



Florida Department of TRANSPORTATION

Office of Inspector General
Kristofer B. Sullivan, Inspector General

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Kristofer B. Sullivan
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Audit Report No. 23I-002
Florida East Coast Railway 2021 Indirect Rates

January 23, 2023

What We Did

The Florida Department of Transportation's (Department) Office of Inspector General reviewed the Florida East Coast Railway's (FEC) labor additive, material handling and supplies, and equipment (indirect) rates for the calendar year 2021, to determine whether they are reasonable, based on allocable and allowable costs, and supported by transparent and understandable records.

What We Found

We determined that the indirect rates submitted by FEC for use in billing railroad-highway projects for all Groups, 2, 3, and 4, are reasonable, allowable, and adequately supported, and supporting records and procedures are transparent and readily understandable. **We also determined** FEC's accounting procedures, including supporting documentation, continue to meet the visibility rule set forth in Title 48, Part 9904, Code of Federal Regulations-Cost Accounting Standards, Section 405-50-Techniques for application, which requires adequate cost identification to deem expense allowability.

What We Recommend

We recommend the Department's Freight and Rail Office review and approve FEC's 2021 indirect cost rates for use in billing costs for railroad-highway projects and communicate this decision to the Federal Highway Administration.

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BACKGROUND AND INTRODUCTION

The Florida East Coast Railway (FEC) is a Class II regional railroad that owns the 351-mile mainline track in Florida from Jacksonville to Miami. It is the exclusive rail provider for Port Miami, Port Everglades, and Port of Palm Beach. FEC is a wholly owned subsidiary of Grupo México Transportes (GMXT), a Class I railroad in Mexico.

FEC connects to the national railway system in Jacksonville, allowing it to provide rail service in and out of Georgia, Tennessee, South Carolina, North Carolina, and Florida's east coast. Based in Jacksonville, FL, FEC provides end-to-end intermodal and carload solutions to customers.

Criteria

The following regulations authorize the Florida Department of Transportation (Department) to pay labor surcharge and indirect cost rates, define allowable costs for purposes of inclusion in the rates, and set minimum standards for calculation methods and supporting records:

- Title 23, Part 140, Code of Federal Regulations (C.F.R.), Subpart I- Reimbursement for Railroad Work, Subsection 908(e)-Materials and Supplies;
- 23 C.F.R.140.910(a)-Equipment;
- 23 C.F.R.140.906(b)(2)(ii)-Labor Costs.
- 48 C.F.R. 9904.405-Cost Accounting Standards, Accounting for Unallowable Costs.

Rate Utilization

FEC uses its indirect rates to bill for certain overhead costs related to rail/highway safety projects. Indirect rates are approved by the Department's Freight and Rail Office (FRO) and the Federal Highway Administration (FHWA), and applied as follows:

- For its hourly in-house labor charges, to recover costs associated with workman's compensation, public liability, and property damage charged at the flat fee of 8 percent of direct labor costs instead of actual costs, per 23 C.F.R. 140.906(b)(2)(ii).
- Employee benefits and the employer-paid portion of payroll taxes. These components make up the balance of the total rate, which ranges between 56 and 82 percent, during the years 2017 to 2021.
- As an additional material handling charge of 5 percent of the amounts billed for material and supplies issued from company stores and material yards instead of actual costs, per 23 C.F.R. 140.908(e).
- As the industry rate for equipment costs is based on the "Blue Book for Railroad Equipment," per 23 C.F.R. 140.910(a).
- FEC's accounting procedures, including supporting documentation, continue to meet the visibility rule set forth in Title 48, Part 9904, Code of Federal

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Regulations-Cost Accounting Standards, Section 405-50-Techniques for application, which requires adequate cost identification to deem expense allowability.

