Bay Area Air Quality Management District

Performance Audit

Report No. 24-3900-074
March 2025

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Transmitted via e-mail

March 14, 2025

Jack Kitowski, Division Chief
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Final Report—Bay Area Air Quality Management District Fiscal Compliance Audit

The California Department of Finance, Office of State Audits and Evaluations, has completed its fiscal compliance audit of the Bay Area Air Quality Management District's implementation of the California Air Resources Board air pollution reduction incentive programs.

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

If you have any questions regarding this report, please contact David Shockey, Manager, or Robert Scott, Supervisor, at (916) 322-2985.

Sincerely,

Original signed by:

Cheryl L. McCormick, CPA
Chief, Office of State Audits and Evaluations

cc: On following page

cc: Lucina Negrete, Assistant Division Chief, Mobile Source Control Division, California Air Resources Board
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BACKGROUND, SCOPE, AND METHODOLOGY

BACKGROUND

The California Air Resources Board (CARB) administers state-level financial incentive programs with the aim to reduce emissions from on- and off-road vehicles and equipment. Vehicle and equipment owners apply for funds through local air quality management districts or air pollution control districts. While CARB is responsible for program oversight, districts implement the incentive programs.[1]

The Bay Area Air Quality Management District is 1 of 35 air districts partnering with CARB to improve air quality through implementing CARB's air pollution reduction incentive programs. The District regulates air pollution sources in the nine counties surrounding the San Francisco Bay: Alameda, Contra Costa, Marin, Napa, San Francisco, San Mateo, Santa Clara, southwestern Solano, and southern Sonoma counties. It is governed by a 24-member board of directors composed of locally elected officials from each of the nine Bay Area counties, with the number of board members from each county being proportionate to its population.[2]

The District shares responsibility with CARB for ensuring state and federal air quality standards are achieved and maintained. The District receives incentive program funds from CARB through grants. The grants provide the District funding to offset program implementation costs and reimburse applicants for replacing or retrofitting vehicles or equipment with low-emission vehicles or equipment. Districts are required to follow CARB-approved program guidelines for implementing programs.[3]

The District participates in the six incentive programs detailed in Table 1.

Table 1: Incentive Programs

Carl Moyer Memorial Air Quality Standards Attainment Program (CMP)	CMP contributes to cleaner air by funding the incremental costs of retrofitting older engines with cleaner-than-required engines and equipment. Eligible equipment includes medium and heavy-duty trucks and buses, mobile agricultural and construction equipment, marine vessels, locomotives, and school buses. Public or private entities operating eligible engines or equipment within the District's jurisdiction participate by applying for a grant. CMP requires a 15-percent match of local funds.[4]

[1] Excerpts obtained from https://ww2.arb.ca.gov/our-work/topics/incentives.
[2] Excerpts obtained from https://www.baaqmd.gov/en/about-the-air-district.
[3] Excerpts obtained from https://ww2.arb.ca.gov/california-air-districts.
[4] Excepts obtained from https://ww2.arb.ca.gov/our-work/programs/carl-moyer-memorial-air-quality-standards-attainment-program.

Community Air Protection Incentives (CAP)	CAP focuses on reducing exposure in communities most impacted by air pollution. The District prioritizes projects that reduce emissions in the District's most impacted communities, including West Oakland, Richmond-San Pablo, East Oakland, Bayview Hunters Point/Southeast San Francisco, and disadvantaged and low-income communities as designated by California Climate Investments. Eligible project types include mobile sources and infrastructure projects also eligible under the CMP.[5]
Clean Cars 4 All (CC4A)	CC4A provides incentives to help lower-income consumers living in priority populations replace their old, higher-polluting vehicles with newer, cleaner transportation. Participants can purchase or lease a new or used hybrid electric vehicle, plug-in hybrid electric vehicle, zero-emission vehicle, or zero-emission motorcycle.[6]
Funding Agricultural Replacement Measures for Emission Reductions (FARMER)	FARMER provides funding through local air districts for agricultural harvesting equipment, heavy-duty trucks, agricultural pump engines, tractors, and other equipment used in agricultural operations.[7]
Low Carbon Transportation/Air Quality Improvement Program (LCT/AQIP)	LCT/AQIP provides mobile source incentives to reduce greenhouse gas, criteria pollutant, and toxic air contaminant emissions by deploying advanced technology and clean transportation.[8]
Volkswagen Environmental Mitigation Trust for California (VWM)	VWM provides about $423 million for California to mitigate the excess nitrogen oxide emissions caused by Volkswagen's use of illegal emissions testing defeat devices in certain Volkswagen diesel vehicles.[9]

SCOPE

At the request of CARB, the California Department of Finance, Office of State Audits and Evaluations, conducted a fiscal grant compliance audit of the District's implementation of CARB's air pollution reduction incentive programs. The audit included the incentive programs and fiscal years detailed in Table 2.

Table 2: Funding Received by Incentive Program and Fiscal Year

	Fiscal Year						
Incentive Program	**2015-16**	**2016-17**	**2017-18**	**2018-19**	**2019-20**	**2020-21**	**2021-22**
CMP	✓	✓	✓	✓	✓	✓	✓
CAP			✓	✓	✓		✓
CC4A		✓	✓	✓		✓	✓
FARMER			✓	✓	✓		✓
LCT/AQIP		✓					
VWM				✓			

[5] Excerpts obtained from https://ww2.arb.ca.gov/capp/fund/capi/community-air-protection-incentives.
[6] Excerpts obtained from https://ww2.arb.ca.gov/our-work/programs/clean-cars-4-all.
[7] Excerpts obtained from https://ww2.arb.ca.gov/our-work/programs/farmer-program.
[8] Excerpts obtained from https://ww2.arb.ca.gov/our-work/programs/low-carbon-transportation-incentives-and-air-quality-improvement-program.
[9] Excerpts obtained from https://ww2.arb.ca.gov/our-work/programs/volkswagen-environmental-mitigation-trust-california.

