



Office of the City Auditor
Review of HRT Cost Allocation Agreement

Report Date: June 30, 2010



Office of the City Auditor

"Promoting Accountability and Integrity in City Operations"

www.vbgov.com/cityauditor

Lyndon Remias, CPA, CIA

Chris Ford, CPA

City Auditor

Deputy City Auditor

Office of the City Auditor

2401 Courthouse Drive, Room 344

Virginia Beach, VA 23456

Telephone: 757.385.5870

Fax: 757.385.5875

Fraud, Waste, and Abuse Hotline 757.468.3330



Office of the City Auditor Transmittal Letter



Date: June 30, 2010

To: James K. Spore, City Manager

Subject: Review of HRT Cost Allocation Agreement

I am pleased to present the report of our review of the Cost Allocation Agreement between the City and the Transportation District Commission of Hampton Roads (HRT). The results of this review will be provided to City Council through the City's Audit Committee.

This agreed-upon procedures engagement was conducted in accordance with Government Auditing Standards. Government Auditing Standards incorporate financial and attestation standards established by the American Institute of Certified Public Accountants. These standards also provide guidance for performing and reporting the results of agreed-upon procedures.

The Office of the City Auditor reports to City Council through the City's Audit Committee and is organizationally independent of all other City Departments. The procedures we agreed to perform and the associated results are enclosed. We completed the agreed-upon procedures on May 17, 2010.

This report is intended solely for the information and use of the Audit Committee, City Council, City Manager, and appropriate management including the Department of Planning. It is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.



Office of the City Auditor
Transmittal Letter

James K. Spore, City Manager
Review of HRT Cost Allocation Agreement
June 30, 2010
Page 2

We would like to commend HRT and the Department of Planning for the courtesy and cooperation extended to us during the review. If you have any questions about this report or any audit-related issue, I can be reached at 385-5872 or via email at lremias@vbgov.com.

Respectfully submitted,

Lyndon S. Remias, CPA, CIA
City Auditor

c: City Council Members
Audit Committee Members
Steve Herbert, Deputy City Manager, City Manager's Office
Jack Whitney, Director, Department of Planning



Transmittal Letter	i
Purpose, Scope and Objectives.....	1
Methodology and Standards	2
Background	3
Results	9
Management’s Response	9
Conclusion and Acknowledgements	9
Management’s Response	Attachement



Purpose

To verify HRT's compliance with the Cost Allocation Agreement whereby the City of Virginia Beach and the other six cities of Hampton Roads are allocated costs to provide public transportation for the region.

Scope and Objectives

The objectives of our review were:

1. To ensure that the City and HRT are in compliance with the Cost Allocation Agreement dated October 1, 1999 (renewable annually) in providing public transportation to the City of Virginia Beach.
2. To determine the reasons for the City of Virginia Beach's increased annual contribution requirement to HRT from 2006 to 2011.

We reviewed the City's fiscal year 2010 Transportation Service Plan (TSP) which determines the City's annual transit costs for compliance with HRT's Cost Allocation Agreement dated October 1, 1999 and renewable annually.

We reviewed HRT's audited financial statements from 2006 through 2009 (the most current year audited) and HRT's Transportation Service Plans from 2006 through 2011 to determine the amount and reasons for Virginia Beach's increased required contribution from 2006 to 2011.



Methodology

Inquiry and examination of documents and data were the methods used to review internal controls. To accomplish our objectives, we performed the following procedures:

