



Transmitted via e-mail

December 31, 2014

Mr. John Laird, Secretary
California Natural Resources Agency
1416 Ninth Street, Suite 1311
Sacramento, CA 95814

Dear Mr. Laird:

Final Report—The Mexican Museum, Proposition 40 Interim Grant Audit

The Department of Finance, Office of State Audits and Evaluations, has completed its interim audit of The Mexican Museum's (Museum) grant CCHER2-39, issued by the California Cultural and Historical Endowment.

The enclosed report is for your information and use. The draft report was issued October 24, 2014, and the Museum's response to the draft report required further analysis. As a result of our analysis, a change was made to Recommendation A under Observation 1 to provide further clarification. The California Natural Resources Agency also provided a response to the draft report and its response is incorporated into this final report. This report will be placed on our website.

We appreciate the assistance and cooperation of the Museum. If you have any questions regarding this report, please contact Frances Parmelee, Manager, or Alexis Calleance, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations

Enclosure

cc: Ms. Polly Escovedo, Executive Officer (A), California Cultural and Historical Endowment
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
Mr. David de la Torre, Director, Mexican Museum

INTERIM AUDIT REPORT

The Mexican Museum Proposition 40 Bond Program Grant Agreement CCHER2-39



The Mexican Museum

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

MEMBERS OF THE TEAM

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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

California voters approved the California Clean Water, Clean Air, Safe Neighborhood Parks, and Coastal Protection Act of 2002 (Proposition 40) for \$2.6 billion. The bond proceeds finance a variety of resource and educational programs.

In June 2012, the California Cultural and Historical Endowment (CCHE) awarded The Mexican Museum (Museum) an \$800,000 grant to plan for the design and construction of a new museum building in the Yerba Buena Arts District of San Francisco. The Museum was founded in 1975, and has since gathered a permanent collection of over 14,000 Latino art objects.¹

SCOPE

In accordance with the Department of Finance's bond oversight responsibilities, we audited grant agreement CCHER2-39 for the period June 1, 2012 through May 31, 2014.²

The audit objectives were to determine whether the Museum's grant expenditures claimed were in compliance with applicable laws, regulations, and grant requirements; and to determine whether the grant deliverables were completed as required. We did not assess the efficiency or effectiveness of program operations.

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

METHODOLOGY

To determine whether grant expenditures were in compliance with applicable laws, regulations, and the grant requirements; and if the grant deliverables were completed, we performed the following procedures:

- Examined the grant files, the grant agreement, and applicable policies and procedures.
- Reviewed the Museum's accounting records, vendor invoices, and bank statements.
- Selected a sample of claimed expenditures and determined whether they were allowable, grant-related, incurred within the grant period, supported by accounting records, and properly recorded.

¹ Excerpt from the Museum's website.

² An interim audit was conducted on grant CCHER2-39 because audit fieldwork was performed prior to the grant end date of July 31, 2014.

- Evaluated whether other revenue sources were used to reimburse expenditures claimed for reimbursement under the grant agreement.
- Evaluated whether a sample of grant deliverables were met by reviewing supporting documentation.

In conducting our audit, we obtained an understanding of the Museum'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 the conduct of our audit and determined to be significant within the context of our audit objectives are included in this report.

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

The results of the audit are based on our review of documentation, other information made available to us, and interviews with staff directly responsible for administering grant funds.

Based on the procedures performed, neither the grant funds nor match expenditures claimed complied with the grant requirements. Additionally, the grant deliverables available for inspection at the time of our audit were not completed as required. The Schedule of Claimed and Questioned Amounts is presented below.

Schedule of Claimed and Questioned Amounts

Grant Agreement CCHER2-39		
Task	Claimed ¹	Questioned
1. RFQs/RFPs/Project Management ²	\$ 33,750	\$ 33,750
2. Conceptual Design	91,162	91,162
3. Schematic Design	0	0
4. Design Development	0	0
5. Construction Documents	0	0
6. Indirect/Administrative Costs	12,491	12,491
Total Grant Funds	137,403	137,403
Total Match	137,403	137,403
Total Project Expenditures	\$ 274,806	\$ 274,806

