



Audit of State and Federal Cost Sharing Agreements

Report # 06-18

Prepared by
Office of Inspector General

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SOUTH FLORIDA WATER MANAGEMENT DISTRICT

February 13, 2008

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Re: Final Report – Audit of
State and Federal Cost-
Sharing Agreements - Project
06-18

This audit was performed pursuant to the Inspectors General's authority set forth in Chapter 20.055, F.S. The audit focused on determining whether the District and the United States Army Corps of Engineers are contributing towards construction of the critical restoration projects in accordance with cost-sharing agreement terms and conditions. This report was prepared by Dan Sooker.

Sincerely,

John W. Williams, Esq.
Inspector General

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BACKGROUND

In accordance with the Office of Inspector General's FY 2006 Audit Plan, we conducted an audit of the South Florida Water Management District's (the District) process of accounting for and monitoring critical restoration project cost-sharing and Modified Water Deliveries to the Everglades National Park agreements (Modified Waters) with the Federal government.

The District routinely enters into cost-sharing agreements with state and federal governments as partners in environmental restoration and other projects. The Kissimmee River Restoration, Comprehensive Everglades Restorations Program (CERP) and critical restoration projects are the more high profiled cost-sharing arrangements but there are many more. Excluding the Kissimmee River Restoration and CERP agreements, there are 121 various types of agreements with Federal and State governments valued at \$115 million.

In previous fiscal years, we have audited the Kissimmee River Restoration and CERP programs and smaller cost-sharing agreements with county and local governments. An audit of the Acceler8 program was recently completed by auditors from an independent accounting firm. Based on the audit work completed on these cost-sharing programs, we have limited the scope of this audit to state and federal government agreements outside of the above-mentioned major programs. As a result, the **critical restoration and Modified Waters** projects were the only remaining federal and state government agreements that met our audit criteria.

According to the critical restoration project cooperative agreements, these projects are primarily 50/50 cost share arrangements between the local non-federal sponsor and U.S. Army Corps of Engineers (USACE). The federal cost-sharing for these projects was authorized by Congress in the Water Resource Development Act of 1996. The purpose of the critical project authorization was to implement projects that are essential to the restoration of the Florida Ecosystem. This authorization was the basis for Federal cost-sharing on nine critical restoration projects, seven of which are cost-shared with the District but limited the USACE contribution to a maximum of \$75 million for all the critical projects and \$25 million for a single project. Approximately \$47 million of the USACE funding was allocated for District projects.

The District's contribution normally consists of a combination of land, cash and in-kind support. The USACE most often is responsible for construction. The cost-sharing agreement stipulates that the federal government will perform a final accounting to determine that the District as the non-federal sponsor has met the agreed upon obligation when the project is completed.

The Modified Waters agreement varies from the other cost-sharing agreements in that the District will contribute unspecified land for the project and pay 25% of the total cost to operate and maintain the infrastructure. Such costs will include exotic plant control and environment enhancement projects that will be determined by a tri-party agreement with Department of Interior, the USACE and the District.

OBJECTIVE, SCOPE AND METHODOLOGY

Our objective was to verify that the District as the non-federal local sponsor and the USACE (Federal sponsor) are contributing their share of the committed participation in accordance with the agreements. Our focus was to examine the process for accumulating, reporting and obtaining credit for the District's share of cost and ensure that project manager's maintain accurate records related to each sponsor's contribution towards completion of a cost-shared project. In order to accomplish our objectives, we performed the following procedures:

- Interviewed appropriate District and cost-sharing partner staff
- Reviewed agreements and other financial records
- Requested documents from the cost sharing partner that support their contribution

Our audit was conducted in accordance with Generally Accepted Government Auditing Standards. These 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 objectives.

AUDIT RESULTS

Executive Summary

To date, the District contributed \$79.1 million towards its 50% critical restoration projects cost-sharing obligation surpassing that of the USACE by \$26 million. The District actual expenditures included in-kind costs of \$17.1 million, land certified to the USACE valued at \$29 million and cash contributions of \$33 million. An estimate of \$18.6 million to complete the projects will be funded by the District, which will bring the total District contribution to \$97.7 million. Records provided by the USACE indicate that they have contributed \$53.1 million.

