



Transmitted via e-mail

February 15, 2017

Mr. Samuel Schuchat, Executive Officer  
State Coastal Conservancy  
1330 Broadway, 13<sup>th</sup> Floor  
Oakland, CA 94612-2530

Dear Mr. Schuchat:

**Final Report—The River Project, Proposition 84 Grant Audit**

The Department of Finance, Office of State Audits and Evaluations, has completed its audit of The River Project's (TRP) grant 11-075 issued by the State Coastal Conservancy.

The enclosed report is for your information and use. TRP's response to the report findings is incorporated into this final report. TRP disagreed with our findings; however, because TRP did not provide additional supporting documentation, the findings and recommendations remain unchanged. This report will be placed on our website.

We appreciate the assistance and cooperation of TRP. If you have any questions regarding this report, please contact Susan Botkin, Manager, or Fabiola Torres, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

Jennifer Whitaker, Chief  
Office of State Audits and Evaluations

Enclosure

cc: Ms. Mary Small, Deputy Executive Officer, State Coastal Conservancy  
Ms. Regine Serrano, Chief of Administrative Services, State Coastal Conservancy  
Ms. Amy Hutzel, Deputy Executive Officer, State Coastal Conservancy  
Ms. Melanie Winter, Director, The River Project  
Mr. Patrick Kemp, Assistant Secretary for Administration and Finance, California Natural Resources Agency  
Ms. Julie Alvis, Deputy Assistant Secretary, California Natural Resources Agency  
Mr. Bryan Cash, Deputy Assistant Secretary, California Natural Resources Agency

# AUDIT REPORT

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## The River Project Proposition 84 Bond Program Grant Agreement 11-075

Prepared By:  
Office of State Audits and Evaluations  
Department of Finance

## **MEMBERS OF THE TEAM**

Susan Botkin, CGFM  
Manager

Fabiola Torres  
Supervisor

Staff  
Randy Enriquez  
Kerri Nelson  
Amanda Voie

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

You can contact our office at:

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

# BACKGROUND, SCOPE AND METHODOLOGY

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## BACKGROUND

California voters approved the Safe Drinking Water, Water Quality and Supply, Flood Control, River and Coastal Protection Bond Act of 2006 (Proposition 84). The \$5.4 billion of bond proceeds finance a variety of natural resource programs.

The State Coastal Conservancy (Conservancy), pursuant to Chapter 5.5 of Division 21 of the Public Resources Code, is authorized to undertake projects that protect and restore coastal watersheds and coastal and marine habitats in order to improve and protect coastal and marine water quality. The Conservancy may undertake projects directly or may award grants for these purposes in consultation with the State Water Resources Control Board and regional water quality control boards.

The Conservancy awarded a \$714,600 grant to The River Project (TRP) to implement portions of the Tujunga/Pacoima Watershed Management Plan, adopted by the Conservancy on January 19, 2012, by completing the Los Angeles Rainwater Harvesting Project (Water LA) for water quality and conservation purposes. TRP implemented the Water LA project to facilitate widespread implementation of residential storm water harvesting in the City of Los Angeles (City). TRP is a non-profit 501(c)(3) organization dedicated to natural resource protection, conservation, and enhancement. TRP's mission is to encourage responsible planning and management of the lands, working toward living rivers nourished by healthy watersheds for the social, economic, and environmental benefit of the City's communities.<sup>1</sup>

## SCOPE

Per the request of the Conservancy and in accordance with the Department of Finance's bond oversight responsibilities, we audited grant 11-075 for the period April 23, 2012 through September 30, 2014.

The audit objective was to determine whether TRP's grant expenditures claimed were eligible for reimbursement under the terms of the grant agreement. We did not assess the efficiency or effectiveness of program operations.

TRP management is responsible for ensuring accurate financial reporting and compliance with applicable laws, regulations, and grant requirements. The Conservancy and the California Natural Resources Agency are responsible for the state-level administration of the bond program.

