

Improving Federal-aid Financial Management: A Call for Proposals

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Introduction

Michael Kay: Welcome to be improving Federal-Aid financial management conference call. On behalf of the Federal Highway administration I would like to welcome everyone to today's webinar, Improved Financial Management. I am Michael Kay with the USDOT center in Cambridge Massachusetts and I will be moderating today's webinar as well as facilitating the question-and-answer period and helping to address any technical problems. Before we begin, I would like to point out some key features of our webinar room. On the top left side of the screen you'll find audio call in information should you get disconnected. Below that is a list of attendees, below that is a file download box you can use to download not only today's presentation but several other supplemental materials. Simply click on any one of the files and click "save to my computer" and follow the prompts on your screen. On the bottom left is the chat box you can use to submit questions to our presenters. We will be taking questions intermittently throughout the presentation so again, please submit those questions to the chat box or press star one on your telephone to ask a question by phone. We will get more instructions about that later. We are recording today's webinar so the colleagues that are unable to join us today can listen at a later date.

We will have three presenters today: first will be Mark Sullivan, Senior Advisor with the Office of Innovative Program Delivery, followed by Dave Bruce, Program Analyst with the Office of the Chief Financial Officer at the FHWA and finally Frederick Warner, Project Finance Manager with the Office of Innovative Program Delivery. And with that I would like to turn the call over to Mark Sullivan. Mark, it's all yours.

Section 1: Looking Back at Financial Innovation

Slide 4: Authorized in Title 23

Mark Sullivan: Okay, well thank you, Michael and welcome everyone thank you all for joining us on this call. I'd say it is great to see all your faces but I know you are all out there and again, we appreciate your participation. I wanted to talk for a quick second about the Office of Innovative Program Delivery and why it is that we have been put in this position, which may seem a little unusual. Where we are helping to steward an effort to improve Federal financial aid management: clearly, financial management is within the purview of the Office of the Chief Financial Officer, and the success of the whole effort will rely upon the hard work of the financial managers at both State DOT and division offices. When our Office of Innovative Program Delivery was established 3 1/2 years ago, we were given responsibility for two of the three programs at Federal Highways that are formally set up to authorize what we call at various times, tests and evaluation, or experimental processes, or any number of words that all sound like chemistry experiments going on in laboratories but actually, apply through some, I think, creative and very successful interpretation of our legal statutes. Applied to administrative activities we are talking about today. Just to ground us in the law, I want us to look at these two little sections from Chapter 5 in Title 23 which do fall under the research and development part of Federal Highways' legal authority in Title 23.

And, the excerpts highlighted here really...the language here really forms the basis for all of that experimental programs that Federal Highways does in this administrative process area. And, you may have heard of this SEP-14 which looks at contract procurement, SEP-15 which looks at promoting public-private partnerships. The third effort which is called TE-045, is focused on financial management improvement. Again, just to look at the language here it talks about how the secretary may carry out research, development, technology transfer, activities with respect to all phases of transportation planning and development and that includes areas of construction development and financing. And, in fact, the next section 502(b)2 goes further and says we may actually run some of these experiments on ourselves. We may test develop or assist testing in developing any material invention, patented article or process. One would read a string of words like that material invention patented article or process and probably think of a manufacturing process but I think we have to thank our attorneys for being able to take that word process and realize what we do every day in terms of management and administration of the Federal-Aid program is very much a process.

So, we have claimed, and I think very successfully so, the authority to deviate from certain processes. Under some controlled conditions, so that we are able to call these experiments, every kind of deviation we might perform is going to be evaluated and considered potentially a new process.

The scope of authority, because this is authorized in Title 23, the Federal-Aid title, we also have always been very clear that we are experimenting with processes that are authorized or otherwise described in Title 23. The kind of question that comes up very quickly after laying out this kind of experimental authority, is its application to certain administrative processes having to do with environmental review, right-of-way, purchases, etc. And as you get into the laws you find that most of those laws and procedures line outside of Title 23 and apply government-wide, so we are not claiming any authority to revise NEPA or any of the other Federal administrative laws throughout the government.