Prior to starting the critical restoration projects, the District met with USACE officials to develop a project cost reporting process for District in-kind credit. As a result of this meeting, the District customized a process to accumulate costs and prepare reports in a manner that was believed to be acceptable to the USACE. Semiannually, the District remitted a work-in-kind project report for USACE approval, which captured all District project costs incurred for the period to the USACE.

The USACE reviewed the first District work-in-kind submittal in 2001 but did not review the subsequent work-in-kind reports until last year. Their preliminary review of work-in-kind reports valued at \$6 million revealed a lack of documentation supporting the District's in-kind costs and other deficiencies. As such, only 39% of in-kind costs were eligible for project credit. Subsequently, the District provided the USACE reviewer with additional support for work-in-kind project credit, which resulted in the USACE, preliminarily approving \$3.8 million of the \$6 million costs submitted for credit. Almost all of the remaining balance of \$2.2 million represents costs submitted to the USACE for unfinished projects. Upon completion of the projects, the USACE will review the District submitted cost support for in-kind credit approval, which will be subject to proper documentation and USACE funding availability. We recommended that the District in collaboration with the USACE determine documentation requirements and reestablish an acceptable in-kind credit approval process. Management stated that a process for documenting project expenses has been initiated. This new process should

reduce the USACE review effort for in-kind reports and reduce the number of disputed costs.

A final accounting will determine the District's project liability, if any. Currently, District project management estimates a liability to the USACE of \$1.4 million after the critical projects are completed. Considering the District has over spent the USACE by approximately a 2 to 1 margin, the District should attempt to eliminate any liability that may exist at the project's completion through an amendment or other offset. Management has informed us that Congress has recently approved an increase in the federal spending cap for Critical Projects from \$75 million to \$95 million. As a result, the USACE may allocate some of this authorization to the District sponsored projects. In addition, for the upcoming Water Resource Development Acts or Appropriation Bills, the District's Everglades Restoration Resource Area staff will take the lead in coordinating with the Government and Public Affairs Department to develop and gain Congressional support for legislation, which authorizes the USACE to balance the 50/50 cost-share across all projects with the District. Management believes that this would eliminate the need for cash contributions and reimbursements.

Develop a Process to Support District In-Kind Costs

Prior to starting the critical restoration projects, the District met with USACE officials to better understand the concepts of reasonableness, allowability and allocability of District incurred project costs which will be submitted for in-kind credit. According to USACE staff, it is not a common practice for the USACE to assign in-kind project responsibilities to a local sponsor like the District because work-in-kind credit is a reduction in cash contribution.

As a result of this meeting, a project cost reporting process was developed to accumulate District cost in a manner that was believed to be acceptable to the USACE. This process established project activity codes and job numbers to segregate, account for and monitor critical restoration project expenditures. The process starts with Project

Managers providing the project activity codes and job numbers to staff working on critical projects to ensure that time is posted to the appropriate cost codes.

Then monthly, District project managers conduct detailed reviews of project reports that capture all the costs including labor and non-labor charged for the period. A USACE approved cost and fringe benefit rate is applied to all direct labor charged to the project. The detailed review of labor costs includes verifying that appropriate staff charged the project and the hours worked and the activity code appears reasonable. Project Managers also examine non-labor costs such as construction costs and other outside charges. Unknown costs are researched and corrections are made where appropriate before submitting to the USACE.

We reviewed the critical project detailed expenditure reports for FY 2005 and FY 2006. For labor costs, we examined the expenditures to determine that staff time charged to the project was appropriate and the hours worked appeared reasonable. We found two instances in which staff misclassified time and the error was not caught by the Project Manager. These errors were not material. We also reviewed non-labor charges to determine whether the project costs for design, engineering and other in-kind costs were coded and allocated correctly. We found no coding errors or misallocated expenditures.

