



Florida Department of TRANSPORTATION

Office of Inspector General
Kristofer B. Sullivan, Inspector General

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Kristofer B. Sullivan

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June 25, 2024

Audit Report No. 24I-005
Florida East Coast Railway 2022 Indirect Rates

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 (CY) 2022, 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 CY 2022 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 consider approving FEC's CY 2022 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, 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.

On June 30, 2017, Fortress Investment Group finalized its sale of FEC, a privately held company, to Grupo Mexico, a publicly traded company listed on the Mexican Stock Exchange. Since FEC uses the calendar year as its fiscal year, this means the 2017 calendar year was evenly split between the old ownership and the new.

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; and
- 48 C.F.R. 9904.405-Cost Accounting Standards

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 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 2022.
- 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).

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- 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 outlined in 48 C.F.R. 9904.405-50, which requires adequate cost identification to deem expense allowability.

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RESULTS OF REVIEW

We determined the Calander Year (CY) 2022 indirect rates submitted by FEC's Payroll Manager 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 outlined 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.

We reviewed the CY 2022 FDOT Indirect Cost Rates Reporting Packet prepared by FEC Payroll Manager and performed substantive testing as a part of our evaluation. 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).

The rate changes between CY 2021 – 2022 for Groups 2, 3, and 4 are illustrated in **Table 1**.

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Table 1: CY 2021-2022 Indirect Rate Comparison

Group 2			
Labor Surcharge Classification	Approved 2021 Rate	Submitted 2022 Rate	Rate Change Approved 2021 Rate - Submitted 2022 Rate
Sick Pay	0.000803302	0.001852	0.1%
Holiday & Vacation Pay	0.091472962	0.0837	-0.8%
Other Paid Absences	0.022048718	0.020463	-0.2%
Bonus	0	0.000085	0.0%
Payroll Taxes	0.2412	0.2398	-0.1%
Health and Welfare	0.191632442	0.201	0.9%
W/C, Public Liability & Property Damage Insurance	0.08	0.08	0.0%
Subtotal	62.72%	62.69%	0.0%
Group 3			
Labor Surcharge Classification	Approved 2021 Rate	Submitted 2022 Rate	Rate Change Approved 2021 Rate - Submitted 2022 Rate
Sick Pay	0.001267229	0.000885	0.0%
Holiday & Vacation Pay	0.089869368	0.0868	-0.3%
Other Paid Absences	0.09541503	0.131794	3.6%
Bonus	0	0.003733	0.4%
Payroll Taxes	0.256831423	0.2652	0.8%
Health and Welfare	0.181130525	0.176	-0.5%
W/C, Public Liability & Property Damage Insurance	0.08	0.08	0.0%
Subtotal	70.45%	74.44%	4.0%
Group 4			
Labor Surcharge Classification	Approved 2021 Rate	Submitted 2022 Rate	Rate Change Approved 2021 Rate - Submitted 2022 Rate
Sick Pay	0.00905	0.01047	0.1%
Holiday & Vacation Pay	0.094051276	0.073	-2.1%
Other Paid Absences	0.00812132	0.005918	-0.2%
Bonus	0	0.038527	3.9%
Payroll Taxes	0.240526283	0.2446	0.4%
Health and Welfare	0.173466373	0.1803	0.7%
W/C, Public Liability & Property Damage Insurance	0.08	0.08	0.0%
Subtotal	60.52%	63.28%	2.8%

