



November 9, 2010

Mr. Larry Greene, Executive Director
Sacramento Metropolitan Air Quality Management District
777 12th Street, Third Floor
Sacramento, CA 95814

Dear Mr. Greene:

Final Report—Fiscal Review of the Sacramento Metropolitan Air Quality Management District's Carl Moyer Program, Lower-Emission School Bus Program, and AB 923 Funds

The Department of Finance, Office of State Audits and Evaluations, has completed its fiscal review of the Sacramento Metropolitan Air Quality Management District's (District) Carl Moyer Program, Lower-Emission School Bus Program, and AB 923 funds for the period July 1, 2005 through December 31, 2009.

The enclosed report is for your information and use. The District's response to the report findings and our evaluation of the response are incorporated into this final report. In accordance with Finance's policy of increased transparency, this report will be placed on our website.

We appreciate the assistance and cooperation of your staff and management during our review. If you have any questions, please contact Cheryl McCormick, Manager, or James Kong, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

David Botelho, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: On following page

cc: Mr. Mark Loutzenhiser, Land Use/Mobile Source Program Supervisor, Sacramento
Metropolitan Air Quality Management District
Mr. Mike Neuenburg, Program Coordinator, Sacramento Metropolitan Air Quality
Management District
Mr. Scott Rowland, Branch Chief, Air Resources Board
Ms. Heather Arias, Manager, Air Resources Board
Mr. Charles Kersey, Manager, Air Resources Board
Ms. Laura Zaremba-Schmidt, Engineer, Air Resources Board

Sacramento Metropolitan Air Quality Management District
Carl Moyer Program
Lower-Emission School Bus Program
Assembly Bill 923

Prepared By:
Office of State Audits and Evaluations
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Final reports are available on our website at <http://www.dof.ca.gov>

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BACKGROUND, SCOPE, AND METHODOLOGY

Background

The Sacramento Metropolitan Air Quality Management District (District) was created in 1996 under Health and Safety Code sections 40960-40963. The District's mission is to achieve clean air goals by leading the region in protecting public health and the environment through innovative and effective programs, dedicated staff, community involvement, and public education. The District works in conjunction with the California Air Resources Board (Board) in achieving its clean air goals. The Board authorizes grant awards to the District and provides guidance and oversight for the Carl Moyer Program (CMP) and the Lower-Emission School Bus Program (LESBP). The Board also reviews the use of Assembly Bill 923 (AB 923) funds for match projects supporting the CMP.

The CMP objective is to contribute to cleaner air by funding the incremental cost of replacing or retrofitting older engines with cleaner-than-required engines and equipment. Public or private entities that operate eligible engines or equipment within the local air district's jurisdiction participate by applying for a grant. Eligible engines and equipment include heavy-duty vehicles, marine applications, locomotives, agricultural pumps, forklifts, and auxiliary power units. The Multi-District portion of the CMP provides incremental cost funding for projects operating in more than one local air district. The Board is authorized to reserve 10 percent of CMP funds to finance multi-district projects. CMP administration grant funds are provided to local air districts to fund costs associated with program implementation tasks outlined in the CMP Guidelines.

Local air districts participating in the CMP are required to provide \$1 in match funding for every \$2 of CMP funding awarded by the Board with a cap on statewide match funds of \$12 million. Match fund sources may include AB 2766 and AB 923 funds.

The primary goal of the LESBP is to reduce school children's exposure to cancer-causing and smog-forming pollution. The LESBP achieves this goal by funding the replacement of older high-polluting school buses with new buses and the installation of Board-approved pollution control devices on diesel school bus engines.

The Board advances CMP funds and LESBP funds to the local air districts. The interest income on these funds must be reported to the Board and used to fund projects that meet the respective current program guidelines. The local air districts are required to track interest and fund eligible projects.

AB 923 (Chapter 707, Statutes of 2004) provided two additional sources of funding for the CMP. AB 923 adjusted fees assessed on purchasers of new tires and provided air district governing boards with the authority to approve a \$2 increase in motor vehicle registration fees. These fees provide additional funding to local air districts for four incentive programs: (1) the CMP, (2) the LESBP's Replacement Program, (3) light-duty accelerated vehicle retirement or repair programs, and (4) the Agricultural Assistance Program.

Scope

In accordance with an interagency agreement with the Board, the Department of Finance, Office of State Audits and Evaluations, conducted a fiscal review of the District's administration of the CMP, LESBP, and AB 923 funds for the period July 1, 2005 through December 31, 2009.

