PPLC Meeting 11/8/10
Agenda Item 3C Handout

ALAMEDA COUNTY CONGESTION MANAGEMENT AGENCY

MANAGEMENT LETTER

YEAR ENDED JUNE 30, 2010

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ALAMEDA COUNTY CONGESTION MANAGEMENT AGENCY
Report to Management
Year Ended June 30, 2010

October 27, 2010

To the Executive Director,
Alameda County Congestion Management Agency:

In planning and performing our audit of the basic financial statements of the Alameda County Congestion Management Agency (the "Agency") for the year ended June 30, 2010, we considered the Agency's internal control in order to determine our auditing procedures for the purpose of expressing an opinion on the basic financial statements and not to provide assurance on the effectiveness of Agency's internal control. Accordingly, we do not express an opinion on the effectiveness of the Agency's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all such deficiencies have been identified.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

During our audit we also became aware of several other matters that are opportunities for strengthening internal controls and operating efficiency. The Findings and Recommendations section of this report summarizes our findings and recommendations. We previously reported on the Agency's internal control over financial reporting in our report dated October 27, 2010. The information contained herein does not affect our report dated October 27, 2010 on the basic financial statements of the Agency.

We will review the status of our recommendations during our next audit engagement. We have already discussed our recommendations with Agency management and would be pleased to discuss them further, to perform additional study of these matters, or to assist you in their implementation upon request.

This report includes certain matters that are required by auditing standards generally accepted in the United States of America to be communicated to the Agency's Audit Committee.

The accompanying findings and recommendations, and required communications are intended solely for the information and use of the Agency's Board of Directors, Audit Committee, management and others within the Agency and are not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

ALAMEDA COUNTY CONGESTION MANAGEMENT AGENCY
Report to Management
Year Ended June 30, 2010

REQUIRED COMMUNICATIONS

Professional auditing standards require auditors to communicate with the audit committee, or its equivalent, on a number of subjects. The following information satisfies these requirements, and is solely for use of the Agency's Audit Committee, Board of Directors and management.

I. Our Responsibility under U.S. Generally Accepted Auditing Standards and *OMB Circular A-133*

As stated in our engagement letter dated May 28, 2009, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

In planning and performing our audit, we considered the Agency's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with U.S. Office of Management and Budget (OMB) Circular A-133.

As part of obtaining reasonable assurance about whether the Agency's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. Also, in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the Agency's compliance with the types of compliance requirements described in *OMB Circular A-133 Compliance Supplement* applicable to each of its major federal programs for the purpose of expressing an opinion on the Agency's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the Agency's compliance with those requirements.

II. Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to the Agency in our engagement letter dated May 28, 2009.

III. Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Agency are described in the notes to the Agency's financial statements. The disclosures in the financial statements are consistent, and clear.

REQUIRED COMMUNICATIONS (Continued)

Accounting estimates are an integral part of the basic financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were depreciation estimates for capital assets and allocation of indirect costs to projects.

Management's estimate of depreciation for capital assets is based on estimated useful lives of assets and allocation of indirect costs to projects is based on methodologies required by granting agencies. We evaluated the key factors and assumptions used to develop these estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. None of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

Disagreements with Management

For purposes of this report, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting or auditing matter that could be significant to the basic financial statements or the auditors' report. No such disagreements arose during the course of our audit.

Management Representations

We have requested and received certain written representations from management in accordance with standards of the American Institute of Certified Public Accountants.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the Agency's basic financial statements or a determination of the type of auditors' opinion that may be expressed on those financial statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all relevant facts. To our knowledge, there were no such consultations with other accountants.

