

FINANCIAL MANAGEMENT OVERSIGHT REVIEW

Cost Allocation Plan Review

of

**Metropolitan Council
(Met Council)**

PERFORMED FOR

U.S. DEPARTMENT OF TRANSPORTATION

FEDERAL TRANSIT ADMINISTRATION



UNDER

CONTRACT: DTFT60-16-Q-00017

TASK ORDER: 5

Prepared by

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U.S. DEPARTMENT OF TRANSPORTATION
FEDERAL TRANSIT ADMINISTRATION

REPORT ON THE REVIEW OF THE
INDIRECT COST RATE PROPOSAL

Metropolitan Council

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EXECUTIVE SUMMARY

EXECUTIVE SUMMARY

The **Metropolitan Council (Met Council)** submitted its Fiscal Year (FY) 2017 Indirect Cost Allocation Plan (ICAP) to the **U.S. Department of Transportation (DOT), Federal Transit Administration (FTA)** for review and approval. The ICAP submission proposed fixed indirect cost rates with carry forward based on 2015 actual costs for the Metro Transit and Metro Transportation Services (MTS) departments. The plan was submitted for review because the Metro Transit rate exceeded the previously approved rate by more than twenty (20) percent. FTA Circular 5010.1D states that a Cost Allocation Plan/Indirect Cost Rate Proposal should be submitted to the “cognizant” or “lead” Federal Agency when the grantee’s proposed CAP/Indirect Cost Rate Proposal exceeds the amounts and rate approved for the previous year(s) by more than 20 percent.

FTA contracted **Hamilton Samlin Milligan, JV, LLC (HSM)** to perform a review of Met Council’s FY 2017 ICAP rate submission. This review was performed to determine whether the ICAP submission meets the requirements of Office of Management and Budget (OMB) 2 CFR Part 200, “Cost Principles”, FTA Circular 5010.1D and other applicable Federal regulations.

Conclusion

HSM’s review of Met Council’s FY 2017 ICAP rate submission indicated that Met Council’s methodology was in substantial compliance with the requirements of 2 CFR Part 200 and FTA circular 5010.1D. The rate proposed in the initially submitted ICAP was reasonable with few exceptions. Specifically, we identified unallowable costs amounting to \$1,043,750 in the 2017 proposed indirect cost pool that should have been excluded from costs allocated to the departments (Refer to **Section 3.1** for the details of the unallowable costs).

Met Council subsequently updated the ICAP in April 2017 to exclude the unallowable cost. This resulted in changes in the initially proposed ICAP rates as follows:

Departments	Proposed 2017 Indirect Cost Rates	Adjusted 2017 Indirect Cost Rates
Metro Transportation services	84.39%	74.52%
Metro Transit (Bus & Rail)	45.03%	44.57%

Based on the results of our review of Met Council’s ICAP submissions, we recommend that FTA approve the following adjusted proposed rates for reimbursement of indirect costs to the Grantee:

Departments	Adjusted 2017 Indirect Cost Rates
Metro Transportation services	74.52%
Metro Transit (Bus & Rail)	44.57%

SECTION 1
SCOPE

SCOPE

1.1 Objective

Under contract to FTA, Hamilton Samlin Milligan performed a review of Met Council's FY 2017 Cost Allocation Plan submission to FTA to determine if the amounts claimed by Met Council meet the requirements of 2 CFR Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, FTA policies, and other applicable Federal regulations. Furthermore, the review was designed to determine whether the costs were:

- Necessary and reasonable for the operation of FTA supported programs;
- Permissible under the terms of the awards; and
- Not otherwise unallowable under 2 CFR Part 200 and FTA policies.

2 CFR Part 200 allows the Grantee considerable discretion in the methods that can be used in determining allowable indirect cost and in applying the indirect cost rate(s) that result from the methods. Additional factors, where applicable, were considered during the review of the Cost Allocation Plan submission, including:

- Purpose of the Federal awards and their reimbursement provisions;
- Methodology used by the Met Council to develop the ICAP;
- Cost groupings used to accumulate common costs for allocation to benefiting department units and awards;
- Appropriateness of the statistical bases used to allocate the costs of the selected cost groupings to the activities that benefit from them;
- Type of rate calculated in the ICAP;
- Type of rate (provisional/final, fixed rate, or predetermined) to be approved;
- Period for which the approval will be given;
- Outstanding issues, which might be warranted as a condition of approval.