Observation 1: Inadequate Fiscal Controls and Questioned Costs

The Mexican Museum (Museum) was unable to demonstrate claimed costs were allowable, grant-related, supported by accounting records, and properly recorded. The Museum is responsible for exercising appropriate fiscal controls over grant funds. However, we determined the Museum lacks the necessary fiscal controls to ensure compliance with grant provisions. As a result, costs totaling \$274,806, the entire claimed amount, are questioned as follows:

- Unsupported costs: \$92,482 of costs pertaining to Tasks 1 and 6 including the corresponding match funds are questioned due to a lack of sufficient supporting documentation. Because a clear audit trail did not exist, the eligibility of costs claimed could not be determined. Although the Museum incurred costs, it could not provide sufficient evidence demonstrating costs were related to grant activities. Grant Agreement, Exhibit D, section 4, states the grantee shall maintain satisfactory financial accounts, documents, and records relating to the project for three years following the date of final reimbursement by the California Cultural and Historical Endowment (CCHE).

¹ CCHE awarded \$800,000; however, the Museum claimed only \$137,403 of grant funds as of May 31, 2014.

² RFQ/RFP stands for Request for Qualifications/Request for Proposal.

- Ineligible costs: \$182,324 of costs pertaining to Task 2 including the corresponding match funds are ineligible for reimbursement. The conceptual design costs reimbursed to the Museum were incurred and paid for by a separate entity. Additionally, \$91,162 of the grant costs were incurred prior to the start of the grant term. Grant Agreement, part I.G, section 1, states CCHE will disburse funds to the grantee for items requested for reimbursement that have been paid by the grantee. Grant Agreement, Exhibit C, section 1, also states the grantee may not request reimbursement for work performed prior to the Agreement being in effect.

Additionally, the Museum's accounting records did not separately identify grant-related costs. Grant expenditures were commingled with other unrelated expenditures, and the Museum could not demonstrate how the grant funds claimed traced to the accounting records. Grant Agreement, part I.D, section 4, states the grantee's financial management systems must be capable of distinguishing expenditures attributable to the grant from expenditures not attributable to the grant.

Recommendations:

The Museum should:

- A. Remit \$123,662³ to CCHE. CCHE will make the final determination regarding the disposition of the questioned grant funds and corresponding match costs.
- B. Implement adequate fiscal controls, such as:
 - a. Ensure a clear audit trail is maintained for all claimed expenditures. The audit trail should facilitate the tracing of expenditures claimed on the CCHE invoices to the accounting records and supporting source documents. Bridging documents should be developed to reconcile accounting system and support document information with the CCHE invoices.
 - b. Ensure the accounting system is structured to separately identify and account for grant funds and corresponding match.
 - c. Develop appropriate claim preparation and review policies and procedures that ensure claimed costs are allowable, grant-related, incurred within the grant period, supported by accounting records, and properly recorded. The grant agreement provisions should be used as a guide in developing such policies and procedures.
 - d. Provide training and ongoing guidance to staff directly responsible for administering bond funds on the claim preparation and accounting procedures.

³ CCHE withheld a 10 percent retention from the reimbursement claim; therefore, CCHE paid the Museum \$123,662 (\$137,403 - \$13,741 = \$123,662).

Observation 2: Incomplete Grant Deliverables

The Museum did not complete the deliverables as specified in the grant agreement as follows:

- Task 1: The Museum was required to issue numerous RFQs/RFPs by December 31, 2012; however, actual issuance dates ranged from June 2013 through November 2013, six to eleven months late. This delay significantly delayed the completion of subsequent tasks.
- Task 2: The Museum was required to complete space planning and conceptual design drawings and documents by December 31, 2012. Space planning documents were not made available upon request. Therefore, completion of the space planning tasks in accordance with grant requirements could not be determined. The conceptual design drawings and documents were completed in May 2014, seventeen months after the required completion date.
- Task 3: The Museum was required to complete schematic design drawings and documents by June 30, 2013. Evidence supporting completion of this task was not provided upon request. Therefore, completion of the tasks in accordance with grant requirements could not be determined.
- Task 4: The Museum was required to complete design development drawings and documents by December 31, 2013. However, this task was not completed until April 2014, four months after the required completion date.
- Task 5: The Museum was required to complete construction drawings and documents by June 30, 2014. At the time of our site visit, June 9 through June 12, 2014, the Museum did not appear on task to complete this deliverable by June 30, 2014.