Slide 5: A Brief History of...TE-045

So, with that kind of clear boundary, using this authority has I think provided some very clear benefits for Federal Highways and I want to just talk about an effort that began in the mid-1990s under the initiative that was known as "Test and Evaluation" TE-045. I'm sorry I can't describe Test and Evaluation 001 through 044 or any of the ones beyond, but this one in particular was and still is, I guess that's the important point to take away from here, this authority is still very much a part of our toolbox...

It began as part of the innovative finance program in the mid-1990s. The objectives taken from the Federal Register notice that announced the program at that time, the objectives were to increase investment and accelerate projects. It's certainly no surprise that the issues that were being discussed in the mid-90s are the issues that we talk about today. And we will be talking about I am sure in the next 10 to 20 years. But that solicitation that was formally launched in 1994 asked State DOTs to propose some experimental processes, some tests, that would do a few things. In some cases, there were specific provisions in the ISTEA Bill of 1991 that, although they had been placed in statute, had had no activity at administrative level and those were the toll credit and Section 129 loan programs. So it was a specific effort to get the implementation of those programs up and going. But then also, it was a way of testing certain things that have since become very much a part of the standard terrain in Federal-Aid

financial management landscape. Things like advanced construction, partial conversion of construction, flexible match, tapered match, things that in fact were within a year were codified into Title 23, codified by the national Highway system act of 1985. The 88 initial test that were sort of approved conducted by the states really gave a lot of momentum to all of those different programs which were really all very new and untested and again have since become I think such a standard part of financial management. We can look back and really see the benefit of using this kind of authority to really jumpstart some things that the regular rulemaking processes make very difficult and very time-consuming.

When that initial burst of tests was over in the mid-1990s, the folks in the financial management office had certainly the foresight to leave the door open and to accept TE-045 proposals as ideas and new issues came to the states. Through 2003, at a much slower rate, the CFOs office was still evaluating and considering and authorizing some of these tests so the number that started with 80 grew over the next several years to be about a total of 110. That sort of is where the activity stopped. From 2004 until just a couple of years ago there were no new requests from the states at all and I don't think anyone here at headquarters would have said that we are no longer accepting proposals but as was pointed out in the web conference a few weeks ago, that may have appeared to have been the policy act the time at DOT but in fact, we have never closed the door on TE-045.

Slide 6: District of Columbia – 11th Street Bridge

The example that is on the screen right now is a story about a review and a TE-045 approval done in late 2010 where the experimental authority was able to be used in a way to address something of an anomaly in the guidance that Federal Highways currently has in place regarding GARVEE bonds and it was a situation where the District of Columbia in order to build a very large project a \$300 million project for a bridge over the Anacostia River about a mile from the DOT headquarters where I am talking from right now, the 11th St., Bridge was going to be partially funded with GARVEE bonds that the District was going to issue. And the district, all along and looking to get the bonds issued by the end of 2010, in order to take advantage of the Build America bond provisions, was planning to match \$80 million in GARVEE proceeds with \$20 million they had already spent on this project. In fact money they had advanced on the project well in excess of their local share. And that unfortunately kind of ran into issues with the GARVEE guidance, which very explicitly denies the use of a tapered match for GARVEE repayment and in effect requires states to match the debt service payments, the principal and interest payments on GARVEE bonds throughout the life of the debt service schedule. And, it was a situation that we didn't necessarily say was good government, but it was certainly something that from just reading the guidance on the face of it didn't seem to be permitted.

So the ability to intervene onto the authority of TE-045 and allowing for the district to use some of those early funds to match the GARVEE debt service and allow ultimately for Federal Highways to pay 100% of the GARVEE debt service was something that allowed the project to move forward.

In retrospect I don't think you'd look back at this and say it is all that innovative, all that unusual or exciting, but we certainly were very, very appreciative that TE-045 was available there to document our deviation from the guidance. And, as we look to revise the guidance, we will take the lesson learned

here and hopefully come up with a system that would allow these kinds of things to go forward a little bit reflectively.

Dave Bruce is going to talk in detail about the two experimental approvals that really launched this effort and I don't want to steal his thunder but, I would just say that the reason for this effort here by Federal Highways to go back out and ask all of the State DOT is to come up with their best ideas, really comes directly from the Federal Highway Administrator and I think Dave can maybe fill us in a little bit on some of the feedback that we got from him at the point when we went to him with the Vermont and California stories that he is going to talk about next. So, I think with that I will just bring my introductory remarks to an end and turn it back to Michael Kay.