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<sup>1</sup> Excerpts from The River Project website [www.theriverproject.org](http://www.theriverproject.org)

## METHODOLOGY

To determine whether grant expenditures were eligible for reimbursement, we performed the following procedures:

- Examined the grant files, grant agreement, project work plan and budget.
- Interviewed TRP's Director.
- Reviewed TRP's accounting records, sub-contractor and vendor invoices, bank statements, cancelled checks, and other relevant expenditure documentation.
- Selected a sample of claimed expenditures and determined whether they were grant related, incurred within the grant period, and supported by the accounting records. For example:
  - Labor:
    - Obtained and reviewed TRP's Labor Hour Excel Spreadsheet (spreadsheet) for each reimbursement period.
    - Performed an analytical procedure comparing the labor hours reported on the spreadsheet and the labor hours claimed on the reimbursement claims.
    - Obtained and reviewed Form 1099 (Miscellaneous Income) Vendor (1099 Vendor) reports for years 2012 through 2014. Performed an analytical procedure comparing the labor costs claimed and the income reported as paid to vendors on the 1099 Vendor reports.
  - Overhead:
    - Examined the Conservancy's General Budget Guidelines for Nonprofits.
    - Reviewed TRP's Profit and Loss by Job report for the period April 2012 through September 2014, rental rate cost allocation methodology, invoices, receipts, and other relevant expenditure documentation.
  - Contractor Expense:
    - Reviewed contracts, approved pay rates, invoices, bank statements, and cancelled checks.
    - Confirmation letters were sent to all contractors still in business to verify payments received from TRP.
- Evaluated whether other revenue sources were used to reimburse expenditures claimed for reimbursement under the grant agreement.

In conducting our audit, we obtained an understanding of TRP's internal controls, including any information systems controls that we considered significant within the context of our audit objectives. We assessed whether those controls were properly designed and implemented. Any deficiencies in internal control that were identified during our audit and determined to be significant within the context of our audit objectives are included in this report.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Except as noted below, the grant expenditures claimed by TRP were eligible for reimbursement under the terms of the grant agreement. The Schedule of Claimed and Unallowable Costs is presented below.

**Table 1: Schedule of Claimed and Unallowable Costs**

<b>Grant Agreement 11-075</b>		
<b>Expenditure Category</b>	<b>Claimed</b>	<b>Unallowable</b>
Materials and Equipment	\$ 52,514	\$ 0
Labor	383,999	383,999
Overhead	47,779	47,779
Sub-Contractor	230,342	2,178
<b>Total Project Expenditures</b>	<b>\$ 714,634</b>	<b>\$ 433,956</b>

**Finding 1: Unallowable Costs**

Costs totaling \$433,956 stemming from unsupported and misclassified labor costs, ineligible overhead costs, and unpaid contractor expenditures are unallowable for reimbursement as follows:

- TRP incorrectly claimed consultant services costs as labor costs. Additionally, TRP could not provide documentation to show the costs were project related. Specifically, TRP was unable to provide time and attendance (timesheets) to support the labor hours claimed. The costs claimed as labor were provided by independent consultants and therefore not labor costs but consultant services. Further, TRP did not enter into written contracts with the independent consultants. Without a contract that clearly defines the scope of work, allowable and unallowable costs, a current fee schedule, and final deliverable, there is an increased risk that expenditures will not be in compliance with grant agreement requirements. Moreover, TRP did not maintain adequate supporting documentation to provide an audit trail that permits tracing from support documentation to the accounting records and to the reimbursement claims. As a result, claimed costs totaling \$383,999 are deemed unsupported and unallowable for reimbursement.

TRP stated it has no policies and procedures for identifying expenditure categories and no formal timekeeping policies that require time and attendance reports for all individuals who are compensated or reimbursed under the grant for the work they performed. Without time and attendance reports, TRP cannot ensure claimed costs are allowable, grant-related, and supported by accounting records.

