



Transmitted via email

December 22, 2011

Mr. Jim Branham, Executive Director
Sierra Nevada Conservancy
11521 Blocker Drive, Suite 205
Auburn, CA 95603

Dear Mr. Branham:

Final Report—Pacific Forest Trust, Proposition 84 Grant Audits

The Department of Finance, Office of State Audits and Evaluations, has completed its audits of the following Pacific Forest Trust's (Trust) Proposition 84 grants:

<u>Grant Agreement</u>	<u>Audit Period</u>	<u>Awarded</u>
SNC070153	November 26, 2007 through December 31, 2009	\$ 25,000
SNC070278	April 30, 2008 through March 31, 2010	\$ 50,000
SNC070301	May 30, 2008 through June 30, 2010	\$ 75,000
SNC080131	May 19, 2009 through October 8, 2010	\$ 50,000
SNC080132	June 24, 2010 through December 24, 2010	\$500,000
SNC080133	June 24, 2010 through December 24, 2010	\$500,000

The enclosed report is for your information and use. The Trust's response to the report observation and our evaluation of the response are incorporated into this final report. This report will be placed on our website.

We appreciate the assistance and cooperation of the Trust. If you have any questions regarding this report, please contact Diana Antony, Manager, or Beliz Chappuie, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

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

Enclosure

cc: On following page

cc: Ms. Linda Hansen, Mt. Lassen Area Senior Representative, Sierra Nevada Conservancy
Mr. Patrick Kemp, Assistant Secretary for Administration and Finance, California Natural Resources Agency
Mr. Bryan Cash, Deputy Assistant Secretary, California Natural Resources Agency
Ms. Julie Alvis, Deputy Assistant Secretary, California Natural Resources Agency
Ms. Laurie Wayburn, President, Pacific Forest Trust
Mr. Peter Kodzis, Director of Finance and Administration, Pacific Forest Trust

AUDIT REPORT

Pacific Forest Trust Proposition 84 Bond Program Grant Agreements SNC-070153, 070278, 070301, 080131, 080132, 080133



View of Lemon Canyon Ranch
Source: Pacific Forest Trust

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

MEMBERS OF THE TEAM

Diana Antony, CPA
Manager

Beliz Chappuie, CPA
Supervisor

Staff
Marc Dermenjian, CFE

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

You can contact our office at:

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Office of State Audits and Evaluations
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Sacramento, CA 95814
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TABLE OF CONTENTS

Background, Scope, and Methodology.....	1
Results.....	3
Response.....	5
Evaluation of Response	8

BACKGROUND, SCOPE, AND METHODOLOGY

BACKGROUND

In November 2006, 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 provide grants to finance a variety of resource programs.

The Sierra Nevada Conservancy (Conservancy) is one of many state departments that administer Proposition 84 programs and award these funds in the form of grants. The Conservancy was created in 2004 to improve the environmental, economic, and social well-being of the Sierra Nevada and its communities. The Conservancy's region comprises all or part of 22 counties and over 25 million acres.¹

Since 1993, the Pacific Forest Trust (Trust) works with forest owners, communities, and other partners to conserve and sustain America's vital, productive forest landscapes.² The Trust received four acquisition planning grants from the Conservancy for conservation easements on the Lemon Canyon and Jamison Ranches in Sierra County, and two parcels of forested land within the Love Creek watershed in Calaveras County. Additional grant funding contributed towards the acquisition of conservation easements on the Lemon Canyon and Meadow Ranches located in Sierra County.

SCOPE

In accordance with the Department of Finance's bond oversight responsibilities, we conducted audits of the following grants:

<u>Grant Agreement</u>	<u>Audit Period</u>	<u>Awarded</u>
SNC070153	November 26, 2007 through December 31, 2009	\$ 25,000
SNC070278	April 30, 2008 through March 31, 2010	\$ 50,000
SNC070301	May 30, 2008 through June 30, 2010 ³	\$ 75,000
SNC080131	May 19, 2009 through October 8, 2010	\$ 50,000
SNC080132	June 24, 2010 through December 24, 2010	\$500,000
SNC080133	June 24, 2010 through December 24, 2010	\$500,000

The audit objective was to determine whether the Trust's grant expenditures were in compliance with applicable laws, regulations, and grant requirements. In order to design adequate procedures to evaluate fiscal compliance, we obtained an understanding of the relevant internal controls. We did not assess the efficiency or effectiveness of program operations. Further, no assessment was performed on the reasonableness of the land acquisition cost or the conservation value of the acquired land or projects completed.

