. We helped ensure that, once established, the same costs had been excluded when calculating the indirect cost reimbursement and when calculating amounts billed.

In accordance with the MOU and any other applicable agreement, we assessed direct costs used in the base or denominator of indirect rate calculations. Direct costs are those that can be identified specifically with a particular cost objective. Direct costs were assessed for specific applicability and chargeability to Harbor projects. Examples of direct costs analyzed include:

- Employee compensation
- Supplies and materials
- Equipment purchased
- Project travel expenses incurred

In accordance with the MOU or any other applicable agreement, we evaluated indirect costs which comprise the cost allocation rate pool. Examples of indirect costs include the salaries and expenses for the following departments:

- Information Technology
- Accounting
- Human Resources
- Payroll Processing
- Purchasing

However, the specific applicable indirect costs were assessed based on the MOU and any other applicable agreement. To the extent that the agreement does not provide specific guidance on a particular cost, we considered other applicable criteria including Generally Accepted Accounting Principles (GAAP) and Federal Cost Accounting Standards (CAS).

We reconciled amounts in the indirect cost rate calculation to the audited financial statements or final expenditure reports. R&P was expected to provide support or explanation for any material variances. The direct cost base (distribution base) was assessed for best fit in assigning indirect costs to all cost objectives in accordance with the relative benefits received. To the extent that the MOU or other applicable agreement specifies the allocation base, then we tested for compliance with the agreement.

We assessed indirect cost rates for the use of current, accurate and complete information in determining the amounts billed. We quantified the impact of any differences between the method used by R&P and the audit adjusted cost allocation rate.

Detailed Analytical Procedures Applied Include:

1. Historical Context of City Charges to the Harbor for Park and Ground Services

The causes for the trends related to billings to the Harbor identified in Phase I were determined by performing the following steps:

- Analytical procedures were applied to billing trends, and inquiries will be made to gain perspective on changes identified in the billing analysis.
- Specific cost elements where significant changes have been identified (if any) were assessed in greater detail to determine the root cause for significant increases. Our analysis considered root causes due to an increase in costs incurred by R&P or changes in cost allocation methods applied. Both allocation pools (rate numerators) and allocation bases (rate denominators) were assessed to identify the basis for rate changes.

2. Verification of the Calculations and Support Underlying R&P Billings

A verification of R&P billings was performed, with consideration given to the potential exposure areas identified during the Phase I risk assessment. We performed the following steps:

- A sample of R&P billings for the period of FY 2010 through FY 2014 was selected. For the sampled billings, the following steps were performed:
  - Developed test program based on briefing of applicable MOUs and other agreements (as applicable) to verify compliance with the agreement.
  - Requested documentation to support amounts billed including:
    - Invoices for equipment and services.
    - Support for personnel costs.
    - Administrative overhead and benefit charges, including the cost allocation methodologies governing each component.
  - We compared actual practices related to identification and allocation of costs to those contained in MOUs and other agreements. We also assessed equitability from the perspective of verifying that the correct causal and beneficial relationship exists between the allocation methods used and the related Harbor billings (cost objectives). Specific steps involved in the allocation analysis included:
    - Verifying that the R&P Department has created cost pools that are homogeneous with regard to the types of costs accumulated.
    - Assessing cost pools to validate that amounts charged are allocable and allowable to Harbor billings.
    - Verifying that the allocation base used is the most equitable base considering the circumstances and includes all applicable base costs to ensure the Harbor is not being over-allocated costs.
    - Ensuring that unallowable amounts are treated correctly by excluding the costs from cost pools while including those costs in applicable allocation bases.
  - We assessed the compliance of the billings with the requirements of the STTA to assess whether the billings by R&P were consistent with STTA requirements. To accomplish this task, we considered the act itself and the following leading cases:
    - City of Long Beach v. Morse, 31 Cal. 2d 254 (1947)

    - Mallon v. City of Long Beach, 44 Cal. 2d 199 (1955)
    - Other cases as appropriate
  - We then assessed whether R&P billings are consistent with the STTA with regard to billing only actual allocable costs. One area of focus was to ascertain whether amounts billed violated the prohibition for the use of revenues derived from State Lands for general City services. To complete this assessment we considered whether:
    - Billings represented only verifiable actual costs that are allocable to the Harbor.
    - Costs billed included amounts for general City services that should not be billed to the Harbor in accordance with the STTA.
    - Allocation methods represented an equitable billing for use of revenues derived from State Lands. To assess the equitability of allocations, the following criteria was considered:
      - ✓ Applicable MOUs and other agreements regarding cost allocation.
      - ✓ Other principles as appropriate including the Federal CAS. While these standards may not be specified in agreements between the Harbor and R&P, they do provide widely accepted and well-established criteria with which to assess the equitability of allocations performed.