- Reviewed and obtained an understanding of the *Cost Allocation Agreement* between the City (all seven Hampton Roads cities) whereby the City agrees to its share, as specified in the agreement, of costs to provide public transportation to the city of Virginia Beach.
- Met with appropriate City personnel in the Department of Planning and Management Services to obtain information concerning the HRT contract and related issues.
- Researched the HRT website for additional background information.
- Obtained, reviewed and analyzed the audited financial statements of HRT for 2006 through 2009 (most current) to determine the nature, makeup and causes for increased amount of costs passed through to the localities and Virginia Beach specifically.
- Obtained and reviewed the Transportation Services Plan (TSP) whereby the various cities' local contribution amount is determined for the fiscal years ended 2006 through 2011 and documented the increase in Virginia Beach's local contribution from 2006 through 2011.
- Documented the methodology used in the current 2010 TSP and verified it's compliance with the Cost Allocation Agreement.
- Interviewed appropriate HRT financial personnel to resolve issues/concerns.
- Verified that the quarterly payments made in 2010 for Virginia Beach's local contribution agree with the 2010 TSP amount and are properly recorded in InSITE account 002.17130.605633.

Note: *It should be noted that to achieve the stated objectives of 1) determining HRT's compliance with the Cost Allocation Agreement and 2) determining the reasons for Virginia Beach's increased contribution since 2006, one must take a two-fold perspective. First, one must consider the overall financial trends and expenses occurring at the HRT Commission level. This is where the operating expenses occur that make up the pool of expenses that are allocated and recovered via the TSPs of the various cities. To understand why Virginia Beach's local contribution has increased one must analyze both the audited financial statements of the Commission itself and the annual TSPs that allocate and recover those costs through the participating cities.*

Standards

Our audit was conducted in accordance with generally accepted government auditing standards. The Office of the City Auditor reports to City Council through the Audit Committee and is organizationally independent of all City Departments. This report will be distributed to the City's Audit Committee, City Council, City Manager, and appropriate management within the City. This report will also be made available to the public.



Office of the City Auditor Review of HRT Cost Allocation Agreement

Background

The Transportation District Commission of Hampton Roads was formed on June 29, 1999. The formation of the Commission resulted from the merging of the Peninsula Transportation District Commission (PTDC) and the Tidewater Transportation District Commission (TTDC) effective October 1, 1999. The Commission provides public transportation services and facilities within the cities of Hampton, Newport News, Chesapeake, Norfolk, Virginia Beach, Portsmouth, and Suffolk. Each participating locality is represented by their designated Commissioners who exercise oversight responsibility, while day-to-day operations of the Commission are performed by the professional management.

Each year, as part of the budgeting process, the Commission proposes a public *transportation service program* (TSP) for the entire Hampton Roads region. The TSP will contain a description of the specific service provided including the route names, and estimated hours to be provided. Then the service hours are multiplied by a decided rate to come to an estimated cost figure that covers operations. The TSP will then show the estimated revenue from passengers, federal and state sources that offset the costs and then the remaining cost amount required to be funded by the localities, in quarterly payments. This format is presented in the annual TSP in a consolidated presentation for the entire region and for each individual City. The required methodology for the allocations of the various costs and revenues are detailed in the *Cost Allocation Agreement* which each one of the participating cities signed at the origination of the Commission in 1999 and is renewable annually. After year end, a true up reconciliation to actual is performed.

City of Virginia Beach's Increased TSP Contributions

The City of Virginia Beach's annual contribution has nearly doubled in the five years from \$2,152,930 in 2006 to \$3,981,346 in 2011.

City of Virginia Beach TSP 2006 - 2011

<u>Year</u>	<u>Op Rate</u>	<u>Admin Rate</u>	<u>Service Hours</u>	<u>Service Cost</u>	<u>Va Beach Contribution</u>
2006	\$ 44.56	\$ 11.92	138,664	\$ 7,284,516.00	\$ 2,152,930.00
2007	\$ 50.78	\$ 13.05	137,759	\$ 8,051,503.00	\$ 2,593,604.00
2008	\$ 54.37	\$ 14.20	138,272	\$ 8,722,259.00	\$ 3,215,171.00
2009	\$ 61.12	\$ 13.72	139,339	\$10,005,870.00	\$ 3,573,293.00
2010	\$ 59.18	\$ 15.91	139,864	\$10,100,754.00	\$ 3,747,059.00
2011	\$ 54.02	\$ 15.83	152,269	\$10,637,018.00	\$ 3,981,346.00