The review objective was to determine whether the District administered the CMP, LESBP, and AB 923 funds in accordance with applicable laws, regulations, guidelines, and contract requirements. The AB 923 fund review was limited to a compilation of receipts, interest earnings, and expenditures.

Concurrent to our review, the Board conducted a program audit of the CMP, LESBP, and AB 923 funds. Because of this, we did not verify the programmatic validity of the funds.

Methodology

To determine whether the CMP, LESBP, and AB 923 funds were administered in compliance with applicable laws, regulations, guidelines, and contract requirements, we performed the following procedures:

- Interviewed key personnel to obtain an understanding of the programs and accounting processes for receiving, recording, and disbursing funds; allocating administrative costs and earned interest; and meeting match funding requirements.
- Examined program files maintained by the District, the grant agreements, and applicable policies and procedures.
- Reviewed the District's accounting records, vendor invoices, payroll records, and bank statements.
- Selected a sample of expenditures to determine if costs were allowable, grant-related, incurred within the grant period, supported by accounting records, and properly recorded.
- Performed site visits to interview program participants and review pertinent documents ensuring program applicants maintain the appropriate supporting documentation for their project expenditures.
- Compiled schedules summarizing program funds received and disbursed for the period July 1, 2005 through December 31, 2009. See Appendices A, B, and C.

The results of the review are based on our evaluation of documentation, other information made available to us, and interviews with the staff directly responsible for administering the funds. The review was conducted from February 2010 through June 2010.

Our review included Carl Moyer Program (CMP) regular, multi-district, administration, match, and earned interest funds; Lower-Emission School Bus Program (LESBP) retrofit and replacement, and earned interest funds; and Assembly Bill 923 (AB 923) funds. As described below, except as noted in the observations, the District's administration of the CMP, LESBP, and AB 923 funds was in compliance with applicable laws, regulations, guidelines, and contract requirements. Schedules detailing the receipts and expenditures during program years 8 through 11 are illustrated in Appendices A, B, and C.

CMP

Regular and Multi-District

The CMP regular and multi-district funds were administered in compliance with applicable laws, regulations, guidelines, and contract requirements, except as noted in Observation 1. We identified funds expended after the respective grant periods for years 8 and 9 totaling \$3,646,145. Additionally, as noted in Observation 3, we identified areas where the District could improve its payment processes. See Appendix A, Schedule 1.

Administration

The CMP administration funds were managed in compliance with applicable laws, regulations, guidelines, and contract requirements, except as noted in Observations 1 and 2. We identified year 8 funds totaling \$24,998 that were not expended by the end of the grant period. However, year 9 funds had been fully expended as of December 31, 2009 and years 10 and 11 unexpended funds remain eligible for expenditure through the end of their respective grant periods. Additionally, the District's administration expenditures included staff salaries totaling \$539,634 for which the allocation rates were not fully documented. See Appendix A, Schedule 2.

Match Funds

The District fully met the match requirements for years 8, 9, and 11 by completing eligible projects funded with local-control funds. As of December 31, 2009, the District had a remaining year 10 match requirement of \$98,745. However, the District used staff salaries totaling \$161,215 as in-kind match for which the allocation rates were not fully documented, as described in Observation 2. See Appendix A, Schedule 3.

Earned Interest

The District's interest calculation methodology is appropriate and allocations are materially correct and properly recorded. As of December 31, 2009, the District used \$476,916 of earned interest to fund CMP eligible projects; \$480,765 of interest earnings remained unexpended. See Appendix A, Schedule 4.

LESBP

Retrofit and Replacement

The LESBP retrofit and replacement funds were administered in compliance with applicable laws, regulations, guidelines, and contract requirements. The LESBP was not funded during fiscal year 2006-07. As of December 31, 2009, \$16,170,000 of LESBP funds remained unexpended. See Appendix B, Schedule 1.

Earned Interest

The District's interest calculation methodology is appropriate and allocations are materially correct and properly recorded. As of December 31, 2009, the District had expended \$41,637 of earned interest on eligible projects; \$2,140 of interest earnings remained unexpended and \$10,174 had been returned to ARB. See Appendix B, Schedule 2.

AB 923

We compiled a schedule of AB 923 funds from the District's internal summary schedules. The compilation depicts funds received and expended during the period July 2005 through December 2009. See Appendix C, Schedule 1. We relied on the expenditures and administration charges as reported in the District's summary schedules and did not perform testing to validate the amounts reported. The District expended \$4,163,307 on projects, and \$89,700 expended on administration charges (up to 5 percent of collections) was appropriate as allowed by statute. As of December 31, 2009, \$5,886,204 remained unexpended.