3. Review of R&P Personnel Assigned and Billed to the Harbor

For billings selected for review for the period of FY 2010 through FY 2014, we determined the personnel assigned and billed to the Harbor. Total headcount, position classification, names, payroll numbers and schedules were given specific consideration in our analysis. For each employee, we obtained supporting documentation including the rationale for charges billed for these employees and to the Harbor. We then assessed the documentation and compared the methodology used to that described in the MOU or other applicable agreements.

4. Assessment of Allowability of Billings in Accordance with Tidelands Trust Allowable Objectives

Applicable MOUs identified in Phase I were reviewed for compliance through the steps to be performed above. The relationship between work billed to Tidelands Trust allowable cost objectives was analyzed. Specific emphasis was placed on identifying unallowable and unallocable costs. Questioned and unsupported costs that were identified in our analysis were summarized by noncompliant cost category and amount.

5. Review of Cost Allocation Plan Rates and Models to Impute the Harbor's Share of Services

The cost allocation plan review will leverage the Phase I risk assessment. In conjunction with the allocation review performed in Step 2 above, the following detailed allocation testing steps were performed:

- We performed detailed analysis of allocation methods used. In those cases where the MOU and any other applicable agreements did not provide specific guidance regarding identification and allocation of cost, we utilized GAAPs, CASs, and/or other relevant criteria to assess the equitability and compliance of methods used.
- We assessed practices applied and controls in place at R&P to help ensure that unallowable costs are excluded from billings to the Harbor. Specific focus and attention was given to the rates and models applied to billings. The imputed Harbor individual share of service amounts incurred and noncompliant charges were analyzed and summarized.

RESULTS

The results of the analysis of R&P billings to Harbor for the period FY 2010 through June 30, 2014, are as follows:

Comparative Analysis

Our scope included performing a comparative analysis of R&P billings to Harbor overtime. The analysis indicated the following changes in cost billings between FY 2010 and FY 2013:

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2010-13
FT Salaries	$2,351,801	$2,534,270	$3,469,955	$3,791,908	$1,440,107
FT Fringe	1,231,167	1,326,689	1,816,519	2,128,207	897,040
FT Central Services	666,032	717,705	982,686	1,059,936	393,904
FT Dept Admin	287,155	309,430	423,681	481,396	194,241
PT Salaries	1,454,331	1,243,246	431,286	664,881	(789,450)
PT Fringe	129,872	111,021	38,511	58,446	(71,426)
PT Central Services	411,865	351,787	122,140	179,231	(232,634)
PT Dept Admin	171,321	149,002	50,806	92,102	(79,219)
O&M Expenses	445,852	465,212	272,596	431,430	(14,422)
Citywide Construction	142,672	124,874	131,365	131,548	(11,124)
Pacific Region	153,529	140,276	136,844	159,625	6,096
Rangers-Security	68,833	8,172	5,371	49,861	(18,972)
TOTAL	**$7,514,430**	**$7,481,684**	**$7,881,760**	**$9,228,571**	**$1,714,141**
Change from Prior Year		**(0.4%)**	**5.3%**	**17.1%**	

The $1.7 million increase between the two periods represents a 23 percent increase. In addition, review of year-to-date (YTD) FY 2014 data indicates a further significant escalation in amounts billed as compared to 2013 levels.

R&P indicated that it had no significant changes in scope of services, hours charged or service levels provided that would account for the cost increases. Please see Observation 2 below for the results of the follow-up related to the cost increases identified in the analysis above.

PERFORMANCE AUDIT RESULTS

Observations, assessments of practices, recommendations and views of responsible officials are as follows:

Observation 1 – Duplication of Direct Labor Charges with Department Overhead Allocation

Observed Practice

Analysis of all positions charged directly to Harbor by R&P for FY 2013 and the six-month period ended March 31, 2014, identified a number of positions that were accounting and/or management in nature. We also observed that the Departmental Administration Overhead rate that was applied to both FT and PT labor charged to Harbor also included labor costs for accounting and management activities. This appeared to be a duplication of costs, both as a direct and indirect cost.