Questions

Michael Kay: Great, thanks. I would like to change your layout to expand upon the chat box in of my questions people may have again of you have any questions for Mark will be happy to take them now or we will also have time later on for additional Q&A. At this point I will ask the operator, Amber, would you provide instructions about asking questions over the phone?

Operator: Yes, thank you. Ladies and gentlemen if you wish to ask a question press star then one; you will hear a tone indicating you been placed into an improbable indicate when or line is open. You may remove yourself at any time by pressing star followed by 2. If you are listening on a speakerphone please lift up your handset before pressing the corresponding digit. Again please press star one at this time.

Michael Kay: Great. We will have they present now that I did want to mention again that checkbox is now on the bottom left in your screen and if you have any questions while Davis became are looking back on Mark's presentation, please do so that those again by the chat box or pressing star one and we will adjust the letter. With that, I will turn it to Dave Bruce.

Section 2: Recent and Potential Innovations

Slide 8: Issue: Indirect Cost Allocation

Dave Bruce: Thank you, Michael and thank you, Mark. As you all are gathering, we want to keep this a fairly informal presentation today and allow sufficient time to get your questions on the table and hopefully provide you with sufficient responses as we go through this initiative. So, as Michael mentioned earlier, I am Dave Bruce, a program analyst in the policy arena for the Office of the Chief Financial Officer with the Federal Highway Administration. And the purpose for my segment of the presentation is basically to get the creative juices flowing a bit, just to get some ideas on the table, plant some seeds for some off-line discussions that you are all going to have in terms of ideas that make the most sense given your individual state situations given the parameters we will be discussing and as Mark has already alluded to.

I will go into more detail about the recent proposals. In terms of the feedback we received from the Administrator, it is a fair statement to say that he was very pleased to see the two proposals that I am going to talk about briefly and he wasted no time encouraging all of us to put our best feet forward and

to solicit additional ideas from all of you. That's been our charge for the past month or so and I will be continuing to work in a support capacity at OCFO with the office of program delivery over the upcoming months as we see this come to fruition.

So, just a little bit of background to start with; the two proposals from Vermont and California that I will be talking about, they're both initially in the area of indirect cost allocation. And just to set the table a little bit here, if you are going over these proposals, indirect cost allocation in general for anyone on the call not familiar, is really how states recover their general and administrative and other indirect costs of implementing the Federal-Aid highway program. Without getting too much into this, the state's first entered indirect cost recovery arena with the passage of TEA-21 back in November 1998.

At that time we only reimbursed direct project costs, which was in line with Title 23 of United States Code Section 302 which states that states must be suitably equipped and staffed to carry out the functions of the Federal-Aid highway program. Essentially, on their own dime, on their own time. 1998 rolls around and we've now entered the arena, we've entered the picture that most Federal grant programs have been involved in, for many generations before us. So it is nothing new in terms of indirect cost allocation but fairly new to the Federal-Aid Highway program.

Federal costs regulations, by the way, they fall outside of Title 23 USC. Generally, for states and local governments, they're at two code of federal regulations, so that is something that promulgated by the Office of Management and Budget as such generally, off the table for our experimenting, unless there is legal authority within the bounds of OMBs' cost principles elsewhere that gives us that authority.

So, by regulation, there are really two general methods for recovering indirect cost. The general, most common method is that most everybody on this call may be familiar with would be the rate method. Indirect cost rate development and charging against individual Federal-Aid projects. Also something called the Narrative Cost Allocation Methodology. It's a little bit less familiar, especially in the Federal-Aid Highway program, but even elsewhere in Federal grant management, and I will be referring to this throughout the next few slides as the NCAM: narrative cost allocation methodology.

So briefly, the description for a NCAM is really a cost allocation plan that does not use rates. Rather, it distributes costs, indirect costs, and in some even direct costs, to the specific funding sources. It's directly taken from a 2CFR 225 in appendix E. So that's what we're talking about here in terms of both proposals that Mark mentioned, a moment ago.