***These amounts are from the adopted TSPs, which could be slightly adjusted through the year for route changes or true-ups.**

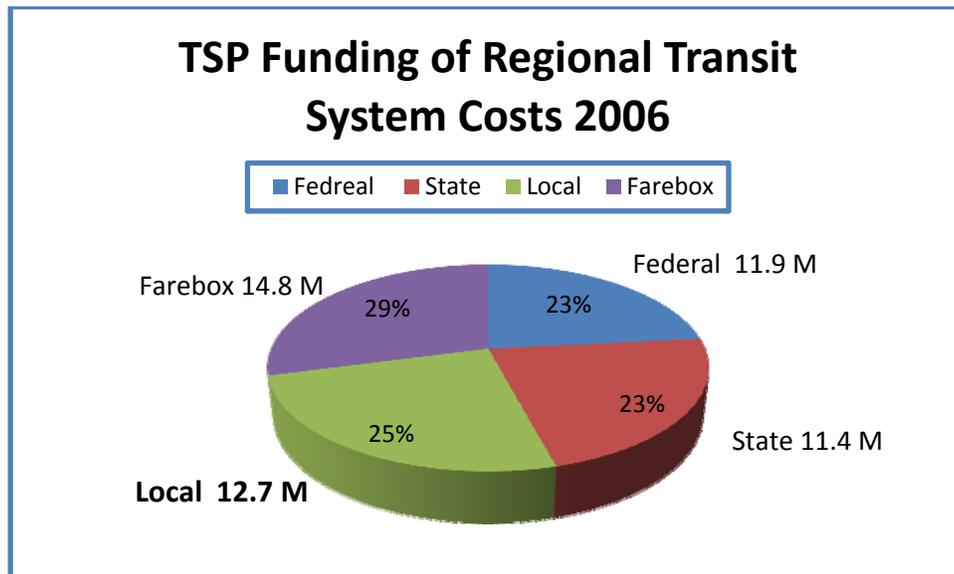


Figure 1 – Total Service Cost 50.8 Million

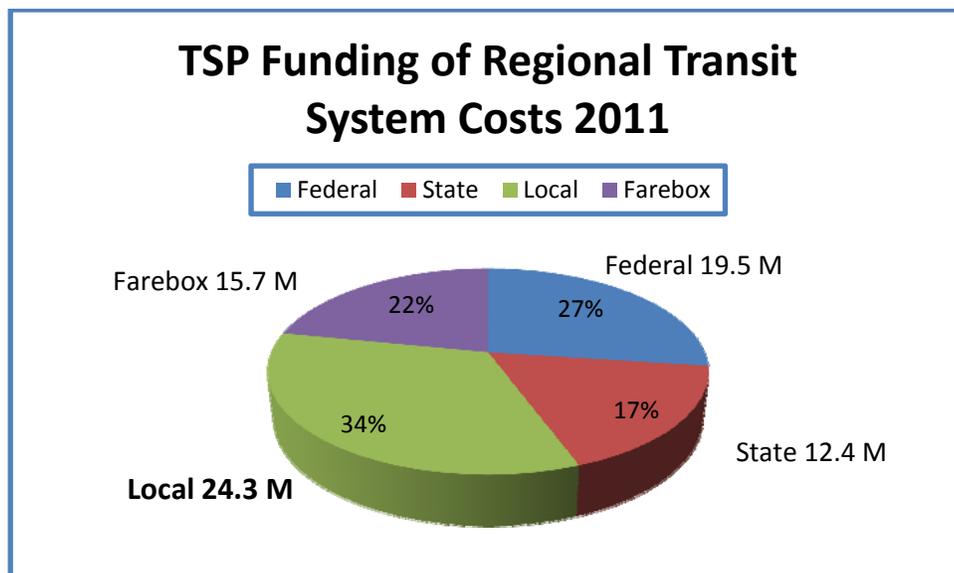


Figure 2 – Total Service Cost 71.9 Million

Note – These amounts are funding of total TSP service costs before Commission expense, Vanpool profit and Capital contribution.