Assessment of Practice

We inquired with R&P on July 18, 2014, as to whether these positions were potentially duplicative of labor costs included in R&P's Departmental Administration Overhead rate that was applied to both FT and PT labor charged to Harbor. We also followed up on at least three occasions regarding the status of R&Ps response to this request. R&P has not responded to our request as of the date of this report.

The impact of this issue was quantified for FY 2013 and the six-month period ended March 31, 2014. We question direct labor charges (and associated indirect costs) of $75,808 for FY 2013 and $162,869 for the six-month period in FY 2014, which ended March 31, 2014. Please see Appendix B for further details.

Recommendations

1.1 We recommend removal of $238,677 duplicated in costs billed to Harbor.
1.2 An analysis should be performed by the R&P Department to determine the impact and removal of duplicative charges for prior years.
1.3 Actions should be taken to improve visibility and avoid duplicated billings for accounting and management cost charges in the future.

Views of Responsible Officials

Although requested on July 18, 2014, and during numerous follow up requests, an official response was not provided by R&P as of the date of this report.

Observation 2 – Shift from Part-Time (PT) to Full-Time (FT) Personnel Resulted in Significant Cost Increases

Observed Practice

Cost increases in billings from R&P to Harbor between FY 2010 and present were the result of an employment terms shift from using PT personnel to using FT personnel. The cost increase is caused primarily by the much higher fringe benefit rate for FT personnel. This appeared to represent excessive costs which could have been prevented.

Assessment of Practice

R&P did not provide documentation to substantiate the rationale behind the shift in employee categories and resulting cost increases. Because PT personnel were used much more frequently in 2010, significantly lower costs were incurred that year as compared to FYs 2012, 2013 and 2014. This is primarily due to the large difference in the fringe benefit rate for PT and FT personnel. We also compared FY 2011 against FY 2010 and noted a less significant change from PT to FT personnel for FY 2011.

Review of MOU Article 2, Section D "Change of Service Level" indicates that "…all increases and decreases shall be solely authorized by the Department (POLA) by written amendment…" The article goes on to state that "if the proposed change amounts to no more than 5 percent in a fiscal year…" an interim amendment may be agreed to instead of a formal written amendment. The article also clarifies that "normal salary increases" are not subject to the limitation above. The cost increases do not appear to be the result of normal salary increases but rather a change in staffing approach as discussed above. In addition, as is summarized in the comparative analysis section above, the change in FYs 2012 and 2013 exceeded the 5 percent limit, thereby requiring a formal written amendment for the change. However, no written amendments were agreed to related to the cost changes experienced in FY 2012 or FY 2013 and no agreement has been reached for FY 2014 which would address the cost increases experienced thus far in FY 2014. The observed practice of exceeding MOU thresholds for cost increases without obtaining agreement does not appear to be in compliance with the MOU.

We have quantified the approximate impact of the shift to FT personnel for FY 2012 and FY 2013 to be $448,605 and $346,174 respectively. Please see Appendix C for details behind the calculation of the cost impact. Because FY 2014 is only partially complete, we did not attempt to calculate the impact for FY 2014.

Recommendations

2.1 R&P should analyze its current mix of PT and FT staff that is being billed to Harbor to assess whether some positions could be filled by PT personnel, thus resulting in lower costs to Harbor.

2.2 We recommend that R&P inform Harbor and obtain its authorization prior to making decisions that could result in significant cost increases to billings to Harbor prior to incurring the additional costs. Harbor, as the recipient of the services, and the payer of the bills, should have an opportunity to comment on the proposed cost increases and R&P should consider Harbor's position prior to incurring additional costs that it will then bill to Harbor.

Views of Responsible Officials

Although requested both prior to and during the exit conference on September 11, 2014, an official response was not provided by R&P as of the date of this report.

Observation 3 – Unreconciled Labor Billings

Observed Practice

We requested labor reports from R&P for the last two quarters of 2013 and the first two quarters of 2014 to reconcile with labor billings to Harbor. R&P did provide most but not all of the requested reports. In addition, we identified differences between the labor reports provided and the amounts included on billings to Harbor. These differences were both positive and negative for the quarters reviewed; however, the net impact of the differences was that billings were $606,542 less than the labor report totals. We cannot place reliance on the reconciliation performed due to these unexplained differences. Please see Appendix D for additional details related to the reconciliation of labor billings.