Our review of the District's compliance with Carl Moyer Program (CMP) and Lower-Emission School Bus Program (LESBP) funds' fiscal requirements disclosed the following observations:

Observation 1: Grant Funds Expended or Retained after the Grant Period

As shown in Appendix A, Schedule 1, CMP regular and multi-district funds totaling \$3,646,145 were expended after the respective grant periods. Specifically, year 8 regular and multi-district expenditures totaling \$93,242 and \$2,475,000, respectively, were issued after June 30, 2008. Year 9 regular and multi-district expenditures totaling \$1,019,532, and \$58,371, respectively, were issued after June 30, 2009. While these payments were for valid projects, the claims were not approved for payment within the respective grant periods as required by statute.

Additionally, as of December 31, 2009, year 8 administration funds totaling \$24,998 remained unexpended. These funds should have been expended no later than June 30, 2008. See Appendix A, Schedule 2.

Health and Safety Code section 44287(k), states, "Any funds reserved for a district pursuant to this section are available to the district for a period of not more than two years from the time of reservation. Funds not expended by June 30 of the second calendar year following the date of the reservation shall revert back to the state board as of that June 30..."

Recommendation:

Ensure projects are completed and funds expended within the respective grant periods. Final determination as to the treatment of the unexpended funds and funds expended outside the grant period will be made by the Board.

Observation 2: Allocation Rates Inadequately Documented

District rates allocating staff salaries to CMP administration and in-kind match were not adequately documented. The District's rates are based on workload estimates of time spent on CMP related activities. However, the estimates used to determine a particular staff's allocation rate were not documented. As such, we performed analytical procedures and determined the allocated amounts were reasonable. The following table depicts District salaries allocated in relation to the total expenditures incurred.

Table 1: Staff Salaries Allocation

CMP Year	Expenditures Within Grant Period	District Salaries Allocated	Percent
<i>CMP Administration</i>			
8	\$ 126,833	\$ 20,275	16%
9	391,198	390,323	99%
Multi-District	129,036	129,036	100%
Total		\$ 539,634	
<i>CMP Match</i>			
8	\$ 1,029,548	\$ 125,000	12%
9	936,612	36,215	4%
Total		\$ 161,215	

CMP Guidelines Part 3, section 14(c), requires Districts to maintain documentation of CMP funds used for administration and outreach and includes specified personnel documentation requirements. Additionally, section 12(a) (4) requires District in-kind match funds to meet the documentation requirements identified in Section 14.

Recommendation:

Document and retain the methodology for allocating staff salary expenditures, including the rate calculation.

Observation 3: Payment Process Needs Improvement

During CMP project testing, we identified two District payments that exceeded actual costs incurred by two program participants. The District paid the approved contract amount instead of the vendor invoice amounts. One invoice was overpaid by \$4,501 and three invoices were overpaid by a total of \$501. The discrepancies between the approved payments and the invoices were not detected by the District's review and approval process.

Additionally, we identified two overpayments during our CMP site visits. One program participant submitted vendor estimates for reimbursement instead of vendor invoices. Because the District did not require other proof of payment, the District inadvertently paid the estimate, which was \$19,460 more than the actual costs incurred. The second overpayment pertained to a program participant who acquired and installed their CMP equipment. This participant prepared and submitted internally generated invoices instead of vendor invoices. The submitted invoices included a markup on the equipment cost and the equipment installation labor hours charged exceeded the actual hours spent. In total, this program participant overcharged the District \$13,987.

An adequate system of internal control should ensure only valid and accurate payments are processed.

Recommendations:

- A. Strengthen the payment review and approval procedures to ensure payments do not exceed the obligated amounts.
- B. Request documentation such as cancelled checks to validate reimbursement requests prior to issuing payment.

APPENDIX A

Schedules 1 through 4 illustrate Carl Moyer Program (CMP) regular and multi-district, administration, match, and earned interest funds.

Schedule 1: CMP Regular and Multi-District Funds

CMP Year	Fiscal Year	Award Amount	Expenditures Within Grant Period	Balance as of End of Grant Period ¹	Expenditures After Grant Period	Balance as of December 31, 2009
8	2005-06	\$ 6,559,105	\$ 6,465,863	\$ 93,242	\$ 93,242	\$ 0
8 Multi-District	2005-06	2,475,000	0	2,475,000	2,475,000	0
9	2006-07	5,728,920	4,709,388	1,019,532	1,019,532	0
9 Multi-District	2006-07	2,080,728	1,733,712	347,016	58,371	288,645
10	2007-08	5,471,205	598,271	n/a	0	4,872,934
10 Multi-District	2007-08	4,420,028 ²	0	n/a	0	4,420,028
11	2008-09	4,789,919	0	n/a	0	4,789,919
11 Multi-District	2008-09	697,582 ³	0	n/a	0	697,582
Total		\$32,222,487	\$13,507,234	\$3,934,790	\$3,646,145	\$15,069,108

- (1) Year 8 grant period ended June 30, 2008; Year 9 grant period ended June 30, 2009; Year 10 grant period ended June 30, 2010; Year 11 grant period ends June 30, 2011.
- (2) The District received \$3,467,170 of the year 10 multi-district funds as of December 31, 2009
- (3) Year 11 multi-district funds had not been received as of December 31, 2009.