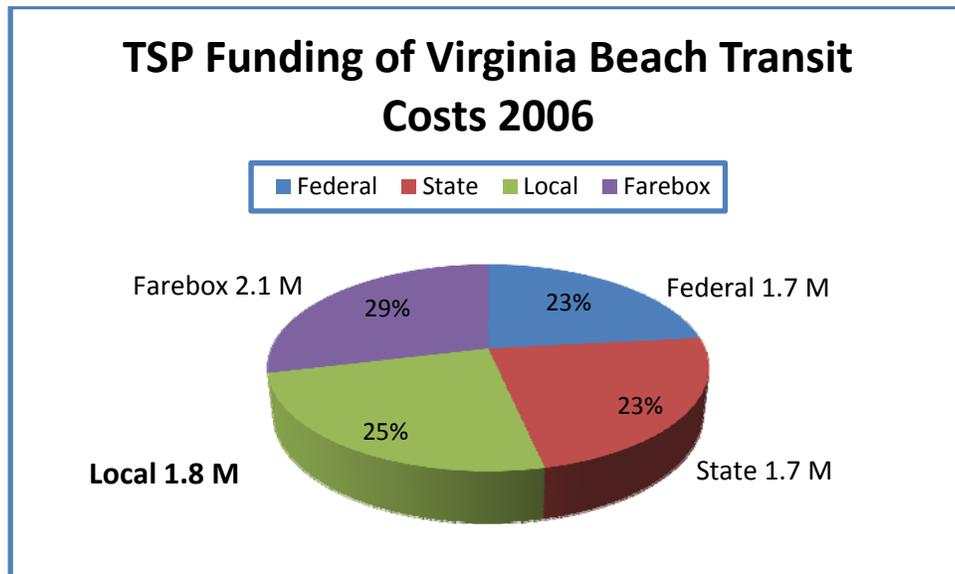


Figure 3 – Total City of Virginia Beach Service Cost 7.3 Million

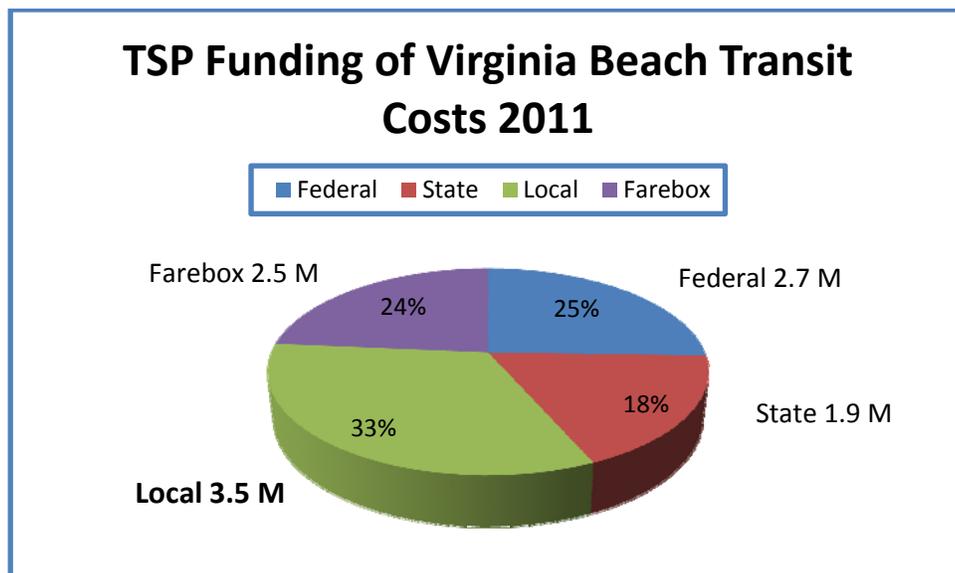


Figure 4 – Total City of Virginia Beach Service Cost 10.6 Million

Note – These amounts are funding of total TSP service costs before Commission expense, Vanpool profit and Capital contribution.