Assessment of Practice

We evaluated the reconciliation issues and concluded that the labor charges to Harbor for the periods reviewed were not fully supported.

Recommendations

3.1 R&P should perform a complete reconciliation of labor charges to labor billings for FY 2013 and the first two quarters of FY 2014, and provide this information to Harbor for review.

3.2 R&P should implement controls whereby reconciliation of labor reports to labor billings is performed at least quarterly.

Views of Responsible Officials

Although requested initially with document request 20 on July 3, 2014, and in various subsequent requests, an official response was not provided by R&P as of the date of this report.

<u>Observation 4</u> – Compliance with the Tidelands Trust MOU Requirements for Revenue Utilization

<u>Observed Practice</u>

The only revenue offset against billings to Harbor for the period of FY 2010 through the present is parking lot revenue. R&P indicated that there are other revenues (for example, those recorded to Fund 301), but contended that in accordance with the MOU, R&P is not required to offset billings with these revenues. R&P directed us to MOU Article 8 to support its position. MOU Article 8 states, in part: "The Recreation and Park (R&P) Department shall receive all income. Such income shall be expended by the R&P department for operation and maintenance of properties and facilities described in Exhibit B (of the MOU). Any such income deposited in the general fund shall be credited against payments owed according to Exhibit B." R&P contended that since the revenues were not deposited in the general fund, there was no requirement that these other revenues be credited against billings to the Harbor.

We also observed that the MOU Page 2, Paragraph 3 states; "WHEREAS, the Charter requires that all money received or collected from or arising out of the operation of the Harbor and Harbor District lands be credited to the Harbor Revenue fund and that none of the money in the Harbor Revenue Fund shall be appropriated or used for any purpose except as specified in Section 145 of the Charter".

<u>Assessment of Practice</u>

Since R&P controls where the revenues are recorded, and there was no audit to determine if the revenue posting was correct, R&P claims that the revenues were not posted to the general fund should not be the only factor for consideration of compliance. In addition, because requested details were not provided, we are not able to ascertain whether R&P has complied with the MOU Page 2, Paragraph 3 requirement that the revenues should be posted to the Harbor Revenue fund and not used for other non MOU compliant purposes.

A requirement does appear to exist in MOU Article 8 (as cited above) that the revenues be utilized for operation and maintenance of Harbor facilities. R&P declined to provide documentation to assess whether the revenues were in fact utilized for the operation and maintenance of the Harbor facilities. Because we were not provided access to the revenue accounts, we cannot compute the revenue amounts pertaining to R&P's failure to credit the Harbor for non-parking lot revenue against Harbor operations and maintenance charges. As a result, R&P did not demonstrate complete compliance with the MOU.

<u>Recommendations</u>

4.1 R&P should provide information concerning all revenues it has received on Harbor properties for FY 2010 through the present. R&P should also provide information on how the expenditure of these funds complies with the MOU Article 8 provisions discussed above.

4.2 When requested by Harbor (or authorized auditors), R&P should provide requested information concerning the revenues it has received related to Harbor properties. R&P should also provide details on how these revenues were expended so that Harbor (or authorized auditors) can assess whether the MOU requirements discussed above are complied with.

Views of Responsible Officials

R&P contended that since non-parking revenues were not deposited in the general fund, there was no requirement that these other revenues be credited against billings to the Harbor.

Observation 5 – STTA Compliance Documentation for Labor Charges to Harbor from R&P

Observed Practice

R&P did not provide requested information concerning the nature of the services performed by R&P that resulted in the charging of labor costs to Harbor under STTA requirements. While R&P did provide timecards and support for labor rates for a sample of labor transactions, it should provide details on the nature of the work performed to demonstrate STTA compliance. Because the Harbor's assets are held in trust, and those trust assets are restricted by the STTA to certain uses, R&P has failed to demonstrate STTA compliance. R&P indicated that the only documentation that exists is that charge codes were established that provided a mechanism for employees to record time to charge codes that were specific to each of the Harbor properties.

Assessment of Practice

R&P did not demonstrate compliance with the STTA requirements that trust revenues can only be expended for certain specified purposes. Use of charge codes, without information concerning the services performed, does not appear to constitute sufficient documentation to ensure compliance with STTA requirements.