The audit objective was to determine whether the incentive programs' revenues, expenditures, and resulting balances as of June 30, 2022, for the incentive programs and respective fiscal years identified in Table 2, were in compliance with applicable grant agreements, program guidelines, and statutes.

The District's management is responsible for ensuring accurate financial reporting and compliance with applicable grant agreements, program guidelines, and statutes. CARB and the District are responsible for the state and local administration of the incentive programs.

METHODOLOGY

To plan the audit, we gained an understanding of the programs, and identified relevant criteria, by interviewing CARB and District personnel, reviewing the executed agreements and amendments, funding plans, program guidelines, CARB website, and applicable statutes.

We conducted a risk assessment, including evaluating whether the District's key internal controls significant to our audit objective were properly designed, implemented, and operating effectively. Key internal controls evaluated focused on the review and approval process for expenditures, interest revenue calculation and allocation, reimbursement request preparation, and fund liquidation. Our assessment included conducting interviews with District personnel and testing transactions related to expenditures, interest revenue, and resulting balances.

Additionally, we assessed the reliability of the expenditure and revenue ledgers and payroll statements generated from the District's accounting system, Oracle's JD Edwards, and its payroll system, Dayforce. To assess the reliability of revenue and expenditure detail schedules generated by these systems, we interviewed District staff, reviewed information process flows and administrative operating and finance office procedure manuals, examined existing reports and documents, traced and agreed detail expenditure, revenue, and payroll transactions to source documents such as vendor invoices, timesheets, pay statements and disbursement records, indirect cost allocation worksheets, interest income allocation worksheets and bank statements, and to grant agreements, service contracts and approved purchase orders. We determined that the detailed expenditure and revenue ledgers, and payroll statements were sufficiently reliable to address the audit objective.

Based on the results of our planning, we developed specific methods for gathering evidence to obtain reasonable assurance to address the audit objective. Our methods are detailed in the Table of Methodologies.

Table of Methodologies

Audit Objective: To determine whether the incentive programs' revenues, expenditures, and resulting balances were in compliance with applicable grant agreements, program guidelines, and statutes.
Methods

• Randomly selected 38 of 2,888 project expenditures from all incentive programs across all funding fiscal years and 2 project expenditures deemed high-risk. Determined the following:
  o Grant and interest income funded expenditures were allowable, grant-related, authorized, supported, and incurred within the grant period by reviewing grant agreements, project contracts, District accounting records, vendor invoices, and checks, and comparing to relevant criteria.
  o Match-funded expenditures were allowable, grant-related, supported, and incurred within the grant period by reviewing grant agreements, project contracts, District records, and vendor invoices, and comparing to relevant criteria.
• Randomly selected 85 program administrative expenditures assessed as low-risk and 2,970 administrative expenditures assessed as high-risk from 7,874 District direct labor costs and third-party vendor transactions across all incentive programs and all funding fiscal years. Determined if selected expenditures were allowable, authorized, coded to an eligible funding program, supported, and incurred within the grant period by reviewing employee pay statements, grant agreements, invoices, timesheet hours and dollars, and approved year-end journal entries, and comparing to relevant criteria.
• Selected 100 percent of all 27 grants' indirect cost dollars charged to administration funds and recalculated the allowable indirect cost dollars recoverable by applying the District-approved indirect cost rate to direct labor dollars to ensure the amount charged to administration funds is equal to or less than the amount allowable. Additionally, we reviewed cost categories and cost pools included in the indirect cost rate to ensure the costs were not prohibited or also included as a direct cost category.
• Selected 100 percent of the three expired grants requiring match contributions and determined if match funding requirements were met by scheduling program revenues and expenditures, including match expenditures, and comparing to match requirements in relevant criteria.
• Selected 100 percent of all 27 grant revenues for project and administration funds and traced and agreed allocations from District revenue ledgers to the grant agreements.
• Randomly selected 5 of 487 interest revenue allocations across all programs and fiscal years and determined if interest revenue was earned and equitably allocated to the appropriate programs and grants by reviewing San Mateo County interest apportionment reports and District accounting records.
• Selected 100 percent of the 27 expired grants and determined whether the District was required to remit any expired grant unused funds by reviewing grant agreements and accounting records and comparing them to relevant criteria.

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

CONCLUSION

Based on the procedures performed and evidence gathered, we obtained reasonable assurance the incentive programs' revenues, expenditures, and resulting balances as of June 30, 2022, were in compliance with applicable grant agreements, program guidelines, and statutes, except as noted in Findings 1 and 2. Revenues, expenditures, and resulting balances as of June 30, 2022, by program and fiscal year for CMP, CAP, CC4A, FARMER, LCT/AQIP, and VWM are detailed in Appendix A.

FINDINGS AND RECOMMENDATIONS

Finding 1: Unallowable Method Used to Recover Employee Paid Time Off

The District recorded and reimbursed direct labor costs totaling $1,135,812 across six incentive programs throughout the audit period for employee paid time off (PTO), including vacation, holidays, and sick leave. Specifically, District employee PTO hours were directly charged to programs during the period in which the leave was taken and not the period in which it was accrued. Additionally, PTO hours were charged as direct labor hours and were not included in the fringe benefit rate or a fully loaded rate. As a result, PTO costs were not applied to the appropriate programs and periods corresponding to when employees accrued the PTO. Further, the District records indirect costs for all direct labor hours based on calculated and internally approved indirect cost rates. The related indirect costs for these PTO hours were similarly charged to periods where leave was taken rather than accrued. See Table 3 for a summary of impacted PTO costs by program, including the related indirect costs.