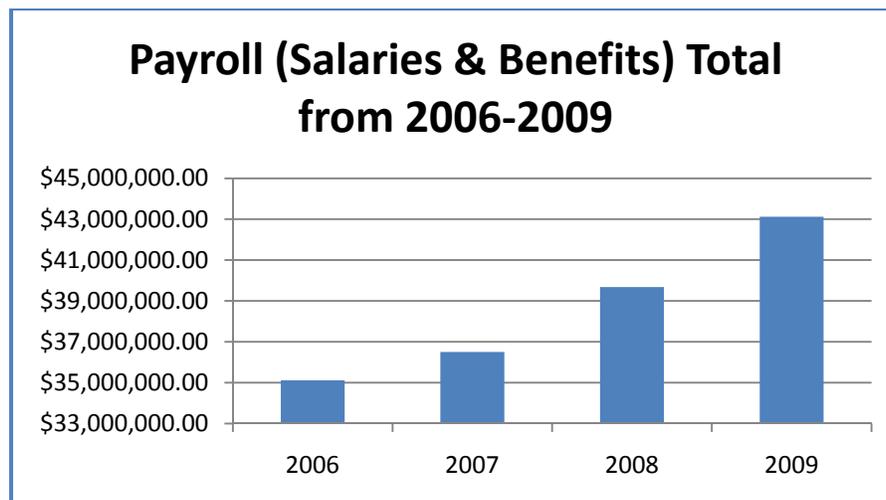


Causes for Virginia Beach's Increased Contribution

- The overall transit costs for the entire region, that HRT allocates and recoups through the seven cities' TSPs from passenger fees, state and federal funding and the remainder from the localities, grew from \$50,847,001 in 2006 to \$71,942,205 in 2011. This increase of \$21,095,204 or 41% over five years averages slightly over 8% a year.
- To understand what is driving the increased costs, it is necessary to analyze the audited financial statements of HRT. From the years 2006 to 2009 transit costs in the audited financial statements grew from \$59,011,422 in 2006 to \$74,226,618 in 2009 (most recent audited statements). Of this \$15,215,196 increase in just three years, \$8,006,871 of the increase (53%) was due to increases in salaries and benefits. Both the audited financial statements and the budget document make the same observation in 2009 and other years:

"Operating expenses of \$74.0 million (net of depreciation and amortization) were 11.95% or approximately \$7.9 million greater than fiscal year 2008, primarily due to increased personnel and fringe benefit costs."- MDA section of 2009 audited financial statements

"Increases in expenses have been primarily driven by salaries, wages and fringe benefits"- 2009 budget transmittal letter