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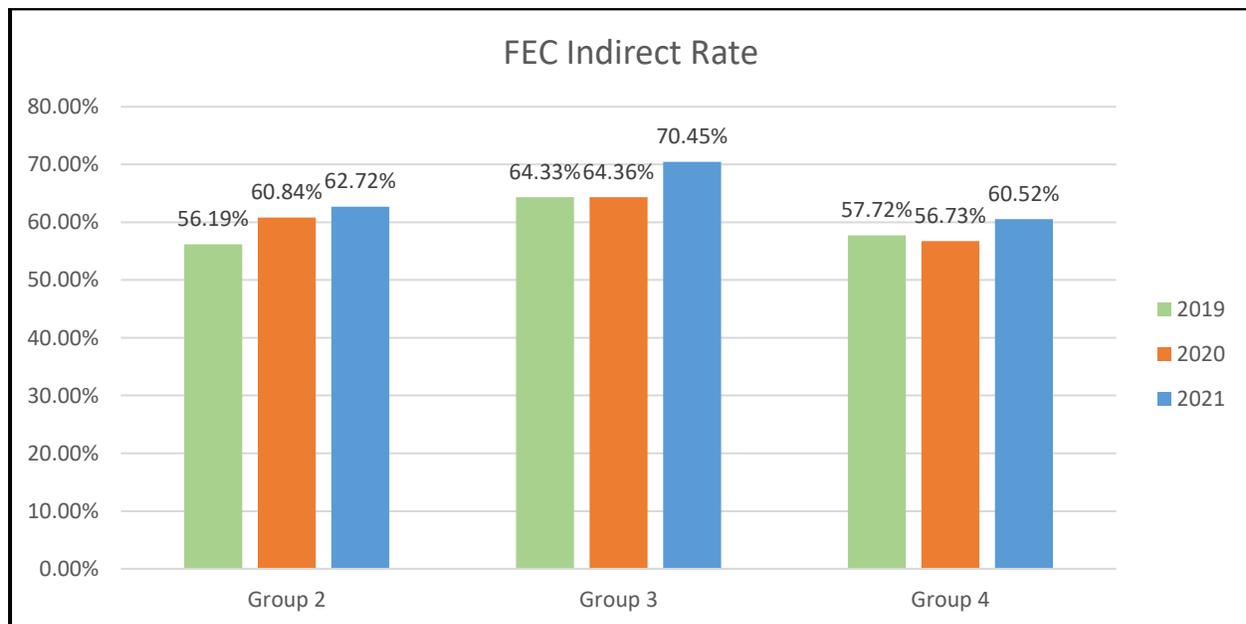
RESULTS OF REVIEW

To assess the reasonableness, allocability, allowability, transparency, and understandability of the indirect rates submission packet, we evaluated the costs associated with the rates (Appendix B) and compared the current to the prior year's submission (Appendix C).

We determined that the indirect rates submitted by FEC for use in billing railroad-highway projects for Groups, 2, 3, and 4, are reasonable, allowable, and adequately supported, and supporting records and procedures are transparent and readily understandable based on the supporting documentation provided by FEC and the applicable criteria. **We also determined** FEC's accounting procedures, including supporting documentation, continue to meet the visibility rule set forth in Title 48, Part 9904, Code of Federal Regulations-Cost Accounting Standards, Section 405-50-Techniques for application, which requires adequate cost identification to deem expense allowability.

The indirect rates for 2021 are slightly higher for Groups 2, 3, and 4 than for 2020's rates. See **Figure 1**. However, FEC provided an explanation as detailed within this section of the report.

Figure 1: FEC Historical Rate Trend¹



Source: The OIG created this table from data submitted by FEC.

¹ FEC completed a review and found that there was an error in the 2020 calculation of the holiday and vacation pay rate for group 4. Since the rate was understated, FEC decided not to submit a revision of their 2020 submitted rates.

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As shown in **Figure 2**, all groups experienced an increase in holiday and vacation, and payroll taxes costs and a decrease in bonus costs.

We inquired about the increases and decreases with FEC, and their explanations were as below:

- FEC discovered an error in the 2020 filing of holidays and vacations for Group 4 that happened in 2018, 2019, and 2020. The 2020 holiday and vacation rate should have been 8.30% instead of 4.09%. Hence the change should have been 1.1% instead of 5.3%;
 - Since the rate was understated, FEC has decided not to submit a revision of their 2020 submitted rates.
- The increase in payroll taxes was attributed to an increase in the railroad unemployment tax rate. Group 3 had the largest increase in the labor base, causing this increase in payroll taxes.
- FEC did not offer bonuses in 2021, and they are not aware of if/when bonuses will be offered moving forward.

The OIG has included the adjustments from FEC because they seem reasonable and allowable; however, we have not conducted an audit of the adjusted rates. The sum of the rates in this chart may have a slight difference from the total due to rounding in the content.

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Figure 2: 2020-2021 Rate Comparison

Group 2					
Labor Surcharge Classification	Approved 2020 Rate	Adjusted 2020 Rate	Submitted 2021 Rate	Rate Change 2020 Approved Rate - 2021 Submitted Rate	Rate Change 2020 Adjusted Rate - 2021 Submitted Rate
Sick Pay	0.08%	0.08%	0.08%	0.0%	0.0%
Holiday & Vacation Pay	8.09%	8.09%	9.15%	1.1%	1.1%
Other Paid Absences	1.97%	1.97%	2.20%	0.2%	0.2%
Bonus	0.35%	0.35%	0.00%	-0.3%	-0.3%
Payroll Taxes	22.49%	22.49%	24.12%	1.6%	1.6%
Health and Welfare	19.85%	19.85%	19.16%	-0.7%	-0.7%
W/C, Public Liability & Property Damage Insurance	8.00%	8.00%	8.00%	0.0%	0.0%
Subtotal	60.84%	60.84%	62.72%	1.9%	1.9%