Schedule 2: CMP Administration Funds

CMP Year	Fiscal Year	Administration Funds Awarded	Expenditures Within Grant Period ⁴	Administration Balance as of December 31, 2009
8	2005-06	\$ 151,831	\$ 126,833	\$ 24,998 ⁶
9	2006-07	391,198	391,198	0
9 Multi-District	2006-07	129,036	129,036	0
10	2007-08	374,210	127,836	246,374
10 Multi-District	2007-08	223,501	0	223,501
11	2008-09	331,085	0	331,085
11 Multi-District	2008-09	49,180 ⁵	0	49,180
Total		\$1,650,041	\$ 774,903	\$ 875,138

- (4) Year 8 grant period ended June 30, 2008; Year 9 grant period ended June 30, 2009; Year 10 grant period ended June 30, 2010; Year 11 grant period ends June 30, 2011.
- (5) Year 11 multi-district administration funds had not been received as of December 31, 2009.
- (6) Year 8 funds should have been expended by June 30, 2008.

Schedule 3: CMP Match Funds

CMP Year	Fiscal Year	Required District Match	Match Expenditures Within Grant Period ⁷	Remaining Match Requirement as of December 31, 2009
8	2005-06	\$1,029,364	\$1,029,548	\$ 0
9	2006-07	882,515	936,612	0
10	2007-08	902,070	803,325	98,745
11	2008-09	911,860	1,184,391	0
Total		\$3,725,809	\$3,953,876	\$ 98,745

- (7) Year 8 grant period ended June 30, 2008; Year 9 grant period ended June 30, 2009; Year 10 grant period ended June 30, 2010; Year 11 grant period ends June 30, 2011.

Schedule 4: CMP Earned Interest

CMP Year	Fiscal Year	Interest Earned	Expenditures ⁸	Balance as of December 31, 2009
8	2005-06	\$ 239,158	\$ 239,158	\$ 0
8 Multi-District	2005-06	198,631	198,631	0
9	2006-07	325,458	39,127	286,331
9 Multi-District	2006-07	137,417	0	137,417
10	2007-08	29,226	0	29,226
10 Multi-District	2007-08	21,947	0	21,947
11	2008-09	5,844	0	5,844
Total		\$ 957,681	\$ 476,916	\$ 480,765

- (8) Year 8 grant period ended June 30, 2010; Year 9 grant period ends June 30, 2011; Year 10 grant period ends June 30, 2012; Year 11 grant period ends June 30, 2013.

APPENDIX B

Schedules 1 and 2 illustrate Lower-Emission School Bus Program (LESBP) retrofit and replacement, and earned interest funds.

Schedule 1: LESBP Retrofit and Replacement Funds

Fiscal Year	Program	Project Award Amount	Administration Award Amount	Expenditures as of December 31, 2009	Award Balance as of December 31, 2009
2005-06	Retrofit	\$ 515,600	\$ 0	\$ 515,600	\$ 0
2007-08	Replacement	16,170,000 ¹	0	0	16,170,000 ²
2008-09	Retrofit	70,680	5,320	76,000	0
Total		\$16,756,280	\$ 5,320	\$ 591,600	\$16,170,000

(1) The District received \$840,000 in fiscal year 2007-08 LESBP funds as of December 31, 2009.

(2) The District has until June 30, 2012 to expend the funds.

Schedule 2: LESBP Earned Interest

Fiscal Year	Interest Earned	Expenditures	Interest Funds Returned	Ending Balance as of December 31, 2009
2005-06	\$ 51,811	\$ 41,637	\$ 10,174	\$ 0
2007-08	1,934	0	0	1,934 ³
2008-09	206	0	0	206 ⁴
Total	\$ 53,951	\$ 41,637	\$ 10,174	\$ 2,140

(3) The District has until June 30, 2012 to expend the fiscal year 2007-08 earned interest.

(4) Per the United States Environmental Protection Agency, the fiscal year 2008-09 earned interest is not required to be returned.

