

July 14, 2025

Steven S. Cliff, Ph.D.
Executive Officer
California Air Resources Board
1001 I Street
Sacramento, CA 95814

Dear Dr. Cliff,

The Air District is pleased to accept the California Air Resources Board's (CARB) 2025 Incentive Program Review -- Final Report. This Program Review was conducted by a third-party auditor, Crowe, LLP (Crowe), on behalf of CARB, and spanned seven years (FY 2015-16 through 2021-22) and eight incentive programs, totaling over \$334 million in grant funds and thousands of emission reduction projects. CARB conducts program reviews to ensure grant funds are awarded and expended in accordance with program guidelines and legal requirements.

Crowe's Final Report highlights extensive commendable efforts and recommendations, with no findings. The report confirms that the Air District's incentive program implementation was fully consistent with applicable statutes and guidelines, including determinations of project eligibility and compliance with reporting requirements. Concurrently, the California Department of Finance (DOF) conducted a fiscal review of the same programs, scope, and timeframes. That report, issued in February 2025, includes the Air District's response.

Over the past 28 years, the Air District's implementation of State-sponsored incentive programs has significantly reduced emissions from mobile sources of air pollution in the Bay Area, greatly enhancing air quality and public health. These comprehensive reviews highlight the success of the Air District's programs in achieving high standards and fulfilling our mission to protect public health, address historical and current environmental inequities, and mitigate climate change and its impacts.

In line with our District's commitment to continuous improvement, we are continuing to review and implement relevant recommendations, such as creating a unified modern data management system to improve the efficiency of tracking and reporting key metrics as they evolve. Our aim is to enhance transparency and expedite the reporting of results for our communities and region.

We appreciate the professional approach of Crowe and CARB staff during the program review process and the ongoing support provided by the CARB liaison team. We remain committed to delivering high-quality incentive programs and look forward to our continued partnership with CARB to proactively address the evolving challenges and demands of these voluntary, but essential, emissions and exposure reduction programs.

Sincerely,



Philip M. Fine, Ph.D.
Executive Officer/APCO

Cc: Marites Sicat, Branch Chief
Incentives and Technology Advancement Branch, Mobile Source Division

Tung T. Le, Executive Director
California Air Pollution Control Officers Association

Marilyn StandingHorse, Certified Public Accountant
Office of State Audits and Evaluations, California Department of Finance

Aaron Coen, Contract Manager
Crowe LLP

Executive Summary Cover Memo
New State Grant Accounting Methodology
August 13, 2025

TO: Philip M. Fine, Executive Officer/APCO 

VIA: Arsenio Mataka, Deputy Executive Officer of Equity & Community Programs 
Hyacinth Hinojosa, Deputy Executive Officer of Finance & Admin 

FROM: Stephanie Osaze, Director of Finance 
Anthony Fournier, Director of Technology Implementation Office 
Karen Schkolnick, Director of Administrative Services 

SUBJECT: Air District's Change in Methodology for State Grants to address Department of Finance Final Audit on Finding #1 Recommendations

RECOMMENDED ACTION

Staff recommend submitting a revised grant accounting methodology for State of California grants to the California Air Resources Board (CARB) for approval, using a two-phased implementation approach:

- **Phase One (FYE 2025):** Implement a revised methodology for calculating Paid Time Off (PTO) and apply a minor modification to the indirect cost calculation for State grants.
- **Phase Two (Beginning FY 2026):** Transition to using the federally approved indirect cost rate in place of the Air District's internally calculated rate.

BACKGROUND

The California Department of Finance (DOF), Office of State Audits and Evaluations, conducted a fiscal compliance audit of the Air District's implementation of CARB's air pollution incentives programs for fiscal years 2016 through 2022. The audit resulted in two findings:

- **Finding #1:** Unallowable method used to recover employee PTO.
- **Finding #2:** Grant match funding requirements were not met within the grant period.

For **Finding #1**, DOF issued two recommendations:

- **Recommendation A:** Collaborate with CARB to revise the fringe benefit allocation to include PTO when accrued, ensuring appropriate benefit charges to respective incentive programs and fiscal years, and addressing \$1,135,812 in questioned costs.
- **Recommendation B:** Develop and implement procedures to ensure PTO-related labor costs charged to incentive program grants comply with grant requirements and Generally Accepted Accounting Principles (GAAP).

DISCUSSION

Implementation of Recommendation A

The Air District’s Finance and Grants teams will meet with CARB to address the \$1.1 million in questioned costs. Staff propose revising the PTO allocation methodology in alignment with practices used by other large air districts, as recommended by DOF.