Source: The OIG created these tables from data submitted by FEC

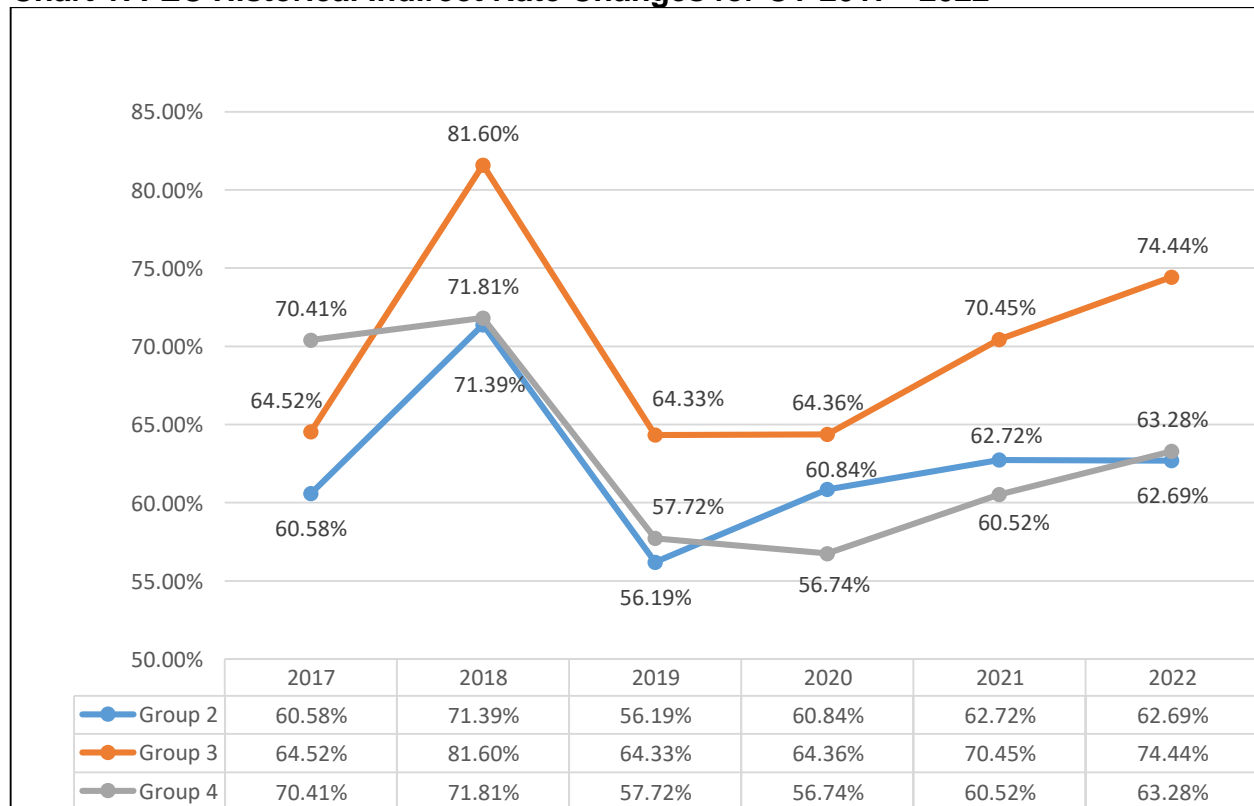
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We inquired about the increases in Groups 3 and 4 with FEC, and their explanations were as below:

- Group 3 had a total variance of a 4 percent increase. Other Paid Absences accounted for 3.6 percent of the increase.
 - Group 3 included training time and FEC paid \$746,425.03 more training in 2022 than in 2021.
- Group 4 had a total variance of a 2.8 percent increase. Bonuses increased by 3.9 percent, and Holiday and Vacation (H&V) decreased 2.1 percent.
 - Group 4 received \$385,007.00 in bonuses for 2022 and bonuses were not offered in 2021.
 - FEC paid \$64,869.90 less in vacation payouts in 2022 than in 2021.

As a part of our review of FEC Indirect Rates, we reviewed the historical rate changes for Groups 2, 3, and 4 from CY 2017 – 2022. See **Chart 1**.

Chart 1: FEC Historical Indirect Rate Changes for CY 2017 - 2022



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

We recommend the Department’s Freight and Rail Office review and consider approving FEC’s CY 2022 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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APPENDIX A – Purpose, Scope, and Methodology

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

- CY 2022 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 CY 2022 indirect rates submitted by FEC and associated records and supporting documentation.