Table 3: Paid Time Off Costs by Incentive Program

Incentive Programs	PTO Costs	Indirect Costs	Total PTO and Indirect Costs
CMP	$ 17,514	$ 9,078	$ 26,592
CAP	585,038	252,414	837,452
CC4A	140,549	36,636	177,185
FARMER	27,053	4,174	31,227
LCT/AQIP	11,442	0	11,442
VWM	49,875	2,039	51,914
Total	**$ 831,471**	**$ 304,341**	**$ 1,135,812**

Grant agreements and incentive program guidelines[10] permit the District to recover actual employee hourly costs for incentive program implementation and monitoring activities and require the District to comply with Generally Accepted Accounting Principles (GAAP), which include Governmental Accounting Standards Board (GASB) pronouncements. GASB Statement 16 paragraph 6 states a liability for compensated absences should be accrued

[10] Grant Agreements in the *Fiscal Management Systems and Accounting Standards* paragraph, Carl Moyer Program Guidelines, 2017 Revision, Chapter 3, Part K, Community Air Protection Incentives 2019 Guidelines, Chapter 2, Part F, paragraph 1, FARMER Program Guidelines, Chapter 4, Part 1.

as employees earn the rights to the benefits. Accounting for compensated absences as a fringe benefit would be considered allowable per GASB standards and reporting practices. For example, the FARMER reporting template notes Fringe Costs as those that "generally refer to benefits (e.g., health benefits, paid time-off, etc.)" However, the District's employee PTO costs were not charged as fringe benefits when the employee accrued PTO hours, but as direct labor hours when the employee used PTO hours for implementing or monitoring program activities.

The District stated that charging incentive program funds for PTO costs when used instead of accrued has been its practice for several years and that PTO is appropriately allocated to each program by the Dayforce payroll system. However, PTO is an employee benefit that is accrued when earned and chargeable to funding sources from the period earned and is not a cost that can be charged when the employee uses the PTO. Therefore, the District could not demonstrate the PTO costs charged to the respective incentive program funds and fiscal year (i.e., grants) are equitable, allowable, grant-related, and incurred within the grant period.

Recommendations:

A. Collaborate with CARB and revise the fringe benefits allocation to include PTO when accrued to determine the appropriate benefits charged to the respective incentive programs and fiscal years to offset the $1,135,812 in questioned costs. Alternatively, identify other incentive program implementation allowable costs to substitute for the questioned PTO costs summarized above.

B. Develop and implement procedures to ensure incentive program grant funds charged for billable PTO direct labor program implementation and monitoring activity costs comply with grant requirements and GAAP.

Finding 2: Grant Match Funding Requirement Was Not Met Within the Grant Period

For LCT/AQIP, the District did not meet the grant match requirement. Specifically, the District reported incurring $1,040,814 of the $1,697,362 (61.3 percent) of the local match funding required and did not obtain written authorization to modify or extend the grant scope and/or schedule by the performance end date of December 31, 2020. As part of a competitive incentive program fund awarding process, the District executed Grant G16-ZTRK-01, which required the District to match its $2,738,557 grant incentive program funds with $1,697,362 of local District funding or in-kind match cost dollars by the grant performance end date.

The District's match was third-party operating costs of "advanced technology pilot" vehicles purchased with grant funds. The District stated that the third party had difficulties deploying and operating the purchased vehicles because of new technology implementation challenges and the negative economic activity impact of the COVID-19 pandemic on operating the purchased vehicles. Additionally, the District stated it expected match funding requirements to be met after the grant period, as it would require an additional three years of vehicle operation to meet its mileage and use requirements. Although the District communicated the challenges with meeting its match requirement, it did not request or receive written approval from CARB to extend the grant beyond the December 31, 2020, performance end-period date.

Grant G16-ZTRK-01, Exhibit A, Section 1.3, and Exhibit B required $1,697,362 in local District match. Per grant amendment 2, the timeline for the District to achieve fiscal and program grant goals was December 31, 2020. Additionally, grant agreement sections 5.2, 5.6, and 10.1 state that changes in the project scope and/or schedule require written approval or a grant agreement amendment made in writing and signed by both parties.

Recommendations:

A. Collaborate with CARB to ensure grant deliverables and outcomes are achieved through data collection, monitoring, and documentation, ensuring CARB has a complete record of achieved fiscal and program benefits, including match funding requirements.

B. Develop and implement procedures to ensure match requirements and deliverables are achieved within specified timelines or amend grant terms and timelines in accordance with the grant agreement.

Schedule 1: CMP Summary

Moyer Year	Fiscal Year	Total Revenue	Total Expenditures (Excluding Match)	Resulting Balance[11, 12, 13]
18	2015-16	$ 7,328,750	$ 7,334,689	$ (5,939)
19	2016-17	7,385,125	7,445,315	(60,190)
20	2017-18	7,904,413	7,875,024	29,389
20 State Reserve[14]	2017-18	1,117,592	1,047,743	69,849
21	2018-19	8,899,261	8,153,706	745,555
21 State Reserve	2018-19	1,294,001	1,270,701	23,300
22	2019-20	10,820,611	2,121,690	8,698,921
22 State Reserve	2019-20	1,482,523	375,358	1,107,165
23	2020-21	10,186,967	12,807	10,174,160
23 State Reserve	2020-21	1,449,760	0	1,449,760
24	2021-22	28,627,171	8,927	28,618,244
24 State Reserve	2021-22	4,800,000	0	4,800,000

[11] Health and Safety Code section 44287, subdivision (j) states funds not liquidated by the District by June 30 of the fourth calendar year following the date of the reservation shall be returned to CARB. Resulting balances were not yet required to be expended as of the end of the audit period, June 30, 2022, for Moyer Years 21, 22, 23, and 24.

[12] The negative grant balances for Moyer Year 18 and 19 are due to interest revenue earned and recorded in prior periods and expended in subsequent periods, and may result in the appearance of a negative grant balance.

[13] Moyer Year 20 balances are attributed to interest income earned in 2017-18 from prior Moyer Year grant balances and expended subsequently within applicable Moyer Year liquidation dates.