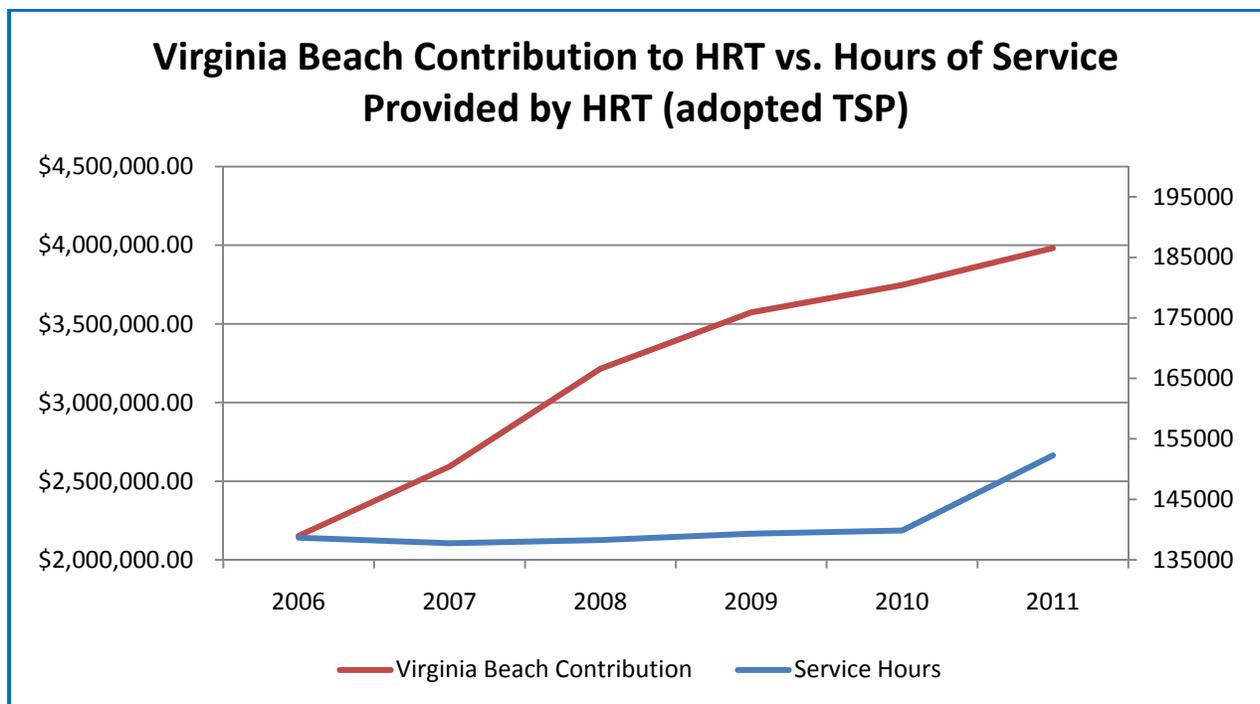
- During that same time regional transit costs were increasing at 8% in the TSP, passenger fees remained almost entirely flat while combined federal and state revenues increased \$8,567,595 from \$23,315,031 in 2006 to \$31,882,626 in the 2011 in the TSP. Thus, nearly all of the \$21,095,204 TSP cost increase since 2006 - except for the \$8,567,595 federal and state increase - was left to be covered by the localities. Indeed, the regions TSP local share during that time has increased from \$12,756,004 in 2006 to \$24,286,191 in 2011(TSP