Grant Agreement, part 1.H, section 2, states all work shall be completed by the dates shown in the Scope of Work. The Grantee agrees to submit all work products identified in the Scope of Work by the dates set forth in Exhibit B-1. Grant Agreement, Exhibit B-1, specifies the completion dates for the above-mentioned tasks.

Recommendations:

- A. Effectively plan and monitor grant activities to ensure grant deliverables are completed as specified in the grant agreement. Work collaboratively with CCHE to determine the actions needed to address the completion of deliverables. CCHE will make the final determination on the actions needed regarding the late or unmet deliverables.
- B. Ensure adequate supporting documentation is retained to demonstrate grant deliverables are timely completed as required.

MEXICAN MUSEUM'S RESPONSE

THE MEXICAN MUSEUM

In association with the Smithsonian Institution

November 7, 2014

Richard R. Sierra, CPA
Department of Finance
915 L Street
Sacramento, CA 95814

RE: The Mexican Museum Response to the Opposition 40 Grant Audit

Dear: Mr. Sierra:

On behalf of the Mexican Museum Staff and Board of Trustees ("Museum") with support from the San Francisco Successor Agency to the Redevelopment Agency (the "City") and Millennium Partners ("Project Developer"), we are pleased to submit our response to the Department of Finance Draft Report of its interim audit of The Mexican Museum's grant CCHER2-39. The audit was undertaken of the first reimbursement request submitted by the Mexican Museum ("Museum") of the California Cultural & Historical Endowment ("CCHE") Planning Grant.

In brief, we applaud the auditor's recommendations which includes a recommendation for the staff of The Mexican Museum to work collaboratively with the staff of the CCHE to determine the actions needed to address the completion of the grant deliverables of the \$800,000.00 planning grant to design and plan for the ultimate construction of a world class museum to house the over 16,000 object of art collection ranging from pre-Columbian, colonial, popular, Chicano, Mexican, Mexican-American, and Latino Art which is one of the largest collections of its kind in California, the United States, and outside of Mexico.

Towards this end, the Museum and the CCHE staff have already worked jointly to amend Exhibit B-1 to the planning grant agreement to jointly revise the scope of work under the grand agreement to reflect the current realities of 706 Mission Street mixed-use residential and Mexican Museum project which is on track to break ground in early 2015.

In this regard, and, in the spirit of cooperation the Mexican Museum with support from the CCHE staff requested an extension of time to be able to meet the grant deliverables and draw down the grant funds consistent with a revised and restated Exhibit B-1 Scope of Work which was jointly restructured by the Mexican museum and CCHE staff.

Moreover, the Museum understands and appreciates the auditors' findings that there was room for improvements by both the Mexican Museum and CCHE staff in the submittal on the one hand and in the processing on the other hand, respectively, of the first grant reimbursement request by both the CCHE and Museum staffs. The fact that some honest

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mistakes where made on both sides in this first initial reimbursement request and in its processing genuinely highlights the need for training for both the grantee and CCHE staff. We genuinely and sincerely welcome grantee training and joint grantee and CCHE staff training to insure that future grant disbursement submittals are properly prepared, submitted and processed in light of the fact that significant work has in fact been performed under the planning grant agreement.

The Museum herein submits Attachment "A" which is a detailed enumerated response to the draft audit to both respectfully explain how some of the mistakes and/or misunderstandings occurred by the Museum in the preparation of the first reimbursement request and to also respectfully qualify and distinguish some of the initial audit findings. The information which was prepared by an independent Certified Public Accountant who represents the Mexican Museum will hopefully shed some light on some of the shortcomings of this initial submittal process, fill information gaps and illustrate the cross mis-communication and/or misunderstandings in the administration of the grant.

The Mexican Museum stakeholders thank the audit committee and CCHE staff for this opportunity to comment on the audit committees' findings and to pro-actively welcome the opportunity to work together.

Moreover, the Mexican Museum kindly request the opportunity for The Mexican Museum and City and County of San Francisco to work with CCHE staff and its Commission to work jointly to deliver to the people of California a new cultural facility where over sixteen thousand objects of art will be made available to the residents and visitors of the great State of California. We are enclosing two letters of support from the Successor Agency and from Millennium Partners which highlight from a third party perspective the progress and successes of the Mexican Museum in its important community undertaking and which also helps to demonstrate that the Mexican Museum is truly working in partnership with other key and important partners.