[14] State Reserve funds are a portion of the CMP funds set aside to provide monetary grants focusing on a specific project type(s).

Schedule 2: CMP Revenue

Moyer Year	Fiscal Year	Program Funds	Administrative Funds	Interest Revenue[15]	Total Revenue
18	2015-16	$ 6,817,150	$ 454,477	$ 57,123	$ 7,328,750
19	2016-17	6,874,030	458,269	52,826	7,385,125
20	2017-18	7,309,435	487,296	107,682	7,904,413
20 State Reserve	2017-18	1,047,743	69,849	0	1,117,592
21	2018-19	8,153,662	543,578	202,021	8,899,261
21 State Reserve	2018-19	1,213,126	80,875	0	1,294,001
22	2019-20	9,946,715	663,114	210,782	10,820,611
22 State Reserve	2019-20	1,389,865	92,658	0	1,482,523
23	2020-21	9,358,173	623,878	204,916	10,186,967
23 State Reserve	2020-21	1,359,150	90,610	0	1,449,760
24	2021-22	26,704,063	1,780,271	142,837	28,627,171
24 State Reserve	2021-22	4,500,000	300,000	0	4,800,000

Schedule 3: CMP Expenditures[16]

Moyer Year	Fiscal Year	Project Expenditures	Administrative Expenditures[17]	Total Expenditures (Excluding Match)	Match Expenditures	Total Expenditures
18	2015-16	$ 6,880,212	$ 454,477	$ 7,334,689	$ 1,090,744	$ 8,425,433
19	2016-17	6,983,979	461,336	7,445,315	1,099,845	8,545,160
20	2017-18	7,309,432	565,592	7,875,024	1,169,510	9,044,534
20 State Reserve	2017-18	1,047,743	0	1,047,743	0	1,047,743
21	2018-19	7,594,369	559,337	8,153,706	1,304,586	9,458,292
21 State Reserve	2018-19	1,189,825	80,876	1,270,701	0	1,270,701
22	2019-20	1,495,063	626,627	2,121,690	0	2,121,690
22 State Reserve	2019-20	282,700	92,658	375,358	0	375,358
23	2020-21	0	12,807	12,807	0	12,807
23 State Reserve	2020-21	0	0	0	0	0
24	2021-22	0	8,927	8,927	0	8,927
24 State Reserve	2021-22	0	0	0	0	0

[15] CMP interest earned is reported as a lump sum figure for all grants including State Reserve funds.
[16] Interest expenditures related to project and administration costs are incorporated into those columns.
[17] Administrative expenditures presented reflect amounts in the District's accounting records and are not adjusted for potential changes as a result of Finding 1.

Schedule 4: CAP Summary

Grant Number	Fiscal Year	Total Revenue	Total Expenditures	Resulting Balance[18]
G17-MCAP-03	2017-18	$ 50,016,894	$ 49,813,660	$ 203,234
G18-MCAP-01	2018-19	40,240,309	23,507,150	16,733,159
G19-MCAP-01	2019-20	31,339,402	1,429,106	29,910,296
G21-MCAP-02	2021-22	39,095,429	0	39,095,429

Schedule 5: CAP Revenue

Grant Number	Fiscal Year	Project Funds	Administrative Funds	Interest Revenue	Total Revenue
G17-MCAP-03	2017-18	$ 46,875,000	$ 3,125,000	$ 16,894	$ 50,016,894
G18-MCAP-01	2018-19	37,312,500	2,487,500	440,309	40,240,309
G19-MCAP-01	2019-20	28,491,219	1,899,414	948,769	31,339,402
G21-MCAP-02	2021-22	35,438,366	2,362,558	1,294,505	39,095,429

Schedule 6: CAP Expenditures[19]

Grant Number	Fiscal Year	Project Expenditures	Administrative Expenditures[20]	Total Expenditures
G17-MCAP-03	2017-18	$ 46,594,302	$ 3,219,358	$ 49,813,660
G18-MCAP-01	2018-19	21,123,377	2,383,773	23,507,150
G19-MCAP-01	2019-20	734,050	695,056	1,429,106
G21-MCAP-02	2021-22	0	0	0

Schedule 7: CC4A Summary

Grant Number	Fiscal Year	Total Revenue	Total Expenditures	Resulting Balance[21]
G16-LCTI-04	2016-17	$ 5,075,887	$ 5,075,887	$ 0
G17-VW-01-1	2017-18	5,021,457	5,021,457	0
G18-PLUS-03	2018-19	4,016,363	4,016,363	0
G20-PLUS-03-03	2020-21	3,009,098	2,466,629	542,469
G21-CC4A-03	2021-22	18,019,972	1,948,223	16,071,749

[18] The District has until June 30, 2023, 2024, 2025, and 2026 to expend or remit resulting balances to CARB for 2017-18, 2018-19, 2019-20, and 2021-22, respectively.
[19] Interest expenditures related to project and administration costs are incorporated into those columns.
[20] Administrative expenditures presented reflect amounts in the District's accounting records and are not adjusted for potential changes as a result of Finding 1.
[21] The District has until June 30, 2023 and 2025 to expend or remit the resulting balances to CARB for 2020-21 and 2021-22, respectively.