1.2 Limitations on Reliability of the Data and Use of the Report

This report does not constitute an audit of any financial statements prepared by Met Council. Instead, this report is a comprehensive, professional analysis focused on compliance with applicable Federal regulations. Since data provided by the Met Council were assumed to be accurate, any inherent limitations, errors or fraud that may have occurred might not have been detected.

This report is intended for the information of FTA and the Met Council and should not be used for any other purpose. However, this report is a matter of public record, and its distribution is not limited.

1.3 Background

The Minnesota Legislature established the Metropolitan Council (Met Council) in 1967 to coordinate planning and development within the Twin Cities metropolitan area and to address issues that could not be adequately handled within the existing governmental arrangements. Additional legislative acts in 1974, 1976 and 1994 reinforced the Council's planning and policy roles and merged the functions of three agencies (the Metropolitan Transit Commission, the Regional Transit Board and the Metropolitan Waste Control Commission) into the Metropolitan Council. The Met Council is composed of sixteen members, each of whom represents a geographic district, and one chairperson who serves at large. Each member is appointed by and serves at the pleasure of the governor. The State Senate confirms the nominees and the chairperson to the council. The geographic region for which the Met Council has responsibility includes the counties of Anoka, Carver, Dakota (excluding the city of Northfield), Hennepin (excluding the cities of Hanover and Rockford), Ramsey, Scott (excluding the city of New Prague), and Washington.

The Met Council is organized into three operating divisions, namely: Transportation, Environmental Services, Community Development, and Supporting Central Administrative Units. The Met Council operates transit services from two divisions, Metro Transit and Metropolitan Transportation Services (MTS). The Met Council contracts some services which are administered by MTS, such as Metro Mobility that operates the system wide ADA paratransit service. The public transportation services in the region are centered on the two major cities of Minneapolis and St. Paul. The total service area includes 189 cities and townships, with a population of approximately 3.46 million people.

MTS has an active operating fleet of 1,025 vehicles, which are operated by 9 contractors and subrecipients to provide purchased fixed route, demand response, dial-a-ride, ADA complementary paratransit, and van pool services. These contractors utilize a total of 695 Council-owned vehicles. Metropolitan Council also provides financial resources and FTA funded vehicles to communities who have opted out of their service area. These resources are used to operate express, local, and dial-a-ride bus services in the region. The Metropolitan Council provides an additional 330 buses to opt-out jurisdictions for a total MTS fleet of 1,025 vehicles.

Metro Transit directly operates a network of 131 fixed routes. Metro Transit opened its first rapid bus line, the A Line, in June 2016. The A Line provides faster and more frequent service connecting the METRO Green and Blue lines and several other destinations. Metro Transit operates a fleet of 902 buses, a fleet of 86 light rail vehicles, 6 rail locomotives and 18 commuter rail cars for route services.

**SECTION 2
OVERVIEW**

OVERVIEW

2.1 Indirect Cost Allocation Plan Approach

The initial Met Council Indirect Cost Allocation Plan (ICAP) proposed two separate indirect costs rates. A separate rate was developed for the Metro Transit (Bus & Rail) and Metropolitan Transportation Services (MTS).

The method used in calculating the rates is as follows:

$$\frac{\text{Indirect Costs Allocated to Department}}{\text{Salaries and Wages of Department}} = \text{Indirect Cost Rate}$$

See Appendix A for the calculation of the indirect cost rates for Metro Transportation Services and Metro Transit (Bus & Rail) for FY2017.

The Met Council used a double step-down allocation procedure to distribute costs among Central Services and to other departments that receive benefits.

The Met Council's Indirect Cost Allocation Plan is composed of the following components:

- Central service departments,
- Benefitting departments,
- Expenditures of central service departments,
- Descriptions of activities provided by central service departments, and
- Methods of allocating the expense of central service departments.