Consultations with fiscal staff from the South Coast Air Quality Management District (SCAQMD) and San Joaquin Valley Air Pollution Control District (SJVAPCD) air districts revealed that both agencies allocate regular PTO using an indirect cost method. The SJVAPCD approach is particularly favorable, having recently passed a DOF audit with no findings. Based on the review of the SJVAPCD methodology, staff recommend the following changes:

Phase One: Revised PTO Allocation Methodology (Effective FYE 2025)

- PTO will be allocated quarterly or semi-annually based on actual hours worked on specific grants, rather than bi-weekly payroll.
- Only regular PTO hours (e.g., holidays, vacation, sick leave, comp time taken) will be charged to grants.
- PTO payouts due to terminations, resignations, or annual cash-outs will no longer be charged to grants and will instead be covered by the General Fund.
- The financial impact to the General Fund of this change is expected to be minimal.

This approach removes regular PTO from being directly charged as part of bi-weekly salary costs. Instead, total regular PTO costs will be allocated to each grant based on total hours worked by grant staff. PTO will be based on a % of total hours of all grant staff and their total time worked on specific grants over a longer timeframe (ex. Semi-annually or annually) . Cash-out PTO costs will be excluded from grant charges and absorbed by the General Fund.

This change slightly affects the indirect cost rate calculation. **Table 1 and Table 2** illustrate the minimal impact by comparing the original and revised indirect cost rates.

Table 1: Indirect Cost Rate Comparison (original rate vs. revised rate)

Fiscal Year	Original Indirect Rate	Indirect Rate with revision/study	Difference in Rate
			D=B-C
15/16	46.6055	No Indirect Assessed	
16/17	47.4267	No Indirect Assessed	
17/18	48.6598	48.6599	-0.0071%
18/19	51.8326	51.8327	-0.0059%
19/20	51.3607	51.3607	-0.0045%
20/21	51.6878	51.6879	-0.0120%
21/22	51.5900	51.5901	-0.0122%

Table 2: Cost Impact (original indirect rate vs. revised indirect rate)

If the revised indirect cost rate was applied to the grant periods noted below, the Air District allowable indirect cost would decrease by \$11,204.80.

Fiscal Year	Allowable Indirect Personnel/Admin Costs at District Revised Rate	Allowable Indirect Personnel/Admin Costs at Original District Rate	Allowable Indirect cost Rate Impact
15/16			
16/17			
17/18	248,117.49	249,925.39	(1,807.90)
18/19	827,704.24	829,302.04	(1,597.80)
19/20	1,100,651.40	1,101,861.71	(1,210.31)
20/21	1,442,892.05	1,446,163.54	(3,271.49)
21/22	1,933,872.11	1,937,189.40	(3,317.29)
Total	5,553,237.29	5,564,442.08	(11,204.80)

Despite multiple attempts, the Air District was unable to meet with DOF to clarify how the \$1.1 million in questioned costs were calculated. However, because the Air District did not fully charge all allowable indirect costs to the grants, the uncharged portion effectively offsets the questioned amount. **Table 3** shows the difference between total allowable grant cost using the allowable indirect costs under the new methodology and the actual indirect costs charged using the original indirect cost rate, demonstrating a total of \$3.3M allowable indirect costs were not recovered by the Air District. This amount would offset the \$1.1M questioned costs noted by DOF.

Table 3: Allowable Indirect Cost vs Actual Indirect Cost Charged to Grants

Fiscal Year	Allowable Indirect Personnel/Admin Costs at District Revised Rate	Actual Indirect Charged to Grants	Indirect not recovered by District using the revised rate
15/16		-	-
16/17		-	-
17/18	248,117.49	249,925.39	(1,807.90)
18/19	827,704.24	752,011.88	75,692.36
19/20	1,100,651.40	834,053.52	266,597.88
20/21	1,442,892.05	203,897.92	1,238,994.13
21/22	1,933,872.11	224,535.99	1,709,336.12
Total	5,553,237.29	2,264,424.70	3,288,812.59

Phase Two: Adoption of EPA-Approved Indirect Cost Rate (Effective FY 2026)

Transitioning to the Federally approved indirect cost rate, as used by SJVAPCD, provides a transparent and validated methodology. This rate, approved by the U.S. Environmental Protection Agency (EPA), is fixed annually based on prior-year data. It simplifies grant administration, reduces audit risk, and allows for greater recovery of indirect costs—helping offset the exclusion of PTO cash-outs from grant charges. The Phase 2 proposal is consistent with other Air District grants (including: CMAQ, CEC REACH, and the FHWA/CFI) that already use the Federally approved indirect cost rate is already used for cost allocations.

Upon CARB approval, the revised methodology will be formally incorporated into the Air District’s financial procedures.

Implementation of Recommendation B

To ensure compliance with accounting standards, the Air District consulted its external auditor, an audit advisory firm, and the Governmental Accounting Standards Board (GASB). All parties confirmed that the current Air District practice of recognizing PTO expense when taken (rather than when accrued) aligns with GAAP. Accordingly, the Air District will continue its current practice to remain in compliance with GAAP.

BUDGET CONSIDERATION / FINANCIAL IMPACT

PTO cash-out hours will no longer be charged to grants. This amount is typically minimal. The average annual cash-out amount is approximately \$75,000.