Group 3					
Labor Surcharge Classification	Approved 2020 Rate	Adjusted 2020 Rate	Submitted 2021 Rate	Rate Change 2020 Approved Rate - 2021 Submitted Rate	Rate Change 2020 Adjusted Rate - 2021 Submitted Rate
Sick Pay	0.15%	0.15%	0.13%	0.0%	0.0%
Holiday & Vacation Pay	7.68%	7.68%	8.99%	1.3%	1.3%
Other Paid Absences	7.85%	7.85%	9.54%	1.7%	1.7%
Bonus	0.32%	0.32%	0.00%	-0.3%	-0.3%
Payroll Taxes	23.61%	23.61%	25.68%	2.1%	2.1%
Health and Welfare	16.75%	16.75%	18.11%	1.4%	1.4%
W/C, Public Liability & Property Damage Insurance	8.00%	8.00%	8.00%	0.0%	0.0%
Subtotal	64.36%	64.36%	70.45%	6.09%	6.09%

Group 4					
Labor Surcharge Classification	Approved 2020 Rate	Adjusted 2020 Rate	Submitted 2021 Rate	Rate Change 2020 Approved Rate - 2021 Submitted Rate	Rate Change 2020 Adjusted Rate - 2021 Submitted Rate
Sick Pay	0.94%	0.94%	0.90%	0.0%	0.0%
Holiday & Vacation Pay	4.09%	8.30%	9.41%	5.3%	1.1%
Other Paid Absences	0.84%	0.84%	0.81%	0.0%	0.0%
Bonus	4.44%	4.44%	0.00%	-4.4%	-4.4%
Payroll Taxes	22.46%	22.46%	24.05%	1.6%	1.6%
Health and Welfare	15.97%	15.97%	17.35%	1.4%	1.4%
W/C, Public Liability & Property Damage Insurance	8.00%	8.00%	8.00%	0.0%	0.0%
Subtotal	56.73%	60.94%	60.52%	3.8%	-0.4%

Source: The OIG created these tables from data submitted by FECR.

We recommend that the Department's FRO review and approve FEC's 2021 indirect cost rates for use in billing costs for railroad-highway projects and communicate this decision to the FHWA.

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APPENDIX A – Purpose, Scope, and Methodology

The **purpose** of this engagement was to determine whether FEC's:

- The calendar year 2021 indirect rates are reasonable, allocable, and based on allowable costs; and
- supported by transparent and understandable records.

The **scope** of this audit consisted of the proposed 2021 indirect rates submitted by FEC and associated records and supporting documentation.

The **methodology** included the following:

- reviewing relevant regulations:
 - 23 C.F.R. 140.908(e)-Materials and Supplies
 - 23 C.F.R. 140.910(a)-Equipment
 - 23 C.F.R. 140.906(b)(2)(ii)-Labor Costs
- reviewing FEC's rate preparation procedures;
- identifying and reviewing account classification differences between 2020 and 2021;
- re-performing rate calculations;
- performing comparative analysis on 2020 and 2021 rate data; and
- interviewing key management staff and reviewing selected work papers prepared internally by FEC.

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APPENDIX B – 2021 Labor Additive Surcharge Rates²

Group II - Maintenance of Roadway, Equipment, and Signal Employees

Sick Pay	0.08%
Holiday & Vacation Pay	9.15%
Other Paid Absences	2.20%
Bonus	0.00%
Payroll Taxes	24.12%
Health and Welfare	19.16%
Workman's Compensation (W/C), Public Liability and Property Damage Insurance	8.00%
Total	<u><u>62.72%</u></u>

Group III - Transportation Employees

Sick Pay	0.13%
Holiday & Vacation Pay	8.99%
Other Paid Absences	9.54%
Bonus	0.00%
Payroll Taxes	25.68%
Health and Welfare	18.11%
Workman's Compensation (W/C), Public Liability and Property Damage Insurance	8.00%
Total	<u><u>70.45%</u></u>

Group IV - General and Administrative Employees

Sick Pay	0.90%
Holiday & Vacation Pay	9.41%
Other Paid Absences	0.81%
Bonus	0.00%
Payroll Taxes	24.05%
Health and Welfare	17.35%
Workman's Compensation (W/C), Public Liability and Property Damage Insurance	8.00%
Total	<u><u>60.52%</u></u>

Source: OIG compiled this table utilizing data provided by FEC.

² The sum of the rates in this chart may have a slight difference from the total due to rounding in the content.