For the purposes of the cost allocation, the departments of a governmental entity are separated into two groups: central service departments and benefitting departments. A central service department is a unit of government that provides centralized services to other government departments. The cost of providing central service is identified from the government's financial records. Benefitting departments are those units of government that do not provide central services but rather deliver services to the public.

Expenditures of the central service departments are analyzed to ensure that the expenditures are allowable according to federal standards and to identify expenditures that may benefit another department or departments disproportionately to others. After the expenditures are analyzed, they are distributed into cost pools for allocation to those departments that benefit from the activities of central service departments. Examples of functions are payroll services, administrative coordination, banking services, building operations, and legal services. The purpose of identifying the various activities within a unit of government is to allow for different allocation bases enabling these activities to be used to distribute the costs of providing the function.

OVERVIEW

An allocation base is a reasonable and measurable means of distributing costs to those units of government that benefit from the service. Different allocation bases are required to recognize that the value of providing a service is proportionate to the service received. It is reasonable to allocate payroll services based upon the number of payroll checks issued. It is most likely not reasonable to allocate payroll based upon square footage of occupied space. The chosen allocation base must reflect the service being provided, and it must reflect those who benefit from the service.

After all of the above is accomplished, the information is entered into a cost allocation spreadsheet that performs the mathematical functions of allocating indirect costs from central service providers to benefiting departments. The spreadsheet performs two allocations. The first allocation distributes expenses according to the financials and any indirect costs that have been allocated to the department from central service departments that are sequentially above the receiving department. The second allocation distributes indirect costs that have been allocated to the department from departments that are sequentially below the receiving department. The reason a multiple allocation is performed is to maximize the distribution of all costs to all departments that benefit from the services provided by the central service department. The result documents indirect costs that are eligible for recovery from certain programs. The sum calculated by the benefiting department is the maximum amount the government should have recovered during the fiscal year in question.

The final step is to calculate a roll forward adjustment, also known as a carry forward adjustment. This adjustment is a calculation of the variance between the actual indirect costs and the total recovered two years previous to the current year. Therefore, for FY 2017 indirect cost rate, the carry forward is calculated from FY 2015 and the difference, positive or negative, is the carry forward amount (2015 Actual Indirect Costs – (2015 Direct Salaries X Rate Used In 2015)). The carry forward amount is added to, or subtracted from, the current year allocations to determine the total proposed costs for use during the appropriate fiscal year. It is the total proposed costs that form the basis for indirect cost rates.

OVERVIEW

2.2 Proposed Indirect Cost Rate

Below are the rates proposed by the Met Council for its grantee departments:

Departments	Proposed 2017 Indirect Cost Rates
Metro Transportation services	84.39%
Metro Transit (Bus & Rail)	45.03%

SECTION 3
EVALUATION OF INDIRECT COST RATE PROPOSAL

EVALUATION OF INDIRECT COST RATE PROPOSAL

3.1 Evaluation of the Met Council's ICAP Submission

We performed a general review of the Met Council's FY 2017 ICAP and other documents to become familiar with the Met Council's operations, accounting system and cost allocation practices. During the review, we analyzed the methodology used for distributing indirect costs and assessed the reasonableness of the costs assigned to the Met Council's central service costs pools. The review of the Met Council's ICAP submission indicated that the overall methodology was reasonable and compliant with the requirements of 2 CFR Part 200 and FTA 5010.1D, except where noted below. The procedures performed to evaluate the adequacy of the submission are summarized below:

HSM reviewed the FY 2017 submissions to determine whether all the supporting documentation required by 2 CFR Part 200 and other related FTA Regulations are included. The required documentation includes a crosswalk of the costs included in the Met Council's FY 2017 submissions to the respective Comprehensive Annual Financial Reports, signed certification, organizational chart, supporting subsidiary work sheets and accounting reports, and details supporting the allocation basis. We noted from our review that the submission included a signed certification, organizational chart, supporting subsidiary worksheets and accounting reports. We also noted that the submissions included an adequate cross referenced reconciliation of all the costs used in the calculation of the indirect cost rates to the audited financial statement as required by 2 CFR Part 200 *Appendix VII Section D(2)(a) and FTA Circular 5010.1D, Appendix F(4)(e)*.