Even though Federal costs regulations allow for the use of an NCAM, FHWA by policy back in 2004 preclude NCAM and really limits the covers of indirect cost rates, reviewed and approved by FHWA, acting as a Federal cognizant agency in accordance with the cost principles. So, that's really the only allowed method or state to recover their general and administrative costs currently.

About half of the states currently do have an approved indirect cost rate structure in place, and this trend towards more states doing so is continuing forward. We've had a slow, steady trickle ever since 1998. And now, we are at the halfway mark. And I suspect that we'll continue to have more states

develop and implement and start using an indirect cost allocation structure to recover their indirect costs in the future.

So, I'm going to be briefly talking about these current two proposals, we are testing right now, in evaluating the NCAM.

Over the past couple of years there's been a lot of attention also paid to Federal cost principles in general. In the Federal-Aid Highway program, not just in the area of indirect cost but also applicable to direct project cost. And in that light the office of the CFO has been looking at reshaping our policy with regard to Federal cost principles in general. We anticipate that the NCAM test I'm going to be talking right here, will really help to shape our FHWA cost principles policy revisions in the near future.

Slide 9: Issue: Vermont - ER Funds

The first test was in Vermont. While I am a headquarters employee based, I am an alternate duty location employee actually based in Vermont so I'm very familiar with the background behind this test. I am just going to give you a real quick background on the emergency relief program for anybody on the conference not that familiar.

The bottom line from the Federal-Aid funding standpoint it's a one-time infusion of Federal-Aid funds. And for any of you on the audience today that has had experience with the ER program, you are already aware it is a one-time shot really an additional Federal dollars, two a states' Federal Highway program. Since indirect costs are eligible under that your program is really critical to FHWA that we get cost allocation right the first time to avoid any unintended windfalls or other reconciliation issues for the state.

Our first forays into this whole arena emerged with hurricanes Katrina and Rita where we had some issues to iron out from a technical standpoint with regard to indirect cost recovery. We have learned quite a bit since that point in time and fully understand the huge influx of Federal-Aid funds to state on a one-time basis really has a distorting effect on an indirect cost rate so the notion of a Narrative Cost Allocation Methodology really has potential and interest for us.

I will quickly go over the Vermont agency of transportation request. The storm occurred last summer. The state initial ER allocation is \$125 million, Vermont not unlike many states, is fairly cash-strapped, a small state program, they do not have an indirect cost rate structure in place, but in addition to the irregular administrative expenses currently paid for through the legislative budget process, they have additional expenses directly related to carrying out the ER program associated with Tropical Storm Irene. There was a definite need to get the cash flowing in a positive manner as soon as possible and any of you with experience in developing and reviewing an indirect cost allocation plan knows it takes not only months but in some cases years and hundreds of thousands of dollars actually develop a compliant indirect cost allocation plan.

So, the need to get the cash flowing really quickly just precluded the notion of developing an indirect cost allocation plan. Again it would've taken a lot of time and a lot of money to get accomplished. So the Vermont Agency of Transportation requested the use of the NCAM to recover their ER specific

administrative expenses only. They weren't after recovering the heat, lights and utilities at their headquarters offices, but really just administrative and indirect costs directly associated with Tropical Storm Irene.

So we worked through the draft proposal providing technical assistance, having conversations back and forth and the Administrator signed the approval for this particular task which will run until all of the Irene related projects are closed out. So, this is a bit of an anomaly in terms of the current initiative where we are looking to get a lot of these test resolved in a short timeframe but in this case throughout the Irene rebuilding and recovery effort we believe that the NCAM holds a lot of promise for providing a consistent approach to ER indirect cost recovery not only for Vermont but across the country in the future so we are eagerly anticipating the results of this test.