The District and USACE also executed a CERP Guidance Memorandum to provide direction to the agencies when implementing the CERP program. Although the guidance was compiled for CERP, it provided overall direction for reporting the District's share of critical restoration project costs to the USACE. However, provisions of the project cooperative agreements with the USACE clearly states that Government Auditors and the District's compliance with OMB Circular A-87 – *Cost Principles for State, Local and Indian Tribal Governments* will ultimately determine the allowability of District project costs.

As part of the guidance, the District routinely submitted to the USACE a semiannual work-in-kind project report, which captured all District costs incurred for the period. The District submitted these reports since 2001 without USACE review. However recently, the USACE conducted a preliminary review of all the backlog work-in-kind reports and found that the documentation supporting a substantial amount of the District's in-kind costs was deficient and not eligible for project credit. The initial

review approved only 39% of \$6 million work-in-kind District costs. A USACE reviewer explained that the in-kind report submitted to the USACE did not provide a description of the work associated with the cost incurred, which supported the credit request. He recommended that a scope of work always accompany all in-kind credit requests, which should describe the work done, explain why these costs were incurred and how they furthered the project. We did not examine the USACE records to determine the nature of their expenditures and the adequacy of documentation supporting these records.

Subsequently, the District provided the USACE reviewer with additional support for work-in-kind project credit, which resulted in the USACE, preliminarily approving \$3.8 million of the \$6 million costs submitted for credit. The USACE will provide a formal letter approving the costs for in-kind project credit. Almost all of the remaining balance of \$2.2 million represents costs submitted to the USACE for unfinished projects. Upon completion of the projects, the USACE will review the District submitted cost support for in-kind credit approval, which will also be subject to proper documentation and USACE funding availability.

Recommendation

- 1. Collaborate with the USACE to determine the documentation requirements and reestablish an acceptable process for work-in-kind credit.**

Management Response: The need for improvements in documentation was recognized during the USACE in-kind review. A process for documenting project expenses has been initiated. This new process should reduce the USACE review effort for in-kind reports and reduce the number of disputed costs. Now that the USACE is reviewing the in-kind reports more promptly, the USACE project managers will have personal knowledge of the work being performed, which should also reduce the number of requests for detailed documentation.

This audit documented two USACE reviews covering a five-year backlog of work in-kind submittals. The USACE requested more detailed information than anticipated

based on the original agreement signed in 2000. As a result, the in-kind credit review became an iterative process that required several months to complete. Subsequent to completion of this audit, the USACE and the District worked together to resolve the disposition of the costs submitted. After the third information exchange, staffs of the two agencies are now in agreement on the disposition of all costs. Please note that at the time the audit was prepared, the USACE review was not completed. The percentage of costs to be disallowed has dropped to approximately .4%, and there is mutual agreement between the USACE and the District on the one remaining disallowed cost item. Approval of approximately \$2 million was temporarily withheld pending completion of construction of one item and Congressional approval of an increase in the federal spending cap for Critical Project Restoration. Since, Congress has recently approved an increase in the federal spending cap for Critical Project from \$75 million to \$95 million, the USACE can now re-evaluate their ability to credit these expenses under the new cap.

Responsible Department: Everglades Restoration Planning
Department

Estimated Completion Date: Completed

Eliminate Potential USACE Liability through Amendment or Other Offset

The critical project agreements between the USACE and District were intended to be 50/50 cost share arrangements. For the District's seven projects, the USACE maximum funding was approximately \$47 million. However, overruns in the Ten Mile Creek Water Preserve, Western C-11 Water Quality and Lake Okeechobee Water Retention critical projects resulted in the USACE prematurely reaching its maximum funding limitation without completing three projects, Southern Crew, Western Tamiami Culverts and Lake Trafford Restoration. The District decided to finish the projects using state and local funding, with the intent of receiving credit for these expenditures if Congress authorized an increase in the federal funding caps for critical restoration projects.