REQUIRED COMMUNICATIONS (Continued)

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Agency's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

FINDINGS AND RECOMMENDATIONS

1. SUNOL SMART CARPOOL LANE JOINT POWERS AUTHORITY

The Agency, along with Alameda County Transportation Improvement Authority and Santa Clara Valley Transportation Authority, created the Sunol Smart Carpool Lane Joint Powers Authority (JPA) was created in February 2006 to plan, design, construct and administer a value-pricing high-occupancy vehicle program on the Sunol Grade segment of Interstate 680. The JPA is a separate legal entity and the Agency was appointed as the managing agent. Toll lane revenue collections began in September 2010. There are several items called for in the joint powers agreement and the JPA's Administrative Code that have not yet been completed, including:

- Arrange for an annual audit of the JPA
- Prepare and adopt a capital budget
- Establish traffic flow guidelines
- Appoint a Treasurer, Auditor-Controller and Secretary
- Obtain a bond for the Treasurer
- Create SunolMAC management advisory committee
- The joint powers agreement allows the Agency to charge the JPA up to 3% of its revenues for management services provided; the Agency has not yet invoiced any amount for these services
- Present financial reports to the JPA board at least quarterly

The joint powers agreement and Administrative Code were written five years ago without full knowledge of how the JPA would be organized. Therefore there are several items in those documents, including several of the items listed above, that may need to be reconsidered.

Certain equipment and infrastructure used in JPA operations was acquired with proceeds of grants awarded to the Agency. A complete list of these assets has not been prepared. It has not been determined how to account for the "transfer" of these assets from the Agency to the JPA. The amount of replacement and rehabilitation reserves that the JPA should accumulate cannot be adequately determined until this asset list is complete.

Recommendation

The Agency should either accomplish the following items called for in the joint powers agreement and Administrative Code, or revise those documents:

- Arrange for an audit of the JPA from inception through June 30, 2011, and annually thereafter
- Prepare a capital budget
- Establish traffic flow guidelines (e.g., mile-per-hour differential between toll lane and other lanes, traffic throughput, minimum and maximum tolls, hours or operation)
- Appoint a Treasurer, Secretary and Auditor-Controller
- Obtain a bond for the Treasurer
- Create SunolMAC management advisory committee
- Reimburse Agency for management services
- Present financial reports to the JPA board at least quarterly

The Agency should identify all assets owned by the JPA, including those acquired with Agency grants, and should determine the accounting entries necessary for both the Agency and JPA to appropriately record these assets.

Agency Response

- **Arrange for an audit of the JPA from inception through June 30, 2011, and annually thereafter** – The JPA will make appropriate arrangements for an audit for the period beginning September 20, 2010 and ending June 30, 2011. Prior to the September 20, 2010 date of opening of the facility, the JPA had no revenues or expenditures.

- **Prepare a capital budget –** The two-year expenditure plan adopted by the JPA Board in August 2010 showed that there are no capital funds available for expenditure during the upcoming fiscal year. When capital funds are available, the JPA will adopt the requisite budget.

- **Establish traffic flow guidelines (e.g., mile-per-hour differential between toll lane and other lanes, traffic throughput, minimum and maximum tolls, hours or operation) –** The hours of operations and toll guidelines adopted by the JPA Board and approved by Caltrans constitute the traffic flow guidelines required by statute. The JPA intends to revise the joint powers agreement and/or administrative code to clarify this issue. Revision to the joint powers agreement and the administrative code are anticipated to be complete by summer 2011.

- **Appoint a Treasurer, Secretary and Auditor-Controller –** Agreed. These positions are scheduled for appointment at the JPA Board meeting on November 8, 2010.

- **Obtain a bond for the Treasurer –** Now that the JPA has revenues and funds of its own, the JPA will take steps to ensure that its financial interests are protected through the filing of an official bond or through appropriate insurance. It is not clear whether an official bond is required, or if this requirement can be addressed through insurance. Legal counsel is researching this issue. A recommended action is anticipated to be brought to the JPA Board in January 2011.

- **Create SunolMAC management advisory committee –** Although not consistently referenced as the SunolMAC, a management steering committee consistent with the requirements of the Joint Powers Agreement and Administrative Code was formed and met during the project development stages of the project to discuss and recommend policy issues. Over the last 12 to 15 months, this group has not met primarily because we have been in the construction phase of the project and policy issues have been brought directly to the JPA Board, which has been meeting on a more frequent basis. Staff believes that now that the project is in the operational phase, it may be appropriate to establish a Technical Advisory Committee (TAC) rather than the MAC. The Joint Powers Agreement and/or Administrative Code will be revised accordingly.