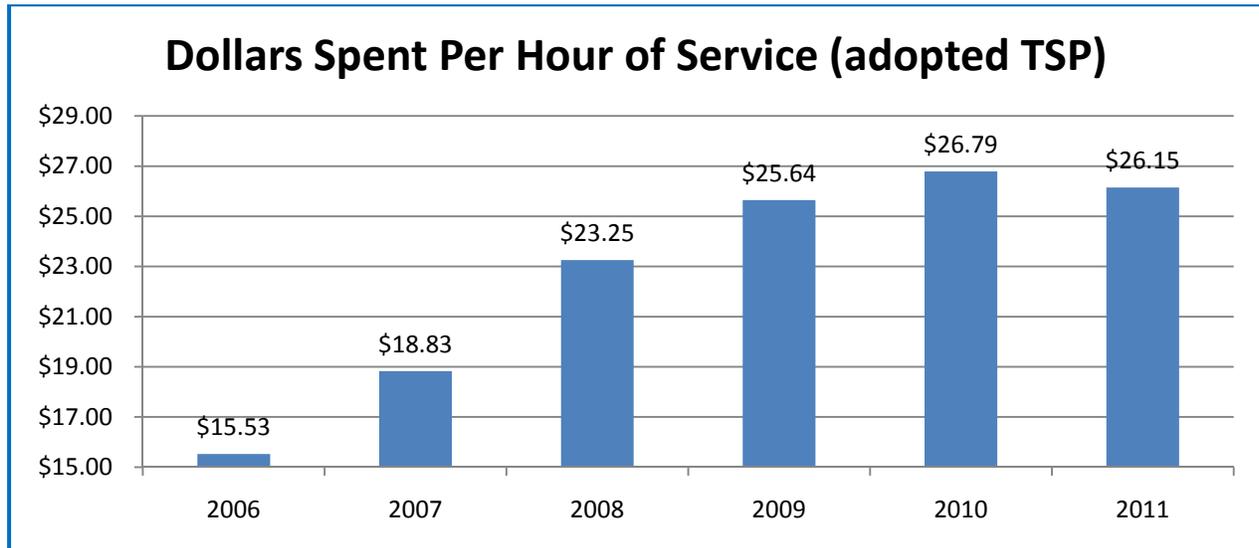


Office of the City Auditor Review of HRT Cost Allocation Agreement

service costs before Commission expense, Vanpool revenues and Capital contributions). Virginia Beach's local share increase is consistent with that doubling effect, having increased from \$1,798,309 in 2006 to \$3,483,414 in 2011. This equates to roughly a 20% annual increase in the localities' contribution – both Virginia Beach's and the other localities as a whole.

These increased transit costs have occurred despite the fact that total service hours in the TSP have increased minimally from 2006 to 2011. The TSP total service hours in 2006 were 907,398 while in 2010 they were 921,179 and 973,313 in 2011. The City of Virginia Beach mimics that overall pattern with total service hours of 138,664 in 2006, 139,864 in 2010 and 152,269 in 2011.





Compliance with Cost Allocation Agreement

Virginia Beach’s 2010 TSP Allocation (Summarized) is as follows:

Virginia Beach Cost	\$ 10,100,754
Less Federal Funding	\$ (2,757,177)
Less State Funding	\$ (1,747,776)
Less Farebox Revenue	\$ <u>(2,296,998)</u>
Va. Beach Local Share	\$ 3,298,803
Less Van Pool Profit	\$ (37,761)
Add Commission Exp	\$ 243,928
Add Capital Contribution	\$ 242,089
2010 Virginia Beach Cost	\$ 3,747,059

Quarterly Payments of \$936,765 in **002.17130.605633**



Results

We reviewed the 2010 City of Virginia Beach TSP (summarized above) and verified the significant line items to the allocation requirements in the Cost Allocation Agreement and found the TSP to comply with the agreement.

Recommendation

We recommend the appropriate Department of Planning personnel meet with the Office of the City Auditor to implement procedures to annually review the TSP to gain assurance that the transit costs allocated to the City of Virginia Beach are in compliance with the Cost Allocation Agreement.

Management's Response

See Attachment for Management's Response.

Conclusion

Based upon the results of our review, we believe the City of Virginia Beach's 2010 Transportation Services' Plan (TSP) to be in compliance with the Cost Allocation Agreement signed by each of the seven cities. We believe the increase in the City's required local contribution since 2006 to be the result of increased operating expenses at the commission level, most notably salary and fringe benefits increases, and not the result of noncompliance with the Cost Allocation Agreement.

Acknowledgements

We would like to thank HRT, the Department of Planning and City staff for their responsiveness to our requests during the review and their receptiveness to questions and comments. We thank all involved in the process for their help and offer our assistance should future concerns regarding this or other audit issues arise.



City of Virginia Beach

VBgov.com

DEPARTMENT OF PLANNING
(757) 385-4621
FAX (757) 385-5667

MUNICIPAL CENTER
BUILDING 2
2405 COURTHOUSE DRIVE RM 115
VIRGINIA BEACH, VA 23456-9040

INTEROFFICE MEMORANDUM

DATE: June 25, 2010

TO: Lyndon Remias, City Auditor

FROM: Mark Schnauffer, Transportation Planning Coordinator

SUBJECT: HRT Audit Recommendation

Lyndon:

Thank you for updating our team on the results of the recently conducted HRT audit. We agree with the findings of the report as well as the recommendation for personnel from our department to meet with you and your staff to develop annual review procedures ensuring that transit costs allocated to the City of Virginia Beach from HRT are in compliance with the Cost Allocation Agreement.

Thank You