In reviewing the Met Council's indirect cost pool components for appropriateness, HSM performed sample testing of the FY 2015 indirect cost pool with the view that any unallowable costs identified from the testing would be excluded from the indirect cost pool to recalculate the rates. Based on the testing that HSM performed, we exclude unallowable cost of \$1,043,750 from the indirect cost pool. The indirect cost that we determined to be unallowable and our rationale for exclusion are summarized below:

Amount	Unallowable Cost Rationale Based on 2 CFR Part 200
\$85,686	The cost relates to project of outreach and engagement plan, community partnerships, which is unallowable under 2 CFR 200.421 Advertising and public relations. As a result, the costs are unallowable as indirect costs and should be excluded from the indirect cost pool.
\$15,427	The cost relates to bad debt expense, per 2 CFR 200.426. Bad debts (debts which have been determined to be uncollectable), including losses (whether actual or estimated) arising from uncollectable accounts and other claims, are unallowable. As a result, the costs are unallowable as indirect costs and should be excluded from the indirect cost pool.
\$9,333	The cost relates to application subscription with a service period of 3 years, which individually exceed the \$5,000 threshold, the cost should either be capitalized and excluded from indirect cost per 2 CFR 200.439 or expensed over its service period. The Met Council

EVALUATION OF INDIRECT COST RATE PROPOSAL

Amount	Unallowable Cost Rationale Based on 2 CFR Part 200
	agreed to exclude \$9,333 (2 years) from the indirect cost pool.
\$9,000	The cost relates to the Met Council's two-day retreat. To be allowable under federal awards, the cost needs to be reasonable and necessary. Per 2 CFR 200.432 the retreat cost is unallowable and should be excluded from the indirect cost pool.
\$12,933	The cost relates to the Install of the Labor Mitel System. The cost should be capitalized upon completion of the project per 2 CFR 200.439 Equipment and other capital expenditures (7). Equipment and other capital expenditures are unallowable as indirect costs. As a result, the costs are unallowable as indirect costs and should be excluded from the indirect cost pool.
\$197,700	The cost relates to the improvement of the phone system, per 2 CFR 200.12. Capital assets improvements to capital assets that materially increase their value or useful life should be categorized as capital assets and removed from indirect cost pool.
\$980	The cost relates to travel expenses exceeding the GSA per diem rate, per travel policies provided, government rates should be requested wherever possible. Thus, the difference higher than the GSA rates should be removed from the indirect cost pool.
\$416	The cost relates to membership dues from Minnesota Employers Workers Compensation Alliance of which 64% is non-deductible lobbying expenses and should be removed from indirect cost pool per 2 CFR 200.454 (e). Costs of membership in organizations whose primary purpose is lobbying are unallowable.
\$25	The cost relates to membership dues from Saint Paul Area Chamber of Commerce of which \$25 are for foundation donation expenses, per 2 CFR 200.434 (a). Costs of contributions and donations, including cash, property, and services from the non-Federal entity to other entities are unallowable.
\$17,250	The expense relates to contract associated with Metropolitan Council Environmental Services and should be treated as direct cost or 100% allocated to Environmental Services
\$695,000	The expense relates to capital lease payments, according to CAFR Page 49. The information provided therein states that the Council intends to continue the lease through its entire term, and the CAFR also classifies the lease as a capital lease. Based on this, this \$695,000 related to this lease-purchase agreement is unallowable as indirect cost per 2 CFR 200.465. As a result, the payment to the lease-purchase agreement should be removed from indirect cost pool.

EVALUATION OF INDIRECT COST RATE PROPOSAL

The Met Council subsequently updated the ICAP on April 2017 to update the indirect cost rates to exclude the unallowable costs identified. These adjustments resulted in the following ICAP rates:

Grantee Department	Proposed 2017 Indirect Cost Rates	Adjusted 2017 Indirect Cost Rates
Metro Transportation services	84.39%	74.52%
Metro Transit (Bus & Rail)	45.03%	44.57%

EVALUATION OF INDIRECT COST RATE PROPOSAL

3.2 Recommendation

There are no findings and recommendations

**SECTION 4
CONCLUSION**

CONCLUSION

The Met Council's FY 2017 ICAP submission provided for a reasonable allocation of indirect costs to Grantee Departments. This review recalculated the Met Council's indirect cost rates and verified that the methodology used to identify, categorize and allocate costs was in accordance with OMB and FTA regulations.