Schedule 8: CC4A Revenue

Grant Number	Fiscal Year	Project Funds	Administrative Funds	Interest Revenue	Total Revenue
G16-LCTI-04	2016-17	$ 4,250,000	$ 750,000	$ 75,887	$ 5,075,887
G17-VW-01-1	2017-18	4,250,000	750,000	21,457	5,021,457
G18-PLUS-03	2018-19	3,400,000	600,000	16,363	4,016,363
G20-PLUS-03-03	2020-21	2,550,000	450,000	9,098	3,009,098
G21-CC4A-03	2021-22	15,300,000	2,700,000	19,972	18,019,972

Schedule 9: CC4A Expenditures[22]

Grant Number	Fiscal Year	Project Expenditures	Administrative Expenditures[23]	Total Expenditures
G16-LCTI-04	2016-17	$ 4,324,851	$ 751,036	$ 5,075,887
G17-VW-01-1	2017-18	4,275,487	745,970	5,021,457
G18-PLUS-03	2018-19	3,417,392	598,971	4,016,363
G20-PLUS-03-03	2020-21	2,066,264	400,365	2,466,629
G21-CC4A-03	2021-22	1,506,000	442,223	1,948,223

Schedule 10: FARMER Summary

Grant Number	Fiscal Year	Total Revenue	Total Expenditures	Resulting Balance[24]
G17-AGIP-02	2017-18	$ 2,024,732	$ 2,024,732	$ 0
G18-AGIP-07	2018-19	1,950,274	1,836,370	113,904
G19-AGIP-02	2019-20	815,316	444,633	370,683
G21-AGIP-01	2021-22	3,756,900	0	3,756,900

Schedule 11: FARMER Revenue

Grant Number	Fiscal Year	Project Funds	Administrative Funds	Interest Revenue	Total Revenue
G17-AGIP-02	2017-18	$ 1,866,375	$ 124,425	$ 33,932	$ 2,024,732
G18-AGIP-07	2018-19	1,802,522	120,168	27,584	1,950,274
G19-AGIP-02	2019-20	757,652	50,510	7,154	815,316
G21-AGIP-01	2021-22	3,522,093	234,807	0	3,756,900

[22] Interest expenditures related to project and administration costs are incorporated into those columns.
[23] Administrative expenditures presented reflect amounts in the District's accounting records and are not adjusted for potential changes as a result of Finding 1.
[24] The District has until June 30, 2023, 2024, and 2026 to expend or remit the resulting balances to CARB for 2018-19, 2019-20, and 2021-22, respectively.

Schedule 12: FARMER Expenditures[25]

Grant Number	Fiscal Year	Project Expenditures	Administrative Expenditures[26]	Total Expenditures
G17-AGIP-02	2017-18	$ 1,898,413	$ 126,319	$ 2,024,732
G18-AGIP-07	2018-19	1,714,635	121,735	1,836,370
G19-AGIP-02	2019-20	400,580	44,053	444,633
G21-AGIP-01	2021-22	0	0	0

Schedule 13: LCT/AQIP Expenditures[27]

Grant Number	Fiscal Year	Project Expenditures	Administrative Expenditures[28]	Match – In-Kind[29]	Match – Funds[30]	Total
G16-ZTRK-01[31]	2016-17	$ 2,600,460	$ 136,696	$ 258,981	$ 781,833	$ 3,777,970

Schedule 14: VWM Summary

Grant Number	Fiscal Year	Total Revenue	Total Expenditures	Resulting Balance[32]
G18-VWM-03	2018-19	$ 11,042,292	$ 1,448,431	$ 9,593,861

Schedule 15: VWM Revenue

Grant Number	Fiscal Year	Project Funds	Administrative Funds	Interest Revenue	Total Revenue
G18-VWM-03	2018-19	$ 10,000,000	$ 1,000,000	$ 42,292	$ 11,042,292

Schedule 16: VWM Expenditures[33]

Grant Number	Fiscal Year	Project Expenditures	Administrative Expenditures[34]	Total Expenditures
G18-VWM-03	2018-19	$ 962,095	$ 486,336	$1,448,431

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25 Interest expenditures related to project and administration costs are incorporated into those columns.
26 Administrative expenditures presented reflect amounts in the District's accounting records and are not adjusted for potential changes as a result of Finding 1.
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28 Administrative expenditures presented reflect amounts in the District's accounting records and are not adjusted for potential changes as a result of Finding 1.
29 The District did not meet the match funding requirement, as noted in Finding 2.
30 Ibid.
31 The Zero Emission Truck Pilot Commercial Deployment Projects grant award was $2,738,557. The District filed four reimbursement claims totaling $2,737,156 (Project plus Administrative Expenditures), leaving an expired grant balance of $1,401.
32 The District has until May 24, 2028 to expend or remit the resulting balance to CARB.
33 Interest expenditures related to project and administration costs are incorporated into those columns.
34 Administrative expenditures presented reflect amounts in the District's accounting records and are not adjusted for potential changes as a result of Finding 1.

February 26, 2025

VIA ELECTRONIC MAIL (OSAEReports@dof.ca.gov)
Cheryl L. McCormick, CPA
Chief, Office of State Audits and Evaluations
915 L Street
Sacramento, CA 95814-3706

Re: Draft Report No. 24-3900-074, Bay Area Air Quality Management District, Fiscal Compliance Audit

Dear Ms. McCormick,

We are in receipt of the above-referenced draft report, dated February 11, 2025, from the California Department of Finance, Office of State Audits and Evaluations (Department of Finance) concerning implementation of the California Air Resources Board (CARB) air pollution reduction incentive programs.

The Bay Area Air Quality Management District (Air District) appreciates your entire audit team's thorough review and efforts invested in ensuring compliance with applicable grant guidelines. We set forth below Air District responses to the Findings and the Recommendations:

Finding 1: Unallowable Method Used to Recover Employee Paid Time Off

Due to the lack of clarity on the criteria being cited and the absence of specific guidelines on how leave time must be charged, we request that this finding be reclassified as a recommendation.

The Air District's financial records are independently audited to ensure compliance with Generally Accepted Accounting Principles (GAAP), including Governmental Accounting Standards Board (GASB) pronouncements. GAAP is a set of standardized guidelines for financial accounting and reporting in the United States that ensures consistency and transparency, and it serves as a "gold standard" for financial practices in America.