- **Reimburse Agency for management services –** To date, Agency expenses have been reimbursed through existing grants. It is anticipated that these grants will be available for reimbursement for at least the first two years of operations of the Express Lane. A recommendation on the staffing level required to support the JPA/Express Lane operations and a proposed financial plan for these activities for fiscal years 2011 and 2012 will be presented to the JPA Board in April 2011 as part of the proposed fiscal year 2011-12 budget and two-year expenditure plan.

- **Present financial reports to the JPA board at least quarterly –** Now that funds are being collected, financial reports will be presented to the JPA on a quarterly basis. The first report will be presented in February 2011 reflecting the first full quarter of operations (October – December 2010).

- **Identify and record all assets owned by the JPA, including those acquired with Agency grants -** To date, all assets acquired for operations of the Express Lane have been acquired through grants administered by the Agency. Many of the assets that will ultimately be Agency/JPA assets have not yet been "accepted" as part of the current or recently completed construction and system integration contracts. A process to transfer these assets from the Agency to the JPA or to acknowledge that the acceptance is on behalf of the JPA who will ultimately claim them as assets is being developed and will be presented to the JPA Board and ACTC Board in January 2011.

2. ACCRUAL OF EXPENSES

At the end of each fiscal year, as part of preparing the Agency's annual financial statements, the Agency accrues expenses for contractor/consultant invoices received and for estimated amounts of services rendered for which no invoices have yet been received. The Agency also accrues grant revenue for expenditures billed to but not yet collected from granting agencies and for reimbursement-eligible expenditures incurred but not yet billed to granting agencies.

Recommendation
The Agency should improve its accrual procedures by assuring that an invoice has been received for each month from every major contractor/consultant with an open contract. This can be done be examining the dates of service on the most recent invoice for each open contract. In addition, Agency management should provide project managers with additional training and prioritization to assure they provide complete and timely estimates of project expenses for which invoices have not yet been received to the accounting department.

Agency Response
Although the Agency concurs and will comply with these recommendations, it should be noted that this is the third consecutive year this recommendation has appeared in our Management Letter. During this time, the Agency has made significant improvements in reducing the amount of accrued expenses at year end; however, it cannot compel consultants to submit timely invoices. The Agency has worked with project managers to communicate with each of their consultants to submit invoices, or estimates, of work completed prior to June 30. We have also modified contract language to include requirements that contractors submit monthly invoices. We will continue to do all that we can to minimize the amount of year end accruals, but cannot offer assurance that the issue will be completely resolved. It is also important to note that while the incomplete accrual of expenses is a concern, since the accrual of the associated grant revenues also does not occur, there is no net financial impact on the Agency's financial statements.

3. COMPREHENSIVE ANNUAL FINANCIAL REPORT

The Agency's basic financial statements meet its external financial reporting requirements. These basic financial statements include a management's discussion and analysis, government wide financial statements, fund financial statements and related note disclosures. The Agency may wish to prepare a more thorough version of its annual audited financial report, called a comprehensive annual financial report (CAFR). A CAFR would add two new sections:

- A statistical section showing multi-year trend information and non-financial data that is useful in evaluating economic condition, and
- A transmittal letter providing a profile of the government, an overview of the local economy, and the Agency's major initiatives and projects.

Governments that prepare a CAFR frequently submit it to the Government Finance Officers Association (GFOA) for consideration for a Certificate of Achievement for Excellence in Financial Reporting. The certificate from GFOA adds an additional level of credibility to the financial statements.

Recommendation
As the Alameda County Transportation Commission establishes its financial reporting procedures and reports, it should consider preparing a CAFR and participating in the GFOA's Certificate of Achievement for Excellence in Financial Reporting program.

Agency Response
The Agency has merged with the Alameda County Transportation Improvement Agency. However, during the current fiscal year, FY 2010/2011, both predecessor agencies are maintaining their own independent budgets. As a consequence, the Agency believes the decision to prepare a CAFR should be postponed until the spring of 2011 when the new agency, the Alameda County Transportation Agency, is fully implemented and has an adopted consolidated budget and combined financial operations.