The Trust's management is responsible for ensuring accurate financial reporting and compliance with applicable laws, regulations, and grant requirements as well as evaluating

¹ Conservancy website: <http://www.sierranevada.ca.gov/about-us>

² Source: Trust website: www.pacificforest.org

³ An interim audit was performed because the grant period ends March 2012.

efficiency and effectiveness of the program. The Conservancy and the California Natural Resources Agency are responsible for state-level administration of the bond programs.

METHODOLOGY

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

- Interviewed key personnel to obtain an understanding of the grant-related internal controls.
- Examined grant files, grant agreements, and applicable policies and procedures.
- Reviewed a sample of expenditures to determine if costs were allowable, grant-related, incurred within the grant period, supported by accounting records, and properly recorded.
- Determined if other revenue sources were used to reimburse expenditures already reimbursed with grant funds.

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 bond funds. The audit was conducted from January 2011 through October 2011.

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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Except as noted below, the Pacific Forest Trust's (Trust) expenditures were in compliance with applicable laws, regulations and grant requirements. The Schedules of Claimed and Questioned Amounts are presented Table 1.

Table 1: Schedules of Claimed and Questioned Amounts⁴

Grant Agreement SNC070153		
For the Period November 26, 2007 through December 31, 2009		
Category	Claimed	Questioned
Project Management	\$ 10,000	
Baseline Report/Monitoring	9,000	
Post Monitoring	6,000	
Total Expenditures	\$ 25,000	\$ 11,230

Grant Agreement SNC070278		
For the Period April 30, 2008 through March 31, 2010		
Category	Claimed	Questioned
Planning and Development	\$ 14,000	
Easement Negotiation	10,000	
Appraisal Services	15,500	
Baseline Report/Monitoring	10,500	
Total Expenditures	\$ 50,000	\$ 22,611

Grant Agreement SNC070301		
For the Period May 30, 2008 through June 30, 2010		
Category	Claimed	Questioned
Planning and Development	\$ 20,000	
Easement Negotiation	19,366	
Appraisal Services	12,290	
Baseline Report/Monitoring	0	
Total Expenditures	\$ 51,656	\$ 25,649

Grant Agreement SNC080131		
For the Period May 19, 2009 through October 8, 2010		
Category	Claimed	Questioned
Planning and Development	\$ 15,650	
Easement Negotiation	13,650	
Appraisal Services	9,000	
Baseline Report/Monitoring	11,700	
Total Expenditures	\$ 50,000	\$ 23,210

⁴ The Trust was unable to provide supporting documentation for administrative costs charged by specific category. Therefore, we reported the amounts questioned as a total expenditure.

Grant Agreement SNC080132		
For the Period June 24, 2010 through December 24, 2010		
Category	Claimed	Questioned
Easement Acquisition	\$ 500,000	
Total Expenditures	\$ 500,000	\$ 0

Grant Agreement SNC080133		
For the Period June 24, 2010 through December 24, 2010		
Category	Claimed	Questioned
Easement Acquisition	\$ 500,000	
Total Expenditures	\$ 500,000	\$ 0

Observation 1: Unsupported Salary Rates Billed

The Trust's billed rates exceeded its actual salary and benefit costs by \$82,700. The billed rates included amounts to cover administrative costs. According to the Trust, at the end of the year, the grant's excess funds are allocated to the Trust's general account to pay administrative costs. The Trust could not provide supporting documentation for the administrative costs incurred and did not have a cost allocation methodology to determine whether costs were reasonably and equitably allocated to bond projects. Although the grants allow up to 15 percent administrative costs, the costs claimed should be based on actual expenditures incurred and distributed to projects based on the relative benefits received.

Grant Agreement, section 12, *Audits/Accounting/Records*, specifically requires grantees to keep separate and complete accounting records for receipt, deposit, and payment of all project funds. It further requires grantees to maintain adequate supporting documentation sufficient in detail to provide an audit trail which will permit tracing transactions from support documentation to the accounting records to the financial reports and billings.