Respectfully submitted:

Original signed by:

By:

David J. de la Torre, Director
The Mexican Museum

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ATTACHMENT "A"

Responses to Department of Finance Draft Report – The Mexican Museum, Proposition 40 Grant Audit
Prepared and submitted by Hugo Delgado, CPA

The following first addresses the Audit Committee's Observations and then its recommendations.

Observation 1: Inadequate Fiscal Controls and Questioned Costs

Response to Findings

Unsupported Costs: \$92,482

\$67,500 are contractual payments made to the Project Manager. The Project Manager **sole** responsibility is to ensure that the undertaking of all facets of constructing the New Museum for The Mexican Museum are achieved. The contract with the Project Manager should be considered sufficient evidence to support eligibility of these costs. There is no other function of the Project Manager. The total submittal was within the approved budget by CCHE for this position.

\$24,982 are costs related to Task # 6, which are Indirect/Admin costs allowed under the Grant. These expenditures are related to the salary of the Executive Director of the Museum whose time was allocated to the Project in the form of management, meetings, administration of the tasks associated with ensuring the progress of this project. These costs under the original submission of a **draft** invoice to the Museum's CCHE project manager were not included on the invoice for reimbursement as Museum staff was unsure as to the whether the nature of the costs qualified under the planning nature of the grant. In fact, the Museum submitted these items for reimbursement because CCHE staff suggested to the Museum's CPA that Museum "Payroll" expenditures could be considered eligible costs under this category and hence to include it in the invoice for reimbursement.

Ineligible costs: \$182,324

The Museum does not dispute that the amount indicated are ineligible for reimbursement as there was a misunderstanding of which costs were acceptable for reimbursement and which were eligible to be submitted as "matching" funds. In fact, the grant agreement does allow to submit "match" funds up to 20% of the total match of \$160,000.

In regards to the Museum's accounting records being commingled with unrelated expenditures, we respectfully disagree with this assessment as the Museum's procedures cannot distinguish grant expenditures from non-grant expenditures. The accounting process clearly indicates all project related costs associated with the Project in not only the financials but also at the beginning of the process with the check requests. This accounting system is properly in place. The nature of the grant is not one of direct costs but of reimbursement. This entails accounting for the Project as expenditures are applied and subsequently determines which costs are to be allocated to the grant. This is not a direct disbursement method, but an accounting journal method given the nature of the project and the after the fact determination of which costs are eligible to request for reimbursement. These costs are contained within the financials once the invoice has been processed for reimbursement.

The following are the Museum's comments to the audit's recommendations:

- A. Remit \$137,403 to the CCHE – Firstly, the Museum did not receive this amount. The CCHE retains 10% of all invoice request reimbursement as a “Performance Retention”, so only the amount received of \$123,662.36 was received. Secondly, CCHE did not dispute \$37,125 of the submitted invoice and the Department's recommendation does not take this into considerations. Finally, this recommendation is in direct contradiction to what the Museum was told by CCHE staff. The Museum was unequivocally told by CCHE staff that the funds paid out under the grant to the Museum could be retained by the Museum as an advance against future invoices and could be used by the Museum in its operations. At this juncture, the Museum would request that the CCHE staff offset these recommended funds from future reimbursement submittals.

- B. Implement adequate fiscal controls
 - a. Clear audit trail – As indicated above the Museum believes that it has implemented a clear audit trail for costs requested for reimbursement from the CCHE. We find that the request from the auditors to be onerous to our system of accounting in that they conclude that since the accounting has to occur after the original transaction has taken place (after the fact) that this is inadequate for tracking. These are not direct costs that can be assessed as being immediately reimbursable by the Museum at the time of payment due to the various contracts and source of funds for the Project, but this determination can and is be made once the invoicing process begins. We track the costs requested for reimbursement within our financials via an “after the fact” journal entry.
 - b. Ensure accounting system is structured separately – We believe this system is already implement as indicated in our response to item “a” above.
 - c. Develop claim preparation – We believe we have implemented these procedures although we will continue to work with the CCHE to ensure that we are meeting all requirements.
 - d. Train staff – The Museum has hired an in-house bookkeeper that will be provided guidance the procedures required and will work with its CPA to ensure that these procedures and processes will be implemented and followed.