The Air District reports accrued paid time off (PTO) in its annually audited financial statements, which are reviewed by an independent auditor to ensure compliance with GAAP. However, GAAP and GASB only require the accrued PTO to be reported as a liability for financial purposes and does not mandate expense recognition at the time of accrual. The Air District uses the modified accrual basis of accounting to report PTO liability, recording it as a long-term debt in its financial report as cited in and supported by GASB Statement 16 paragraph 6: "for governmental and similar trust funds, only the current portion of the liability should be reported in the funds; the remainder of the liability should be reported in the General Long-Term Debt Account Group (GLTDAG) and compensated absences expenditures should be recognized using a modified accrual basis of accounting."

The **modified accrual basis of accounting** is a method used primarily by government agencies for financial reporting. It combines elements of both **cash basis** and **full accrual basis** accounting. As noted in the Air District's audited financial statement, "Expenditures of the governmental funds are generally recognized when the related fund liability is incurred, except debt service expenditures and expenditures related to compensated absences (also known as PTO) which are recognized when the payment is due."

While we agree with the auditor that PTO is an eligible cost, the difference of opinion arises on how and when PTO is charged to the grant programs. Importantly, neither GAAP, nor GASB nor any of the individual grant programs mandate any certain method for when PTO is recognized.

Grant agreements and incentive program guidelines permit the Air District to recover actual employee hourly costs for staff that are directly assigned to the grants program. **The guidance and contractual requirements from *CARB clearly allow for cost-recovery of staff time who work directly on grant programs. They, however, do not specify the method for charging leave time, so we believe the method employed by the Air District, which charges the grant program when time is used, rather than when it's accrued, is an allowable, accurate and transparent method of accounting that is supported by GAAP and GASB.***

Specifically, we disagree with the auditor's assertion that grant programs must be billed at the time PTO is accrued. Charging at the time of accrual could lead to situations where costs are allocated to a grant program even if the employee later leaves the program or separates from employment before using the accrued leave. Our approach—charging the grant program only when leave is taken—ensures that costs are assigned to the appropriate program based on actual usage, thereby maintaining accuracy and accountability.

Furthermore, we strongly disagree with the auditor's statement that "the Air District could not demonstrate the PTO costs charged to the respective incentive program funds and fiscal year (i.e., grants) are equitable, allowable, grant-related, and incurred within the grant period." All staff hours, including leave hours, are meticulously tracked through our Dayforce payroll system and written procedures. Our time-tracking system proportionally allocates all compensated hours—including leave—across the funding sources that benefit from the employee's work for the pay period. The system takes the PTO hours taken in a given pay period and allocates the PTO proportionately using the hours worked on each grant during the pay period. This methodology ensures an equitable distribution of costs based on actual work contributions.

- As to **Recommendation A**, while the methodology used by the Air District for over twenty years (20) has been consistently applied and previously accepted during DOF audits and reporting submittal and reviews by CARB, the Air District agrees to work with CARB to account for the $1,135,812 in questioned, paid time off (PTO) costs. The auditor did not acknowledge the Air District subsidized the grant programs and did not charge the full amount of indirect costs to the grants, which would have fully covered the amount questioned. The Air District also agrees to work with CARB to develop guidance on how to charge billable PTO hours going forward.
- As to **Recommendation B,** the Air District's financial statements and procedures are audited annually by an independent auditor, consistently confirming compliance with Generally Accepted Accounting Principles (GAAP). In accordance with GAAP, the Air District records accrued PTO as a liability when it is earned on its annual financial

statement. However, the associated expense is only recognized when an employee utilizes the accrued sick or vacation leave. This practice is consistent with GAAP, GASB and federal grants, where the expenditure is typically charged when the expense is paid rather than when it is earned or obligated.

Finding 2: Grant Match Funding Requirement was not met within the grant period

We do not agree that the issue should be a Finding because we believe there was approval by CARB to consider expenses incurred after the term in the agreement. Although a portion of the Air District's match requirement was met after the original term of the contract with CARB, we believed there was approval by CARB for us meeting the remaining match requirement within the term of the Air District's agreement with Goodwill and BYD (that ended in December 2022). Additionally, we also provided more matches than what was required, as detailed below.

The Bay Area Air District and its partners, Goodwill and BYD, were awarded $2,738,557 in Low Carbon Transportation/Air Quality Improvement Program (LCT/AQIP project) by CARB on February 15, 2017, for a pilot project to build 11 first-generation electric delivery and refuse trucks and demonstrate the feasibility of operating this leading-edge technology in the field. BYD, our technology partner, was an early manufacturer of heavy-duty electric trucks and buses, and Goodwill, our operations and community partner, is a nonprofit organization that provides job training, employment placement, and other community-based services, including reuse and recovery services through its network of thrift stores. To support this project in 2018, the Air District executed a three-party contract with Goodwill and BYD that included all requirements from CARB, plus a provision for two additional years of vehicle operation, and a retainer of $151,430 to be paid by the Air District as match once all operational requirements were met.

The audit report states that "the third party had difficulties deploying and operating the purchased vehicles due to new technology implementation challenges and the negative economic impact of the COVID-19 pandemic." To clarify, while significant challenges and delays were experienced during the project's implementation, the Air District and our partners successfully addressed and resolved these issues through perseverance and close collaboration. However, the global COVID-19 pandemic and the Statewide Emergency Stay-at-Home Order #N-33-20 issued on March 19, 2020, which required all non-essential workers in California to stay at home, were unforeseen and impossible to fully mitigate. In March 2020, Goodwill services were not considered by the state to be an essential activity and drivers' operations were severely limited for the remainder of 2020.

Although the pandemic-related mandatory work-stoppage was covered under the contract's force majeure provision, we continued to work on this project to meet the contractual requirements and project purpose. The contract required the submittal of quarterly reports to CARB, but due to the significant external challenges, the Air District started providing verbal and written reports at a significantly higher frequency, we increased the meeting frequency among the partners, including CARB, to twice monthly and eventually to twice weekly. At these meetings we discussed impacts to vehicle usage (operations) from the mandatory work stoppage and technical issues inherent to advanced technology projects, both of which subsequently impacted our (and Goodwill's) ability to meet the match requirement by December 2020.