Slide 10: Issue: California- Local Oversight

Now, let us go forward and take a look at the California proposal. Under Title 23 in the USC section 106, as well as in the common grant rule under 49 code of Federal regulations part 18, State DOTs state deities have the responsibility for overseeing locally administered projects funded with Federal-Aid Highway dollars. This is also known in the grand language as sub recipient monitoring. Anybody who has been around the agency for a dozen or so years, or been involved with just the Federal-Aid Highway program in general even on the State DOT side or perhaps especially on the State DOT side, is aware that previous Federal Highway Administrator, declared LPA oversight as a material weakness for the Federal Highway administration. And consequently, we have put a lot of focus into this whole area of LPA oversight. We are well aware this is an area that we have had lots of issues with and continue to have a lot that we continue to iron out on a daily, monthly and annual basis. A recent US Department of Transportation Inspector General report reconfirms the ongoing concerns in this area, including those with the state of California. California's request, under this initiative, stems from the fact that their budget lacked adequate funds to increase staffing to help shore up some of the issues around their oversight response abilities. They do have an indirect cost rate structure in place unlike that in Vermont, but their current methodology does allocate to recover indirect cost against LPA administered projects. In that particular case, they used a labor-based direct labor, they don't charge any labor cost to the locally administered projects in the state of California. Hence, they had no way to recover any of their oversight cost against those projects. So their existing accounting structure really precluded them from beefing up staffing for oversight.

And the LPA administered program in the state of California is huge. There are 600 some LPA's in the state and they get a large part of the Federal-Aid funding in California. So, under their TE-045 proposal they again will be using the NCAM proposed to hire nine oversight engineers, setting up a separate Federal-Aid project, funded specifically with STP flexible funds, flexible enough and eligible for use for just about any eligible Federal-Aid activity in the Federal-Aid Highway program. They will develop a related sub recipient monitoring work plan that's reviewed and approved by the FHWA division office. So, they are working hand in glove with the division to make sure that their oversight monitoring is compliant with statute and with the common ground rule of regulation. Carrying out the activities and that worked on within the funded under the NCAM proposal. This test will last for three years with annual reviews, evaluations of effectiveness and depending on preliminary results, some possible

expansion of scope in years two and three of that particular task. California is not alone in its concerns for inadequate state funding for LPA oversight, so the NCAM does look to be promising for this particular purpose in the future as well.

Slide 11: Ideas for Potential Proposals (Narrative Cost Allocation Methodology)

Now, what I want to do now is just really plant a few seeds to kick-start the conversations in each state. So, I will just talk about a few areas potentially ripe or more testing or some initial testing. I have already mentioned the NCAM, that stems firm to 2 CFR 225 and here's the citation, appendix E paragraph F3 and within that particular provision, one of the questions that has come up is how can we test anything in this area if it is outside of Title 23? Well, the fact is it's allowed by Federal cost principles, it is only by FHWA policy, dated May 5, 2004, that we are prevented from using the NCAM for particular administrative costs borne by state government.

If you go to the cost principles it also states that the NCAM may be used to recover indirect costs and in some cases also direct costs, that really have a benefit to more than one project. It does not involve rates, so it's a departure from the standard indirect cost allocation rate that many states do charge against projects. And, it distributes cost directly to the benefiting fund sources. As I mentioned in both cases of Vermont and in California, those costs were charged to single program fund sources. In the case of Irene, for emergency relief, that was the only particular activity that was being funded was ER activities so charging it to one fund source makes sense there. LPA oversight, local projects may involve many different fund sources, but just a starting point use of STP flexible funds which may be used on any particular type of Federal-Aid projects so eligibility is perfect fine, too.

There could be other instances where finding an equitable distribution to all of the different core program fund categories might make sense. Such as national highway system, bridge project, STP and other core program fund categories. The key is there has to be a causal relationship to the various projects. So this is an area that is ripe for potential testing as I mentioned earlier, the office of chief financial officer is interested in providing additional guidance in the area of cost principles, interpretation and application in the future, and providing testing in the area of NCM might help further inform those policy revisions.

Slide 12: Ideas for Potential Proposals (Tapered Match)

Now, I will jump to something that Mark alluded to earlier. He mentioned that the GARVEE guidance currently does not allow the combined use of bond funding under 23 United States code section 122, in conjunction with the tapered match provisions. And the way the Federal-Aid Highway program works in terms of matching, is that we, meaning Federal Highway administration, reimburse states for whatever the legal Federal share of cost are on any progress voucher by progress voucher basis. Meaning that the non-Federal share or the states match must take place also on a progress voucher by progress voucher basis. Under the use of tapered match provisions, non-Federal share requirement may be met either upfront or at the tail end of the projects life. It is a documented agreement between the state and FHWA division office that allows for deviation from our standard reimbursement policy. And, that policy was devised, updated December 29, 2009, available on FHWA's external website.