The below table summarizes critical restoration project activities:

Critical Project	Original Project Cost Estimate	USACE Actual Expenditures	District Actual Expenditures	District Estimate to Complete	District Actual Expenditures and Estimate to Complete	Project % Complete
East Coast Canal Structures	\$1,300,000	\$1,901,479	\$1,918,740	-	\$1,918,740	100%
Ten Mile Creek Water Preserve	29,066,000	19,872,402	20,354,098	\$4,607,113	24,961,211	91%
Tamiami Trail Culverts	8,336,000	2,622,127	1,182,854	-	1,182,854	100%
Western C-11 Water Quality	9,630,000	9,097,300	9,478,156	-	9,478,156	100%
Southern Crew Projects	12,021,000	7,282,214	20,832,690	7,024,906	27,857,596	90%
Lake Okeechobee Water Retention	16,360,000	10,770,380	14,706,613	1,713,840	16,420,453	99%
Lake Trafford	17,540,000	1,600,942	10,647,719	5,301,616	15,949,335	93%
Total	\$94,253,000	\$53,146,844	\$79,120,870	\$18,647,475	\$97,768,345	

* The District's excess contribution in other critical restoration projects cannot be used to offset the \$1.4 million Tamiami Trail Culvert Project deficit in which the USACE exceeded District funding without amending the project cooperative agreements.

The District's contribution towards its cost-sharing obligation surpasses that of the USACE by \$26 million. The District actual expenditures include all its in-kind costs of \$17.1 million, land certified to the USACE valued at \$29 million and cash contribution of \$33 million. The \$18.6 million estimate to complete these projects will be funded by the District. The expected District contribution at the completion of the critical restoration projects will be \$97.7 million.

The District contribution to the critical restoration projects primarily consists of cash and the land, easements, and right-of-ways necessary for the project. Credit for land contributed to the project depends on when the District purchased the land. For land owned by the District on the effective date of the agreement, the valuation is based on the fair market value as of the date that the real property interest is transferred to the USACE with the authorization to enter the property. For land purchased after the effective date of this agreement, the valuation is the fair market value at the time of purchase.

Cash and land contributed by the District towards its share of the critical projects are subject to limited USACE discretion in determining project credit. However, credit for reasonable in-kind project costs incurred by the District is based on the discretion of the federal government in determining whether the work performed substantially expedited completion of the project and the work was necessary for the project. In addition, an audit will be conducted at project completion to determine whether the costs incurred by the District are eligible for credit towards its cost-sharing obligation.

After a final audit by the USACE, if the District's contribution is determined to be less than 50%, the District will be responsible for providing a cash contribution to the USACE for the balance. If the District's contribution is determined to be more than 50%, the USACE at its discretion and availability of funds shall reimburse the District for the excess of its 50% contribution. The USACE has allocated all of its authorized expenditures for critical projects, completing six of the original nine projects. However, the Water Resource Development Act 2007 became law on November 8, 2007, which increased the USACE Critical Restoration Project authorization from \$75 million to \$95 million. The USACE may allocate some of this authorization to the District sponsored projects.

Upon completion of the project, the government will conduct a final accounting to determine the total project costs and each party's contribution. In the event that the final accounting shows that the District did not contribute 50% of the total project cost, the District is required to no later than 90 calendar days, make a cash payment to the Government for its share of the project.

According to the most current USACE records, the District may owe \$1.4 million to the USACE for their excess contribution to the Tamiami Trail Culverts project. Considering the District's current excess contribution of \$26 million towards its 50% cost-share of the seven critical projects, the District should attempt to eliminate any liability that may exist at the project's completion through an amendment or other offset.

Recommendation

- 2. Eliminate any liability that may exist when the critical projects are complete through amendment or other offset.**

Management Response: Staff will review the remaining work to be completed for the critical Restoration Projects and work with the USACE to determine how to complete the projects such that the cost share is as close to 50/50 as possible.