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APPENDIX C – Comparison of 2020 and 2021 Rates³

Group II - Maintenance of Roadway, Equipment, and Signal Employees	2020 Submitted	2021 Submitted
Sick Pay	0.08%	0.08%
Holiday & Vacation Pay	8.09%	9.15%
Other Paid Absences	1.97%	2.20%
Bonus	0.35%	0.00%
Payroll Taxes	22.49%	24.12%
Health and Welfare	19.85%	19.16%
Workman's Compensation (W/C), Public Liability and Property Damage Insurance	8.00%	8.00%
Total	60.84%	62.72%

Group III - Transportation Employees	2020 Submitted	2021 Submitted
Sick Pay	0.15%	0.13%
Holiday & Vacation Pay	7.68%	8.99%
Other Paid Absences	7.85%	9.54%
Bonus	0.32%	0.00%
Payroll Taxes	23.61%	25.68%
Health and Welfare	16.75%	18.11%
Workman's Compensation (W/C), Public Liability and Property Damage Insurance	8.00%	8.00%
Total	64.36%	70.45%

Group IV - General and Administrative Employees	2020 Submitted	2021 Submitted
Sick Pay	0.94%	0.90%
Holiday & Vacation Pay	4.09%	9.41%
Other Paid Absences	0.84%	0.81%
Bonus	4.44%	0.00%
Payroll Taxes	22.46%	24.05%
Health and Welfare	15.97%	17.35%
Workman's Compensation (W/C), Public Liability and Property Damage Insurance	8.00%	8.00%
Total	56.73%	60.52%

Source: OIG compiled this table utilizing data provided by FEC.

³ The sum of the rates in this chart may have a slight difference from the total due to rounding in the content.

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APPENDIX D – Affected Entity Response



January 17, 2023
Florida Department of Transportation
Office of Inspector General

Kristofer B Sullivan

Cc: Mervat Bebawy
Barbara Brown-Walton
Jessica Mobley
Joseph W Gilboy

Re: Florida East Coast Railway 2021 Indirect Rates

This letter is with regard to the 2021 Indirect Rates. Per our exit conference, Florida East Coast Railway, LLC agrees with Florida Department Of Transportation that the indirect rates submitted by us for use in billing railroad highway projects for all Groups, 2, 3, and 4, are reasonable, allowable, and adequately supported.

Thank you for your quick turnaround

Yours very truly,

A handwritten signature in black ink, appearing to read 'Genaro Guerrero Diaz Mercado', written over a horizontal dashed line.

Genaro Guerrero Diaz Mercado
SVP & Chief Financial Officer

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APPENDIX E – Management Response

On January 18, 2023, the OIG received the response from Rickey Fitzgerald, Manager of the Department's Freight and Rail Office:

Finding 1 – Reasonable, Allocable, and Allowable Costs

Finding: We determined that the indirect rates submitted by FEC for use in billing railroad-highway projects for Groups, 2, 3, and 4, are reasonable, allowable, and adequately supported, and supporting records and procedures are transparent and readily understandable based on the supporting documentation provided by FEC and the applicable criteria. We also determined FEC's accounting procedures, including supporting documentation, continue to meet the visibility rule set forth in Title 48, Part 9904, Code of Federal Regulations-Cost Accounting Standards, Section 405-50-Techniques for application, which requires adequate cost identification to deem expense allowability.

Recommendation: We recommend the Department's Freight and Rail Office review and approve FEC's 2021 indirect cost rates for use in billing costs for railroad-highway projects and communicate this decision to the Federal Highway Administration.

Response to Finding: We concur with the finding and recommendation.

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Kelli Phillips, Rail Operations Administrator, Freight and Rail Office

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Angie Patton, Controller, Florida East Coast Railway
Tresa Landa, Payroll Manager, Florida East Coast Railway

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PROJECT TEAM

Engagement was conducted by:
Mervat Bebawy, Auditor

Under the supervision of:
Barbara Brown-Walton, Senior Audit Supervisor
Jessica Mobley, Deputy Audit Director for Intermodal
Joseph W. Gilboy, Director of Audit

Approved by:
Kristofer B. Sullivan, Inspector General

STATEMENT OF ACCORDANCE

The Department's mission is to provide a safe transportation system that ensures the mobility of people and goods, enhances economic prosperity, and preserves the quality of our environment and communities.

The Office of Inspector General's mission is to provide independent and objective investigative and audit services that promote accountability, integrity, and efficiency within the Florida Department of Transportation and its partners.

This work product was prepared pursuant to section 20.055, Florida Statutes, in accordance with the Association of Inspectors General *Principles and Standards for Offices of Inspector General*, and conforms with The Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

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