Recommendations

5.1 R&P should maintain and provide documentation concerning the nature of services it is providing to Harbor so that the Harbor can be certain that the activities billed by R&P to Harbor comply with the requirements of the STTA's requirements concerning specific allowable uses of trust funds.

Views of Responsible Officials

Although requested multiple time over a several month period, R&P contended that the requested documentation does not exist and that they are not required to provide this information in accordance with the MOU.

Observation 6 – Noncompliance with MOU Requirement to Perform Study At Least Every Five Years

Observed Practice

Review of Article 17 of the MOU indicated that the MOU requires that at least once every five years the parties jointly fund an independent study to determine if the services provided under the MOU are full, complete, accurate and consistent with applicable STTA principles. We determined that it has been over ten years since the last study.

Assessment of Practice

It appears that both R&P and Harbor are in noncompliance with the MOU requirement due to not having obtained an independent study within the last five years.

Recommendations

We recommend that a study be conducted as soon as possible to bring the parties into compliance with the MOU requirement.

Views of Responsible Officials

To be determined.

Observation 7 – Adjustments to R&P Billings

Observed Practice

We noted that for the period of FY 2013 and year-to-date for FY 2014, significant adjustments were made to R&P billing amounts by Harbor before issuing payment. A summary of the adjustments made is presented in Appendix E.

Assessment of Practice

The magnitude of adjustments necessary to billed amounts indicates that additional controls are needed on the part of R&P to ensure that billings are in accordance with Harbor's expectations.

Recommendations

We recommend that R&P review the reasons for adjustments made by Harbor to R&P billing amounts for FY 2013 and FY 2014 and consider modifications to its billing methods to alleviate the need for Harbor to make the adjustments to R&P billed amounts.

Views of Responsible Officials

To be determined.

APPENDIX A – LIST OF DOCUMENTS REVIEWED

The following documents were reviewed during the analysis (see the Objective, Scope and Methodology section):

- Monthly billings for services from the City's R&P Department to the Harbor Department from FY 2010 through FY 2013
- The Nexus MOU
- Listing of key personnel from the R&P Department involved with MOU compliance and billings to the Harbor with contact information
- Cost element detail in support of monthly billings
- Cost details and descriptions covering the City services component cost descriptions, including personnel costs for all staff providing services by cost center, the calculations of all administrative, overhead and benefit charges, as well as the cost allocation methodologies governing cost components
- Transaction detail in support of FY 2013 and YTD FY 2014 operations and maintenance costs in quarterly R&P cost billings to Harbor
- Policies, procedures and guidelines used by R&P to identify and exclude unallowable and unallocable cost from billings to the Harbor Department and prior consultant reports covering R&P billings to the Harbor
- Audited revenue amounts for FY 2013 for locations which are the subject of the R&P billings to the Harbor
- Non-CAP rates
- Indirect rates for Gross PT Salaries (which are not included in the CAP rates)
- Detail calculations of Department Administration, Central Services, and PT Fringe Benefit indirect rates for Gross PT Salaries for FY 2010 through FY 2014 (pool elements, base used, etc.)
- Transaction detail in support of FY 2013 and YTD FY 2014 operations and maintenance costs in quarterly R&P cost billings to the Harbor
- Labor Cost Reports
- Timesheets
- Timesheet variation codes billable to the Harbor

- List of changes that have occurred over time that impact the scope of the services being performed by R&P for the Harbor
- Quarterly labor cost reports
- Labor distribution reports – PDF and Excel versions
- Pay stubs
- Payroll calendar

APPENDIX B – CALCULATION OF COST IMPACT OF POTENTIAL DUPLICATION OF LABOR COSTS

The calculation of the cost impact for accountant and management analyst positions for FY 2013 and FY 2014 (including indirect costs using R&P indirect billing rates utilized on R&P billings to Harbor) follows:

Classification	Regular Hours	Salaries 2013	Salaries 2014	Total	Quarter
Accountant II	520.0	$16,301.48		$16,301.48	4
Accountant II	528.0		$16,839.84	$16,839.84	1
Accountant II	512.0		$15,024.83	$15,024.83	2
Management Analyst II	520.0	$18,850.00		$18,850.00	4
Management Analyst II	528.0		$19,425.12	$19,425.12	1
Management Analyst II	512.0		$20,147.20	$20,147.20	2
		$35,151.48	$71,436.99	$106,588.47	
FT Fringe		$26,166.76	$45,341.06	$71,507.82	
Central Services		$9,199.14	$15,487.54	$24,686.68	
Department Admin		$5,290.30	$30,603.61	$35,893.90	
Indirect Costs		$40,656.20	$91,432.20	$132,088.40	
Total Impact		**$75,807.68**	**$162,869.19**	**$238,676.87**	

APPENDIX C – CALCULATION OF COST IMPACT OF SHIFT FROM PT TO FT PERSONNEL

The impact of the shift from part time to full time personnel during FY 2012 and FY 2013 due to the difference in Fringe and Departmental Administration rates is computed as follows:

	FY 2012	FY 2013	Total
Decrease in PT as compared to FY 2010	$1,023,045	$789,450	$1,812,495
Difference in Fringe Rate	$ 444,206	$342,779	$ 786,985
Difference in Central Services	-	-	-
Difference in Departmental Admin Rate	4,399	3,395	7,794
Total Impact on Indirect Costs	$ 448,605	$346,174	$ 794,779
RATES			
FT Fringe	52.35%	52.35%	
PT Fringe	8.93%	8.93%	
Difference	43.42%	43.42%	
FT CS	28.32%	28.32%	
PT CS	28.32%	28.32%	
Difference	0.00%	0.00%	
FT DA	12.21%	12.21%	
PT DA	11.78%	11.78%	
Difference	0.43%	0.43%	

Note: The indirect rates utilized to determine the cost impact were those found in the City of LA Cost Allocation Plan (CAP) 32. These were the rates which R&P used to bill for seven of the eight quarters analyzed above. R&P used CAP 35 for the last quarter of 2013, but it was determined that identifying the specific cost impact for that quarter with the CAP 35 rates would not result in a significantly different result, and therefore, in the interest of time, CAP 32 rates were utilized for the analysis.

APPENDIX D – RECONCILIATION OF LABOR COSTS

The results of the reconciliation of R&P provided labor reports to labor billed to Harbor for Q3 2013 through Q2 2014 follows:

	Aquarium (7780)				Bath House (2832 + 6645)			
	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2013	Q4 2013	Q1 2014	Q2 2014
Gross Salaries per Billing	$ 662,702.07	$ 443,927.00	$ 713,301.05	$ 665,153.35	$ 45,364.08	$ 32,362.67	$ 48,419.11	$ 50,334.47
Gross Salaries per Labor Report	803,033.02	494,810.68	648,508.04	601,558.65	59,958.77	48,791.54	52,138.12	50,334.47
Difference	$ (140,330.95)	$ (50,883.68)	$ 64,793.01	$ 63,594.70	$ (14,594.69)	$(16,428.87)	$ (3,719.01)	$ -

	Museum (2811 + 2834 + 7740)				Parking			
	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2013	Q4 2013	Q1 2014	Q2 2014
Gross Salaries per Billing	$ 95,492.89	$ 85,069.00	$ 87,133.52	$ 84,042.99	$ 56,314.89	$ 13,407.00	$ 84,947.80	$ 63,690.25
Gross Salaries per Labor Report	171,143.06	128,550.53	168,736.78	162,724.24	-	60,256.79	84,862.24	63,690.67
Difference	$ (75,650.17)	$(43,481.53)	$(81,603.26)	$(78,681.25)	$ 56,314.89	($ 46,849.79)	$ 85.56	($ 0.42)

	Lifeguards (4520)				Lighthouse (2838 + 7770)			
	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2013	Q4 2013	Q1 2014	Q2 2014
Gross Salaries per Billing	$ 155,532.63	$ -	$233,593.50	$152,163.13	$ 25,923.27	$ 39,351.00	$ 27,793.94	$ 26,087.67
Gross Salaries per Labor Report	155,532.63	213,357.17	233,593.50	152,163.13	36,578.72	36,904.19	39,318.10	37,428.82
Difference	$ -	$ (213,357.17)	$ -	$ -	$ (10,655.45)	$ 2,446.81	$(11,524.16)	$(11,341.15)