The **methodology** included the following:

- reviewing relevant regulations:
 - 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; and
 - 48 C.F.R. 9904.405-Cost Accounting Standards, Accounting for Unallowable Costs.
- reviewing FEC's Indirect Cost Rates Reporting Packet;
- identifying and reviewing account classification differences between CYs 2021 and 2022;
- re-performing rate calculations;
- performing comparative analysis in CYs 2021 and 2022 rate data; and
- corresponding with key staff and reviewing selected work papers prepared internally by FEC.

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APPENDIX B – 2022 Labor Additive Surcharge Rates¹

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

Sick Pay	0.19%
Holiday & Vacation Pay	8.37%
Other Paid Absences	2.05%
Bonus	0.01%
Payroll Taxes	23.98%
Health and Welfare	20.10%
W/C, Public Liability & Property Damage Insurance	8.00%
Total	<u><u>62.69%</u></u>

Group III - Transportation Employees

Sick Pay	0.09%
Holiday & Vacation Pay	8.68%
Other Paid Absences	13.18%
Bonus	0.37%
Payroll Taxes	26.52%
Health and Welfare	17.60%
W/C, Public Liability & Property Damage Insurance	8.00%
Total	<u><u>74.44%</u></u>

Group IV - General and Administrative Employees

Sick Pay	1.05%
Holiday & Vacation Pay	7.30%
Other Paid Absences	0.59%
Bonus	3.85%
Payroll Taxes	24.46%
Health and Welfare	18.03%
W/C, Public Liability & Property Damage Insurance	8.00%
Total	<u><u>63.28%</u></u>

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

¹ 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 CY 2021 and 2022 Indirect Rates²

Group II - Maintenance of Roadway, Equipment, and Signal Employees	2021 Approved	2022 Submitted
Sick Pay	0.08%	0.19%
Holiday & Vacation Pay	9.15%	8.37%
Other Paid Absences	2.20%	2.05%
Bonus	0.00%	0.01%
Payroll Taxes	24.12%	23.98%
Health and Welfare	19.16%	20.10%
W/C, Public Liability & Property Damage Insurance	8.00%	8.00%
Total	62.72%	62.69%
Group III - Transportation Employees		
Sick Pay	0.13%	0.09%
Holiday & Vacation Pay	8.99%	8.68%
Other Paid Absences	9.54%	13.18%
Bonus	0.00%	0.37%
Payroll Taxes	25.68%	26.52%
Health and Welfare	18.11%	17.60%
W/C, Public Liability & Property Damage Insurance	8.00%	8.00%
Total	70.45%	74.44%
Group IV - General and Administrative Employees		
Sick Pay	0.90%	1.05%
Holiday & Vacation Pay	9.41%	7.30%
Other Paid Absences	0.81%	0.59%
Bonus	0.00%	3.85%
Payroll Taxes	24.05%	24.46%
Health and Welfare	17.35%	18.03%
W/C, Public Liability & Property Damage Insurance	8.00%	8.00%
Total	60.52%	63.28%

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 D – Affected Entity Response



April 08, 2024
Florida Department of Transportation
Office of Inspector General

Kristofer B Sullivan

Cc: Joseph Gilboy
Jessica Mobley
Nicholas Cooper
Cory Barker

Re: Florida East Coast Railway 2022 Indirect Rates

This letter is with regard to the 2022 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

Finding 1 – Reasonable, Allocable, and Allowable Costs

Finding: We determined the Calander Year (CY) 2022 indirect rates submitted by FEC’s Payroll Manager 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 outlined 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 consider approving FEC’s CY 2022 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.

Corrective Action: None

Estimated Completion Date: N/A

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Tresa Landa, Payroll Manager, Florida East Coast Railway
Yvonne Lacount, Senior Payroll Associate, Florida East Coast Railway

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PROJECT TEAM

Engagement was conducted by:
Cory Barker, Auditor

Under the supervision of:
Nicholas Cooper, Senior Audit Supervisor
Barbara Brown-Walton, Deputy Audit Director for Intermodal
Joseph W. Gilboy, Director of Audit
Jessica Mobley, Director of Quality Assurance and Operations Support

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*.

Please address inquiries regarding this report to the Department's Office of Inspector General at (850) 410-5800.