As noted in the audit, the District has elected to complete some Critical Restoration Projects (Lake Trafford, Southern CREW and Tamiami Culverts) on its own. This has created an imbalance in the 50/50 cost share. The District did this because the USACE was approaching its legislative spending cap for the Critical Projects. This would have prevented them from further financial participation.

Water Resource Development Act (WRDA) 2007 became law on November 8, 2007 and will help reduce this cost-share imbalance. WRDA 2007 increased the USACE authorized spending cap for Critical Restoration Projects from \$75 million to \$95 million. The USACE will allocate a portion of this increased funding to the District sponsored projects.

Each Critical Restoration Project is covered by a separate Project Cooperative Agreement, which outlines cost-sharing responsibilities for the project. Currently, there is no provision to balance the 50/50 cost-share across all of the projects. This sets up a situation where the USACE is required to request cash contributions for some projects and provide reimbursement for others. In the upcoming Water Resource Development Acts or Appropriation Bills, the District will attempt to get Congress to authorize the USACE to balance the 50/50 cost-share across all projects with the District. This would eliminate the need for cash contributions and reimbursements.

Responsible Department: Everglades Restoration Resource Area staff will take the lead in coordinating with the Government and Public Affairs Department to develop and gain Congressional support for this legislation. Everglades Restoration Planning Department will take the lead on balancing the remaining work effort.

Estimated Completion Date: Legislative changes would be included in the next Water Resource Development Act or Appropriation Bill, possibly FY 2008 or FY 2009. The schedule is controlled by the United States Congress. As a result, the District will not be able to control the timing for this item. The determination of how to balance the remaining work will be completed by the end of the second quarter of FY 2008.

Monitor Agreement Changes

In 1989, Congress created a project to improve water deliveries to the Everglades National Park known as the Modified Water Deliveries to the Everglades National Park with a \$50 million appropriation. Since authorization, the project has experienced escalating costs and project scope, the most recent estimate to complete this project is about \$400 million. The project has also been burdened with various unresolved issues that have resulted in significant delays.

According to the project cooperative agreement between the USACE and the District, the USACE will pay for construction of water control structures, levees, seepage canals and pump systems to improve water deliveries to the Everglades National Park. Completion of the project is contingent on the USACE obtaining sufficient funding and, based on discussions with District project managers; this funding has not been obtained. Construction of certain components of the CERP, cannot be started until completion of this project.

After the project is completed, the federal government will pay 100% to operate and maintain the water control structures in Water Conservation Area 3 and 75% in other project areas. The District, as local sponsor, is responsible for funding the remaining 25% of the operations and maintenance costs.

On July 27, 2001, the agreement was amended which greatly increased the District's responsibilities in this project. The following provision was added to the agreement:

“In addition to contributing 25% of the operations and maintenance costs, the local sponsor shall operate and manage at no cost to the government all lands for the project north and west of the perimeter levee

adjacent to the 8.5 square mile residential area in accordance with a jointly developed management plan consistent with the purpose of the project to maximize ecological function and structure, restore hydrological conditions, effectively control exotics species, incorporate fish and wildlife enhancement features and maintain wetlands function...”

The parties to the jointly developed management plan will be the Department of Interior, the USACE and the District. However, according to conditions stipulated in the modified project cooperative agreement, the government will provide the local sponsor the lands described above in a condition allowing for the required operation and maintenance by the local sponsor. This includes removal of all exotics and improvements, as described in option C of Section 7.4 the General Revaluation Report.

These changes and other changes that may occur in the future should be monitored, quantified and evaluated to determine if the project and increased cost continues to fit into District priorities.

Recommendation

- 3. Monitor, quantify and evaluate subsequent changes to the agreement and determine if the project and increased cost continues to fit into District priorities.**

Management Response: The Modified Water Deliveries to Everglades National Park is an important precursor to the Comprehensive Everglades Restoration Program. The District will continue to coordinate with the USACE in its implementation of the project. Once a plan is selected, the resulting operations and maintenance expenses will be determined and prioritized through the District’s standard workplan-budget development process.

Responsible Department: Watershed Management Department

Estimated Completion Date: On-going