APPENDIX C

Schedule 1 illustrates Assembly Bill 923 (AB 923) funds.

Schedule 1: AB 923 Fund Compilation

Total Receipts July 2005 Through December 31, 2009 ¹	Total Expenditures Through December 31, 2009	Administration Charges	Balance as of December 31, 2009 (Excluding Interest)	Earned Interest Through December 31, 2009	Balance as of December 31, 2009 (Including Interest)
\$9,789,824	\$4,163,307	\$ 89,700	\$5,536,817	\$ 349,387	\$5,886,204

(1) Receipts based on fee collections beginning in May 2005

Larry Greene, Executive Director

October 18, 2010

Department of Finance
Office of State Audits and Evaluations
300 Capital Mall, Suite 801
Sacramento, California 95814

Dear Mr. David Botelho, CPA:

The 2010 audit conducted by the Department of Finance (DOF) of our Carl Moyer Program, Lower-Emission School Bus Program, and AB 923 identified three areas of observation as part of the draft final report. We appreciate the insights provided by your audit team because these Programs are something our District has always been very proud of, in part because Moyer was first implemented here. I have a very progressive staff managing this program and they are in the process of looking at ways to improve the process based on your team's observations.

Observation 1: Grant Funds Expended or Retained after the Grant Period. Regarding this observation, the District acknowledges that DOF and the Air Resources Board (ARB) use different definitions of "expended." The District has met the ARB Moyer definition of expended for the time frames in question.

Moyer Guidelines Part 3, section 18 (b) ".... Funds are considered expended when an invoice for that project has been fully or partially paid by the air district and the invoice payment also meets the conditions identified in section 18 (c), below."

In the case of the referenced years, the District has ensured that at least a partial payment was made on all necessary contracts to ensure that funds were expended pursuant to the Moyer Guidelines. The District will continue to push project to completion as quickly as possible though in order to avoid to the extent possible questions arising from the definition of expended.

Observation 2: Allocation Rates Inadequately Documented. The District will develop a more robust and complete explanation of the employee time allocation rates and maintain that information on file.

Observation 3: Payment Process Needs Improvement. During the audit, DOF identified 2 payments exceeding the actual costs and 2 payments where the participant over billed the District. Regarding the payments exceeding actual costs, the District contacted and has received repayment for each exceedance. In addition, the District has added an additional check and balance system within our database to ensure that contract payments do not exceed the actual amounts. The participants who overbilled the District have also been contacted regarding the over charges. At this time one has made repayment and the second is out of business but is being pursued for overall breach of contract. The District is investigating means of ensuring only invoices marked and certified as final are processed toward repayment. We

will continue to investigate these types of issues to ensure that only proper repayments to participants are made.

The District has always had a strong commitment to the success of the Carl Moyer, School Bus, and AB923 Programs. With the substantial funding amounts currently available for eligible projects, the benefits of this program will be enhanced for many years to come. We look forward to working with you and your staff in the future.

Sincerely,

Larry Greene
Executive Director/Air Pollution Control Officer

Original signed by:

cc: Tim Taylor
Mark Loutzenhiser
Scott Rowland, Branch Chief, Air Resources Board

EVALUATION OF RESPONSE

The District's response to our draft report has been incorporated herein. We acknowledge the District's timely reply and willingness to implement corrective actions for the identified observations. Upon review of the District's response, we provide the following comments:

Observation 1: Grant Funds Expended or Retained after the Grant Period

The District indicates that for the years in question, "...the District has ensured at least a partial payment was made on all necessary contracts to ensure that funds were expended pursuant to the Moyer Guidelines." The Moyer Guidelines the District refers to is Part 3, section 18(b), which states, in part, "Funds are considered expended when an invoice for that project has been fully or partially paid by the air district...."

The District further acknowledged the Health and Safety code also applies to expenditures. The Health and Safety Code states any funds reserved for a district are available for expenditure for a period not to exceed two years from the time of reservation. Funds not expended by that date shall revert back to the Board. As such, the District has two years from reservation to expend the program funds, in their entirety. Our audit disclosed that funds were not expended by the District within the specified timeframes. Therefore, our observation and recommendation remains unchanged.

Observation 2: Allocation Rates Inadequately Documented

We concur with the District's response.

Observation 3: Payment Process Needs Improvement

The District states it has added an additional check and balance system to ensure contract payments do not exceed the actual amounts. Additionally, the District is investigating means of ensuring only invoices marked and certified as final are processed toward repayment.

We commend the District on its plans to comply with our recommendations; however, we reiterate and encourage the District to request supporting documentation such as canceled checks to validate reimbursement requests prior to issuing payment.