While the agreement between CARB and the Air District did not include a specific mileage usage requirement, Goodwill's in-kind match that was specified in the agreement was derived based on drivers' salaries and the anticipated usage of the funded vehicles. This anticipated usage was calculated using historical mileage of Goodwill's diesel fleet totaling 273,000 miles for the 10 box trucks and 20,000 miles for the one debris hauler. This method of calculating anticipated usage is the standard accepted procedure used by CARB in many of its grant programs, such as Carl Moyer. However, due to the challenges of implementing new technologies as well as the COVID-19 work stoppage, Goodwill was unable to achieve the anticipated usage, and hence in-kind match, by the end of the term of the agreement with CARB, as shown in Figure 1. The "low usage" concern and related inability for Goodwill to meet its match requirement was brought up and discussed with CARB in the summer of 2019, as often as twice a week throughout 2020, provided in writing in the regular bi-weekly agendas, and meeting summaries, quarterly progress reports, and in the draft and final reports submitted to CARB.

The Air District's contract with CARB states that "any change in budget allocations, re-definition of deliverables, or extension of the project schedule must be requested in writing to [C]ARB Project Liaison and approved by [C]ARB, in its sole discretion." At the biweekly meeting held on August 18, 2020, CARB stated that while the matching funds were part of the original evaluation of the project, they were open to making adjustments to account for reductions in the operation.

On several occasions we discussed with our CARB liaison the possibility of extending the term and were informed that an extension beyond 2020 required legislative action and given the global pandemic, this was not a priority and ultimately deemed unnecessary. Instead, the Air District and CARB agreed on an alternate approach, where the required match would be met by December 2022, within the time frame of the Air District's contract with BYD and Goodwill. This alternative approach was documented in the fourth and final disbursement request, and CARB responded to the request in writing, stating that the information provided by the Air District showed the funds spent, and to be spent for match "are either correct or close enough" and that it was "not changing anything nor asking for any revisions." (See Final Disbursement Request at page 17; CARB email from M. Baker to L. Hui dated December 21, 2020).

The Air District also documented this alternative approach in the final report, which was accepted by CARB in writing. In response, CARB commended the Air District on its successful project: the Air District "created a comprehensive and well-written final project report," and "[i]t was a pleasure to work with [the Air District] on this successful project." (See CARB email from M. Baker to L. Hui dated February 8, 2021).

Our understanding was thus that CARB had given written approval for this alternate approach, where the match would be met within the term of the Air District's agreement with Goodwill, based on our extensive verbal and written communications; acceptance of the fourth disbursement request and the final report, and the fact that CARB made a full final payment when it closed out the grant. Based on this understanding and agreement, we continued to monitor the project and Goodwill continued to operate and report for an additional two years, incurring significant and unforeseen costs as shown in Figure 1 and in Table 1. Goodwill's continued operation resulted in higher usage than what was anticipated, and as a result contributed more in-kind match than what was required by the agreement with CARB.