Recommendations:

- A. Remit \$82,700 to the Conservancy for the unsupported costs claimed. The Conservancy will make the final determination on the appropriate method to recover the questioned costs.
- B. Record all grant related revenues and expenditures in the designated grant account.
- C. Develop and implement a cost allocation methodology to equitably distribute administrative costs to programs and projects.



PACIFIC FOREST TRUST

November 1, 2011

David Botelho, CPA
Chief, Office of State Audits and Evaluations
915 L Street
Sacramento, CA 95814-3706

Dear Mr. Botelho,

Re: Draft Report on the Pacific Forest Trust, Proposition 84 Grant Audits.

Thank you for the opportunity to respond to your draft report referenced above. We appreciate all the work done by your office in connection with the audit. Our conversations with the audit staff were a valuable learning experience, and we appreciated their expertise. However, we respectfully disagree with and object to the Observation and proposed recommendations. PFT adhered to all the applicable Grants Special and General Provisions in the Grant Agreements and Prop 84 Guidelines. PFT's accounting procedures and records are independently audited annually. There have been no issues indicated as to accuracy and completeness of records, financial controls, or compliance with GAAP. We feel that the draft report's Observation #1: "Unsupported Salary Rates Billed" and its associated recommendations are incorrect. We believe that with further discussion and review of the accounting documentation we can resolve any outstanding issues.

The attached memo details why we believe this to be the case.

With many thanks for your review and consideration,

Original signed by:

Laurie A. Wayburn – President
The Pacific Forest Trust, Inc.

cc: T. Pirrung



PACIFIC FOREST TRUST

Response to the Draft Audit Report
by the California Department of Finance
Re

Proposition 84 Bond Program and Pacific Forest Trust
Grant Agreements SNC-070153, 070278, 070301, 080131, 080132, 080133

1. PFT labor rates were fair, non-discriminatory and disclosed. PFT's costs were fully documented.

During the audit, PFT provided supporting documentation for its costs, based on GAAP, which allows for allocation of indirect and general and administrative costs across projects. The Conservancy's "Final Grants Application Packet, SOG 2 Applications" did not include any rate pricing guidelines or formulas. The cost related information in Section II D and E of the packet described eligible and ineligible costs only in general terms. PFT used its best judgment to establish its hourly labor rates based on our business experience and comparative analysis of prevailing rates used by others in similar contracts and work; the rate used for the SNC grants is non-discriminatory towards the state and is the same as PFT's rates for other contracts. PFT's rates were fully disclosed in both the grant application and in the grant contract budgets. SNC accepted these for the entire grant period in question. Further, in our periodical billings, as per section 6 of the grant agreements, we included all the necessary supporting documents and restated our rates. These were never questioned and all the requested payments were approved. SNC staff were always diligent in reviewing supporting documentation. Indeed, one PFT invoice had to be revised as SNC disallowed some meal costs erroneously included. Had there been an error in our labor rates, one would hope it had been brought to light prior to this point.

2. PFT did not allocate "excess funds" to its general account to pay for administrative costs. This statement in **Observation 1** is a misrepresentation of PFT's accounting procedures. PFT's accounting software does not capture the **total labor costs** in project level accounts. It allocates only staff salary costs to each project based on an hourly amount comprised of the "annual salary" divided by 2080 hrs/year. This formula does not take into the account vacation and sick time, holidays, staff training and development time or time spent on support functions necessary to perform the tasks outlined in the grant agreement. Nor does this project level non-salary labor costs include allocation of company's retirement plan contributions, other benefits or standard administrative costs. Therefore the state auditor's inference of labor costs is incomplete and greatly understates the true labor costs. As a result, those "excess funds" were not excess, rather funds used to pay for relevant costs not reflected in PFT's project level accounts. It is an acceptable methodology, reviewed by our independent auditor as being consistent with GAAP, to allocate certain costs on a periodic or annual basis.

We would like to take this opportunity to recommend that any future Grant Application Packets and/or Agreements include guidelines for budget preparation, including desired methodologies for establishing proposed labor rates.

EVALUATION OF RESPONSE

We have reviewed Pacific Forest Trust's (Trust) response to the draft report and provide the following comments:

As noted by the Trust, its accounting software does not capture the total labor costs in the project level accounts, and the additional labor and administrative costs included in the billed rates are separately accounted for. However, because the Trust has not provided documentation for these additional costs charged to the grant, our audit observation and recommendations remain unchanged.