As alternative procedures to determine reasonableness of labor hours and labor expenditures claimed, we performed analytics as described in the Methodology

section of the report; however, the results of those analytical procedures did not corroborate the labor costs claimed to the grant.

- Per the grant project budget, overhead is a function of labor costs and is calculated as a percentage of labor costs. As a result of the unsupported and misclassified labor costs claimed, overhead costs totaling \$47,779 are ineligible for reimbursement.
- TRP claimed and was reimbursed for contractor expenditures that were not incurred. Specifically, TRP claimed \$2,178 for a contractor invoice and was paid by the State Coastal Conservancy (Conservancy); however, due to a dispute between TRP and the contractor over the work completed, the contract was terminated and TRP did not pay the invoice. Further, TRP did not inform the Conservancy of the issue or return the funds to the Conservancy. As a result, \$2,178 is deemed unallowable for reimbursement.

Grant agreement section Audits/Accounting/Records requires the grantee to maintain financial, accounts, documents, and records (collectively “records”) relating to this contract in accordance with generally accepted accounting principles and practices. The grant agreement also requires that the records shall include evidence sufficient to reflect properly the amount, receipt, deposit, and disbursement of all funds related to the services the grantee is providing, and time and effort reports. Further, the Conservancy’s General Budget Guidelines for Nonprofits (guidelines) states that “if a grantee seeks to recover overhead costs from a Conservancy grant, overhead should be included as a line item in the approved project budget”. Additionally, the guidelines also state grantees must be able to document the appropriateness of these charges and maintain appropriate records for all overhead costs.

Grant agreement section “Costs and Disbursements,” states the Conservancy shall disburse funds for costs incurred to date and will reimburse the grantee for expenses necessary to the project when documented by appropriate receipts. Further, the grantee is required to include with their request for disbursement invoices from contractors that the grantee engaged to complete any portion of the work under the agreement and any other source documents for costs incurred.

### **Recommendations:**

- A. Remit \$433,956 to the Conservancy.
- B. Ensure a clear audit trail is maintained for all claimed expenditures. The audit trail should facilitate the tracing of expenditures claimed on the Conservancy reimbursement claims to the accounting records and supporting source documents.
- C. Implement timekeeping procedures that track actual time worked on grant activities to support amounts claimed. Additionally, maintain timesheets that account for 100 percent of all individuals’ time being compensated or reimbursed under the grant (e.g., employee or consultant), separately identifies hours charged to individual projects, and are approved and signed by a supervisor.
- D. Execute written contracts with all consultants performing state-funded services that clearly define the scope of work, allowable and unallowable costs, current fee schedule, and deliverables. Ensure all contracts incorporate requirements as specified in the grant agreement, and original signed contracts and any subsequent amendments are retained.

- E. Develop and implement a formal overhead cost allocation plan that is applied consistently and equitably distributes costs across all projects. Once in place, the cost allocation plan should be routinely monitored and revised as deemed necessary.
- F. Ensure overhead expenditures are based on actual costs incurred, supported, and documented by a cost allocation methodology.

## **Finding 2: Fiscal Controls Need Improvement**

We observed internal control deficiencies which impair TRP's grant fiscal oversight. TRP did not maintain adequate records for claimed labor costs such as supporting documents for rates, employment purpose, or hours worked. Additionally, TRP did not ensure that grant expenditures were accurately tracked in its accounting records. The evidence made available to us could not provide reasonable assurance that the labor costs were allowable, grant-related, supported by accounting records, and properly recorded. Further, TRP did not adequately distribute to the grant project overhead expenditures based on a reasonable and equitable cost allocation methodology. TRP does not have written policies and procedures for administrative and project management processes. Written policies and procedures should describe management and employee responsibilities regarding grant accounting, invoice processing and approval, subcontract awards, record retention, and project monitoring.