So, by policy in the document, and this has been a fairly long-standing, one of the prohibitions, but currently, tapered match provisions may not be used in combination with either advanced construction, which is under 23 USC 115, or under STP program approval. Now advanced construction, what that really is, the state is reserving the right to seek Federal funding on a project at a later date by first ensuring that all the Federal requirements are met and getting Federal Highway administration to authorize the project cost before they are incurred. Those are initially reimbursed State funds only that a later point in time a State may seek to obligate Federal funds on that project through conversion of advanced construction to a Federal-Aid obligation.

So, right now by policy, we can't use tapered match in conjunction with advanced construction. So, this might be an area that a state would want to consider some ideas on TE-045 or tests to determine if there is any other advantage to consider that combination. The other example here is the STP program approval. This is under 23 US Code, section 133, subparagraph E. The provision has been around for a while. The STP program approval itself has been tested a few times. In the past I believe was tested more in the idea of saving paperwork. Now we were talking about ideas on the states might be able to gain flexibility with the use of their non-Federal funds there.

Currently, again, there is a prohibition on using the tapered match, meaning that even if a state wanted to use STP program approval where they say put 50 projects under one Federal authorization, every single voucher that they want to seek reimbursement on would have to be matched by the state at 20% every single time they voucher for reimbursement. Even though you would have just one authorization there still would be a lot of details and a lot of complexity involved in making sure the match happened, voucher by voucher. But potentially a test here would be intriguing to a state where they would be able to test the tapered match in conjunction with STP program approval. This would allow on an annual basis, possibly a state to either provide their match up front or toward the end or somewhere in the middle for example. So, just some thoughts about to kick around there for you all.

Slide 13: Ideas for Potential Proposals (Safe Harbor Indirect Cost Rate)

Now I want to talk about the concept of safe harbor indirect cost rates for a minute. You won't find this terminology directly in the cost principles but it is a concept that has some familiarity in some places.

There are two different applications that I will throw out for consideration. The first being again in the local public agency arena. There are many small local public agencies around the country. I've heard estimates in the tens of thousands for example. Some of these local public agencies regularly deal with Federal-Aid funds from different grants and as such they might already have an indirect cost rate in place approved by the cognizant agency. In other cases they might receive Federal Aid funds only on the sporadic cases and as such, they would be in a situation where they wouldn't have an indirect cost rate developed, reviewed and approved, which as I mentioned earlier, could take a long time and a lot of money. So, again this is outside of Title 23 but in 2 CFR 23, in appendix A, there is in the provision there that allows Federal agencies to work with grantees to test certain fee-for-service arrangements. So, that particular provision allows us to consider this test under the auspices of TE-045 or improving Federal-Aid financial management. So that is an option but because of the cost principles of still must be adhered to, we believe that any particular proposal should still allow the option for a local public agency to develop

a compliant, indirect cost rate or accept a conservative Safe Harbor rate that would both ease the burden for the administrative public agency as well as for the reviewing and approving State Department of Transportation.

That is an option for an idea for considering. I will throw out one more scenario under a Safe Harbor concept. Under 23 United States code section 112 B, we have the whole architectural and engineering design firm arena. And in that particular set of provisions, it says that if a firm has a far compliant, indirect cost rate, all contracting agencies must accept that rate for use in their individual contracts. There are many examples in many situations where somebody from a State DOT or engineering firm might retire or get laid off and decide that based upon their expertise, their skill set, they want to start up their own engineering firm. So one of the challenges they are going to face when trying to get government jobs is having cost history with which to develop a far complaint indirect cost rate. If they haven't had any previous contract work, they're not likely going to have any accounting data in which to develop indirect rate not will they have a cost accounting that could demonstrate the ability to capture all the costs in the right manner.

So one idea for consideration as part of the State DOT risk-based oversight framework with regard to ensuring compliance on the far cost principles by the firms would be to give small startups the option to use a Safe Harbor rate in their initial years of operation.