FIGURE 1. CUMULATIVE MILES OF THE 11 FUNDED ELECTRIC TRUCKS

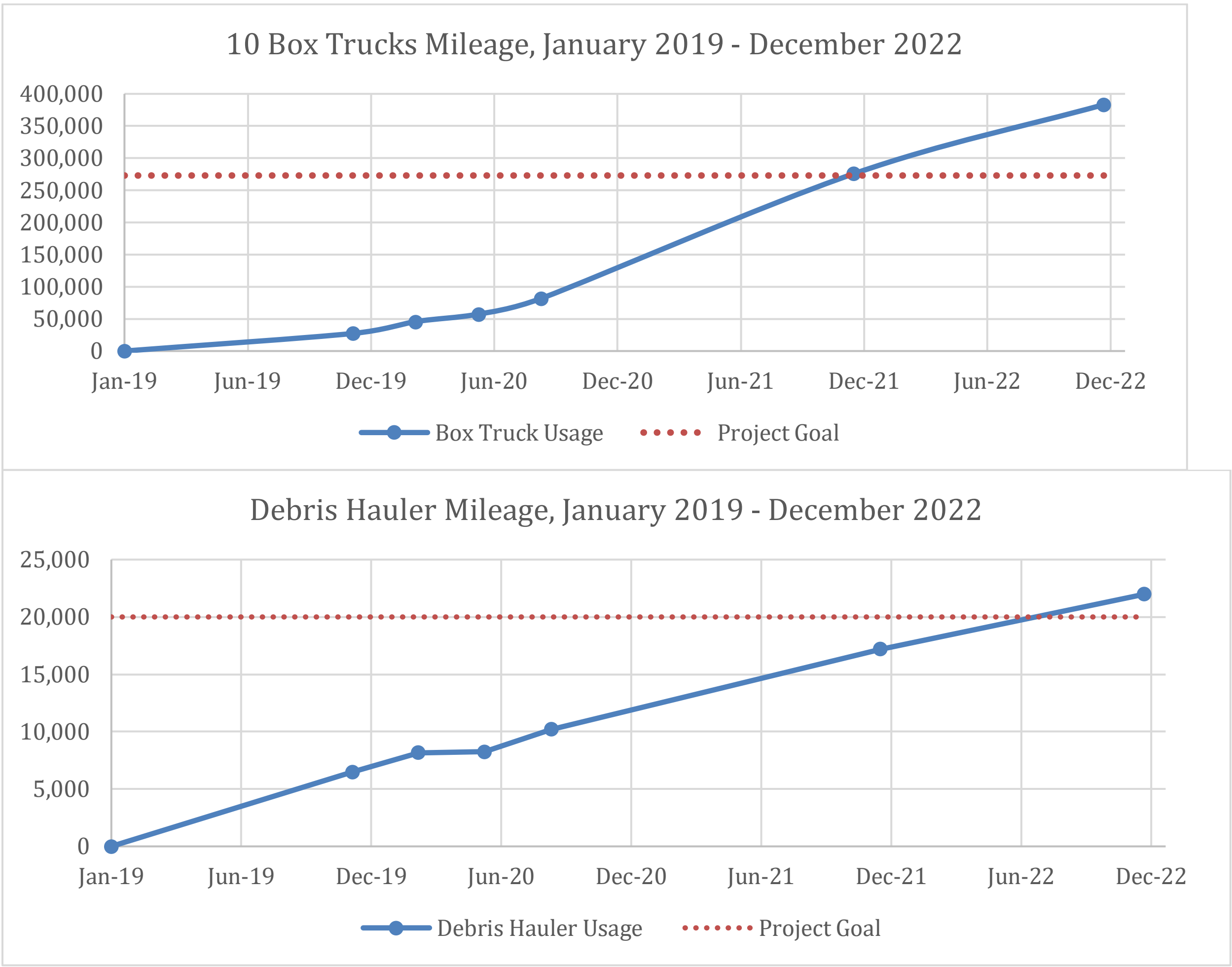

TABLE 1. SUMMARY OF ACTUAL CASH AND IN-KIND MATCH (2018-2022) VS. MATCH REQUIRED

	[A] Required by Contract	**[B] Total Match Incurred by December 2020**	**[C] Total Match Incurred by December 2022***	**[C]-[A] Difference (Additional Match)***
Air District Cash Match	$151,430	$157,892.25	$305,638.45	**$154,208.45**
Goodwill In-Kind Match	$358,468	$165,841.63	$451,637.07	**$93,169.07**
Goodwill Cash Match	$1,187,464	$844,144.35	$1,124,649.75	**($62,814.25)**
BYD Cash Match	$0	$8,177.09	$8,177.09	**$8,177.09**
BYD In-Kind Match	$0	$122,934.60	122,934.60	**122,934.60**
Total	**$1,697,362**	**$1,298,989.91**	**$2,013,036.95**	**$315,674.95**

*The total match amount shown is conservative and lower than the actual amount expended, as not all expenditures were tracked and attributed to this project. Therefore, the actual amount of match contributed is higher than what's reported in Table 1.

- As to **Recommendation A:** We firmly agree that collaboration, including robust communication, is crucial for successfully achieving deliverables and outcomes, and we increased the meeting and reporting frequency to as often as twice weekly, and more often as needed, to ensure there was robust communication among the partners, including CARB.

- We also provided a complete record in bi-weekly meetings verbally and through monthly written reports, as required by the grant agreement. Without this communication and the support of our liaison, we likely would have stopped working on the project soon after March 20, 2020, given the unprecedented and unmitigable impact of the Statewide Emergency Order. Instead, we were encouraged to continue work, including for another two years, thus exceeding the match requirements of the agreement, in accordance with our understanding of CARB's expectations.

- As to **Recommendation B:** We agree that clear written procedures and following terms are critical to ensure requirements and deliverables are achieved within specified timelines as per contractual requirements. Although we were told the contract would not be amended, we believed we had the necessary approval, including in writing, to continue the work needed to meet the match requirement after December 2020.

While our agency maintains emergency procedures for anticipated service disruptions, such as fires and earthquakes, we did not anticipate the prolonged emergency situation caused by the Covid-19 pandemic and the severe and long-lasting restrictions imposed by California and local health agencies. While we and our partners were able to quickly develop and implement procedures to resume remote administrative work, we could not swiftly mitigate the impact on operational services. As a lesson learned, we will develop a process to flag when a Force Majeure clause should be invoked for future projects.

Sincerely,

"Original signed by"

Philip M. Fine, Ph.D.
Executive Officer/Air Pollution Control Officer

Evaluation of Response

The District's response to the draft report has been reviewed and incorporated into the final report. In evaluating the District's response, we provide the following comments:

Finding 1: Unallowable Method Used to Recover Employee Paid Time Off

The District disagrees with Finding 1, as it contends there is a lack of clarity on the criteria cited. The District also contends that its accounting of accrued paid time off (PTO) is reported in its annual financial statements, which are audited for compliance with Generally Accepted Accounting Principles. Further, the District asserts that its allocation of PTO through its Dayforce payroll system results in an equitable distribution of costs based on actual work performed.

Our audit scope, conclusions, and findings are limited to the expenditures, revenues, and resulting balances of the individual incentive programs and not the broader financial statements and accounting policies of the District. Per program guidelines, the District is permitted to recover actual employee hourly costs for incentive program implementation and monitoring activities. Governmental Accounting Standards Board Statement 16 states a liability for compensated absences should be accrued as employees earn the rights to the benefit. The District notes that governmental funds only need to report the current portion of the liability. However, the initial accrual of PTO is still required as it is earned. Further, the allocation of PTO by the Dayforce system as described by the District does not address the underlying issue of the accrual timing for these hours. The District could not demonstrate that charging PTO as it is used resulted in accurate and equitable allocation of PTO costs to each program and grant period. The District did not provide additional evidence to support that PTO charged to these programs relates to actual employee hourly costs for implementation and monitoring activities. Therefore, the finding and recommendations remain unchanged.

Finding 2: Grant Match Funding Requirement Was Not Met Within the Grant Period

The District disagrees that the LCT/AQIP match funding requirement was not met as it contends that there was approval from CARB for match expenditures incurred after the grant term to meet the requirement. While we acknowledge that CARB and the District communicated throughout the grant period regarding the match funding requirement not being met, the documentation provided was not sufficient to substantiate that CARB had approved an extension of the match funding period. As no additional evidence was provided with the District's response, the finding and recommendation will remain unchanged.