Grant agreement section Audits/Accounting/Records requires the grantee to maintain records relating to this contract in accordance with generally accepted accounting principles and practices. The grant agreement also requires that the records shall include evidence sufficient to reflect properly the amount, receipt, deposit, and disbursement of all funds related to the services the grantee is providing, and time and effort reports.

Also, TRP's director performs several conflicting duties that compromise effective internal controls. The director reviews and approves expenses, prepares grant reimbursement claims, receives grant reimbursement checks, and deposits reimbursement checks into the TRP bank account.

Proper segregation of duties is a key element of an entity's internal control, and is essential to reducing the risk of errors and irregularities. Typically, no one person should initiate, approve, record, and reconcile a transaction, and have custody of funds. Without policies and procedures and segregation of duties, TRP has an increased risk of errors and irregularities.

### **Recommendation:**

- A. Develop and implement written policies and procedures to ensure maintenance of supporting documentation, equitable allocation of overhead costs, proper segregation of fiscal duties, and adequate internal controls.





## The RIVER PROJECT

3912 Laurel Canyon Blvd., # 208

Studio City, California 91604

tel: 818-980-9660

[www.TheRiverProject.org](http://www.TheRiverProject.org)

February 3, 2017

Jennifer Whitaker, Chief  
Office of State Audits and Evaluations  
California Department of Finance  
915 L Street  
Sacramento, CA 95814-3706

### Response to the Draft audit report for The River Project, Grant #11-075, dated January 20, 2017

Dear Ms. Whitaker:

We disagree with your findings as follows:

Your assertion that the workers who actually performed the work on the project are not considered "labor" is absurd.

As an initial point, Joan Cardellino of the State Coastal Conservancy has stated that the work on the project was completed and met the standards of the contract. This work was performed by human beings who came to work on a regular schedule over many months. These workers maintained time records to substantiate their time spent working on the project. At the end of the year these workers were given an IRS Form 1099 summarizing the amount they were paid for their services for the particular year. Our grant manager David Hayes was aware of this from the beginning.

The fact that the workers were given a 1099 and not a W-2 does not change the underlying character and nature of their work. They performed labor on the project, and giving this activity a label of "consultant" or any other label does not change the nature of the activity performed.

Furthermore, we do not agree that the time records maintained by the workers were inadequate. The contract is not at all specific as to the requirements of such time records. We believe our records are more than adequate to support the charges to the contract, and an experienced independent non-profit CPA verified that the time records were sufficient. The auditors stated that the time records we maintained are "not what they are used to seeing." However, our records are very good compared to other small non-profits with which we are familiar, and one undergoing an audit for the very first time.

With respect to Finding 2, any deficiencies in internal controls were rectified after the initial 'friendly audit' performed in 2014 and a corrective action was submitted to the Conservancy at that time.

Lastly, we understand staff was directed not to consider project expenses after September 30, 2014. TRP had filed a timely six-month extension request in direct coordination with our grant manager. That we received neither official approval nor denial of that request appeared to us to be a result of the dysfunction occurring within the Conservancy as Mr. Hayes withdrew and resigned shortly thereafter and management of our project had not been re-assigned. A stop-work order was received on January 7, 2015, which we view as a confirmation that the project had been extended beyond September. We believe expenses until that date are valid.

Sincerely -

ORIGINAL SIGNED BY:

Melanie Winter, Director

p.s. Please use a different image on the report cover. That one does not in any way reflect the intent of the project, nor was that the final version of the work done on that particular property.

Cc: Ms. Mary Small, Deputy Executive Officer, State Coastal Conservancy  
Ms. Regine Serrano, Chief of Administrative Services, State Coastal Conservancy  
Ms. Amy Hutzler, Deputy Executive Officer, State Coastal Conservancy  
Ms. Julia Alvis, Deputy Assistant Secretary, California Natural Resources Agency  
Mr. Bryan Cash, Deputy Assistant Secretary, California Natural Resources Agency