Based on the results of this review of the Met Council's FY 2017 ICAP submission, HSM recommends that FTA approve the following adjusted rates:

Grantee Department	Adjusted 2017 Indirect Cost Rates
Metro Transportation services	74.52%
Metro Transit (Bus & Rail)	44.57%

APPENDIX

Metropolitan Council 2 CFR Part 200 Indirect Cost Allocation Plan FY2017

SUMMARY SCHEDULE

	RA Excluded Departments	Community Development	Housing & Redevelopment	Environmental Services	Metro Transportation Services	Metro Transit (Bus & Rail)	Total
	18	19	20	21	22	23	
1 Accounts Payable & Receivable	9,487	4,625	3,742	228,791	22,480	-	269,125
2 Budget and Evaluation	6,867	3,348	2,708	165,602	16,271	298,642	493,438
3 Communications	23,792	352,479	65,891	245,711	392,355	133,165	1,213,393
4 Diversity Management	4,101	7,896	8,786	139,591	9,827	689,073	859,274
5 Document Management	4,136	7,963	8,860	140,770	9,911	694,898	866,538
6 Fiscal Services	19,962	9,731	7,874	481,379	47,298	868,106	1,434,350
7 Human Resources	19,467	37,481	41,705	662,615	46,650	3,270,919	4,078,837
8 Information Services	285,701	340,497	230,912	3,354,082	911,904	6,496,822	11,619,918
9 IS Capital Fund	30,147	35,928	24,365	-	96,221	-	186,661
10 Internal Audit	6,773	3,302	2,671	163,334	16,048	294,553	486,681
11 Payroll	4,690	9,031	10,049	159,651	11,240	788,097	982,758
12 Regional Administrator	4,557	8,773	9,761	155,094	10,919	765,601	954,705
13 Risk Management	1,383	2,662	2,962	47,066	3,313	232,335	289,721
14 Robert Str Op.-Central Serv	243,797	280,042	291,944	546,740	352,892	-	1,715,415
15 Purchasing & Contracting	6,015	3,185	5,662	713,209	43,171	956,489	1,727,731
	670,875	1,106,943	717,892	7,203,635	1,990,500	15,488,700	27,178,545
16 MCES Org Wide	-	-	-	2,832,649	-	-	2,832,649
17 Met Transit Division Admin	-	-	-	-	-	29,589,299	29,589,299
Current Allocations	670,875	1,106,943	717,892	10,036,284	1,990,500	45,077,999	59,600,493
Allowable Assigned Costs	-	509,524	116,327	3,898,295	747,890	10,070,628	15,342,664
Total Current Allocations	670,875	1,616,467	834,219	13,934,579	2,738,390	55,148,627	74,943,157

From C-3

Direct Salaries 2,282,769 32,233,368 2,964,855 151,188,160

2013 CARRY FORWARD CALCULATION

Negotiated Fixed Rate	82.06%	37.67%
Direct Labor Base	2,493,668	126,353,716
Indirect Cost Recovery	2,046,304	47,597,445
Actual Indirect Costs	2,246,653	44,940,925
Carry Forward (Actual Indirect Costs MINUS Indirect Cost Recovery)	200,349	(2,656,520)
Actual Rate	90.09%	35.57%

SCHEDULE OF INDIRECT COST RATES

Actual Indirect Costs - 2015	2,738,390	55,148,627
Carry-forward from 2013	200,349	(2,656,520)
Subtotal Indirect Costs - 2015	2,938,739	52,492,107
Actual Direct Salaries - 2015	2,964,855	151,188,160
Rate used in 2015	116.96%	26.63%
Recoverable Indirect Cost	3,467,694	40,261,407
Plan Year Under(Over) Carry-forward	(528,955)	12,230,700
Total Indirect Cost Pool	2,209,435	67,379,328
Proposed 2017 Salary & Wage Based Rate	74.52%	44.57%