	Beach Maintenance (2812)				Wilders (2850)			
	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2013	Q4 2013	Q1 2014	Q2 2014
Gross Salaries per Billing	$ 11,326.79	$ 21,261.00	$ 9,300.72	$ 13,652.32	$ 12,615.42	$ 12,615.43	$ 13,242.90	$ 12,640.95
Gross Salaries per Labor Report	14,971.99	12,291.20	9,300.72	13,652.32	12,615.42	12,615.43	13,242.90	12,640.95
Difference	$ (3,645.20)	$ 8,969.80	$ -	$ -	$ -	$ -	$ -	$ -

	All Locations			
	Q3 2013	Q4 2013	Q1 2014	Q2 2014
Gross Salaries per Billing	$1,065,272.04	$ 647,993.10	$1,217,732.54	$1,067,765.13
Gross Salaries per Labor Report	1,253,833.61	1,007,577.53	1,249,700.40	1,094,193.25
Difference	$(188,561.57)	$(299,327.64)	$ 52,894.38	($ 26,428.12)
Grand Total of Differences	**$ (606,541.98)**			

APPENDIX E – ADJUSTMENTS TO R&P BILLING AMOUNTS

A summary of Harbor adjustments to R&P billing amounts for FY 2013 and FY 2014 (with estimated amounts for the last quarter of FY 2014) is presented as follows:

	Q1 2013 (Jul-Sep 2012)	Q2 2013 (Oct-Dec 2012)	Q3 2013 (Jan-Mar 2013)	Q4 2013 (Apr-Jun 2013)	Total FY 2013
Billed to Harbor	$2,445,179	$2,414,298	$2,388,381	$2,328,696	$9,576,553
Paid to R&P	1,706,525	1,780,094	1,950,937	1,801,003	7,238,558
Variance	**$738,654**	**$634,204**	**$437,445**	**$527,693**	**$2,337,995**
Variance Explained					
Cabrillo Outer Beach	($82,906)	($82,791)	($97,073)	($84,739)	($347,510)
Gaffety Street - Green Belt	-	-	-	(1,060)	(1,060)
PT/FT Cabrillo Aquarium	(75,804)	(167,303)	-	-	(243,107)
PT/FT Cabrillo Lifeguard	(82,094)	(57,178)	-	-	(139,272)
Labor and facility cost	0	0	0	(39,477)	(39,477)
Parking receipts	(247,786)	(76,867)	(90,307)	(152,352)	(567,313)
Credit for Harbor Property	(120,699)	(120,699)	(120,699)	(120,699)	(482,794)
Nexus Credit	(129,366)	(129,366)	(129,366)	(129,366)	(517,463)
Variance Explained	**($738,654)**	**($634,204)**	**($437,445)**	**($527,693)**	**($2,337,995)**

	Q1 2014 (Jul-Sep 2013)	Q2 2014 (Oct-Dec 2013)	Q3 2014 (Jan-Mar 2014)	ESTIMATED Q4 2014* (Apr-Jun 2014)	Total FY 2014
Billed to Harbor	$2,494,801	$2,244,743	$2,427,961	$2,392,008	$9,559,512
Paid to R&P	1,929,280	1,850,387	1,924,374	1,848,943	7,552,984
Variance	**$565,521**	**$394,355**	**$503,587**	**$543,066**	**$2,006,529**
Variance Explained					
Cabrillo Outer Beach	($134,752)	($88,720)	($94,820)	($95,114)	($413,406)
Gaffety Street - Green Belt	(974)	(974)	(948)	(565)	(3,460)
PT/FT Cabrillo Aquarium	-	-	-	(34,730)	(34,730)
PT/FT Cabrillo Lifeguard	-	-	-	(19,896)	(19,896)
Labor and facility cost	-	-	-	(5,640)	(5,640)
Parking receipts	(179,731)	(54,597)	(157,756)	(137,057)	(529,141)
Credit for Harbor Property	(120,699)	(120,699)	(120,699)	(120,699)	(482,794)
Nexus Credit	(129,366)	(129,366)	(129,366)	(129,366)	(517,463)
Variance Explained	**($565,521)**	**($394,355)**	**($503,587)**	**($543,065)**	**($2,006,529)**

*The Department of Recreation and Parks had not issued to POLA an actual invoice for the fourth quarter of Fiscal Year 2014 as of the date of audit fieldwork. The amounts shown in the fourth quarter of Fiscal Year 2014 are averages of the prior seven quarters by line item.