CALIFORNIA NATURAL RESOURCES
AGENCY'S RESPONSE



December 3, 2014

Richard R. Sierra, CPA
Chief, Office of State Audits and Evaluations
Department of Finance
915 L Street
Sacramento, CA 95814

DRAFT REPORT – THE MEXICAN MUSEUM, PROPOSITION 40 GRANT AUDIT

Dear Mr. Sierra,

Thank you for the opportunity to review and provide comments on the audit of The Mexican Museum grant number CCHER2-29. We would like to point out the following to help clarify the two observations:

Observation 1: Inadequate Fiscal Controls and Questioned Costs

The California Natural Resources Agency (Agency), who now manages these grants on behalf of the California Cultural and Historical Endowment (CCHE), agrees that costs reimbursed to the Mexican Museum were not eligible under the program. Agency is presently working to determine appropriate resolution for the repayment of these costs as this grant expired July 31, 2014. The intent is to recoup the costs as appropriate from a subsequent payment request that included eligible costs incurred while the grant was still active. As not all eligible costs were substantiated with backup, Agency will work with the Mexican Museum to secure same.

Observation 2: Incomplete Grant Deliverables

The recommendation by OSAE assumes there is an active grant agreement between the Mexican Museum and the CCHE. However, as stated above, this grant expired on July 31, 2014. Remaining grant funds will revert back to the State and will be available for future, competitive programs.

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Again, thank you for the opportunity to comment on the audit findings. If you have any questions regarding the responses, please contact Polly Escovedo, Program Manager, at (916) 651-6481.

Sincerely,

Original signed by:

Bryan Cash, Deputy Assistant Secretary
California Natural Resources Agency

cc: Ms. Frances Parmelee, Audit/Evaluation Manager, Department of Finance

EVALUATION OF RESPONSES

The Mexican Museum's (Museum) and the California Natural Resources Agency's (Agency) responses to our draft report have been reviewed and incorporated into the final report.

The Agency indicated it is now managing this grant on behalf of the California Cultural and Historical Endowment (CCHE). Additionally, the Agency stated our report assumes an active grant agreement. Although this report was issued after the grant agreement's end date of July 31, 2014, our audit scope only covered the period through May 31, 2014 and is considered an interim audit.

Along with its response, the Museum submitted two letters in support of the project from third parties which have been omitted herein for brevity. In evaluating the Museum's response, we provide the following comments:

Observation 1: Inadequate Fiscal Controls and Questioned Costs

The Museum generally disagreed with Observation 1. The Museum stated a clear audit trail exists; however, an adequate audit trail should facilitate the tracing of expenditures claimed on payment requests to the accounting records and source documents. Bridging documents would also enable the reconciliation of the accounting system information with the payment requests. The documentation made available to us did not adequately support the claimed costs. Specifically, we provide the following comments in response to Attachment A:

- For Task 1, the Museum stated the contract for the Project Manager should be sufficient support for those costs; however, the contract alone does not clearly demonstrate all costs were related to grant activities.
- For Task 6, the Museum stated the Executive Director completed tasks related to the project; however, the Museum did not provide adequate documentation such as timesheets, activity logs, or other forms of documentation to demonstrate time spent on the grant.
- The Museum acknowledged the reimbursed costs for Task 2 were ineligible because they were incurred outside of the grant period; however, the Museum disagreed that the corresponding match funds are ineligible. Although the grant agreement allows for certain match expenditures to be retroactively applied to the grant, these costs must be adequately supported. The Museum did not provide adequate documentation to support the claimed costs or to demonstrate costs were grant related.
- The Museum stated their procedures cannot distinguish grant expenditures from non-grant expenditures, and that the costs are tracked by journal entries. The journal entries referenced were not made available to us.

Based on the Museum's response, we modified the report and changed the recommendation, Part A, to recommend remittance of the grant funds received totaling \$123,662. We also acknowledge the Museum's willingness to implement some of the recommendations by improving the claim preparation process in collaboration with CCHE and hiring an in-house bookkeeper. However, we reiterate the importance of establishing adequate fiscal controls as described in our recommendations. Because no additional documentation was provided, the observation, with the exception of the recommendation, Part A, will remain unchanged.

Observation 2: Incomplete Grant Deliverables

The Museum generally agreed with Observation 2. The Museum stated it has worked with CCHE staff to amend the grant agreement scope of work, and that it had requested an extension of time to meet the grant deliverables. We acknowledge the steps the Museum has taken to work collaboratively with CCHE, and recommend it continues to do so. As such, no changes were made to Observation 2.