And using the developing and applying an indirect cost rate you have both a numerator, which is the indirect cost pool and the denominator, which is the direct hours labor charge. And the former is based upon having an office, equipment and an accounting system set up and incurring those costs. The denominator comes from actually having contracts in place. Well, in an initial few years of operation you might imagine the wide swings in those particular indirect cost rates depending on the history and availability to win jobs and contracts. So, a Safe Harbor rate would provide an opportunity for some consistency in early years avoiding the wide swings in rates. In other cases, there might be very small firms that do just some things in the A/E arena who could potentially benefit from a Safe Harbor rate always as an option. So I just want to throw the idea out there for some consideration. So at some point in time I will turn it back over to Michael.

Questions

Michael Kay: Thanks, Dave. With that we will turn to Q&A. I did see we have at least one question submitted thus far. And again please press star 1 on your telephone if you would like to ask a question by phone. Let's take a question that came in from the chat box for Mark Sullivan. Why did the number of requests drop to 0 for TE-045? Are there any lessons we learned that we can apply to the future?

Mark Sullivan: Great question. I would focus on the second part - lessons learned. I would say the key lesson is if you have a tool that nobody knows about, then it is not going to get used and I think that's probably the primary reason why we didn't see any requests and why we didn't see much action there for so long. I think folks in State DOTs may have assumed our interest in this was done.

And the examples we have covered, DC, Vermont, California, I would say each and every one of these cases came about because of a problem that we confronted and because of a member of the Chief

Financial Officer's staff, someone in fact who may have just made a presentation as part of this webinar, but it was a recognition by Federal Highways staff that there was a way to address these by using this tool.

So I think what you are seeing now, is the fact that the webinar is even happening, is because the Administrator, who has made it such an important part of his time here that Everyday Counts, we need to accelerate project delivery and we need to look to innovation. He sees this tool and has really challenged us to try and engage everybody across the country in their ideas. So anyway I hope that at least explains the recent energy behind and again we hope to see a lot of good ideas and innovations come forward.

Michael Kay: Thanks, Mark. I think that goes a long way in addressing the next question as well. A question for you, Mark but also applicable to Fred being that you are both in the office of Innovative Program Delivery. The question is: Are there any ideas for potential proposals that you would add to the ones that Dave already mentioned from the OIPD perspective?

Mark Sullivan: Fred has a great deal of background in the Federal-Aid program as a former financial manager. So, he could probably speak with a great bit more authority than I can. But I would just want to reiterate the point that from the point of view of the expertise I think I see that it really all lies with the financial management community and I look at the innovative program delivery office as being just sort of the stewards of this special experimental authority. So, we are not going to get anywhere without the substantive expertise and ideas that are going to come out of things like this call.

I think Dave has provided would seems to me a very interesting list and I am hopeful and expectant there will be some other things we haven't even considered.

Michael Kay: Great. Thanks. Mark. The next question is from Missouri: Were you going to set out a list of current TE-045 projects to avoid duplication of effort??

Mark Sullivan: I can do it. We got the question we talked internally a couple of weeks ago. Certainly there is a report on the mid-90s effort that we will post on our web room library. We will make some documents available. But, this whole idea of duplication, I am not sure how much that is going to apply. I think that if we see 10 different states looking to apply all the same innovative process, I think the inclination here is to say yes to every one of them. So, don't think of these as simply being unique activities happening in different state locations. I think the more experience we have with any one technique, think the more we will learn. It is certainly our inclination to have as large a cohort of tests as possible and if you look back again at the original 88 proposals, there were several dozen that were the same. When it came to advancing things like advanced construction, partial conversion, advanced construction. So, duplication is not a bad word, not something to avoid.

Michael Kay: Great. And this is another opportunity to remind everyone of the files available for download today. At the top of the file download box is this presentation and also an action memo from Administrator Mendez that speaks to his vision for this new round of submissions. Next is the DOT press release on both the California and Vermont project, and finally we included the submission form for new

proposals both in Microsoft Word and in PDF version. Those are both available for download. Fred will go into a little more detail on the submission form in a minute but I want to allow a moment to ask our operator, Amber, if we have any questions in the phone queue?

Operator: There are no phone questions at this time.

Michael Kay: Great. Thanks, Amber. I did see another question came as we look at that and move on to Fred. From FDOT: Would a TE-045 to use NCAM for indirect on ARRA to utilize the annual re-use amount released from projects be a possibility? In Florida, this would be about \$1.25 million per year? Several of our ARRA upward adjustment transfers were determined to be "scope changing."

Dave Bruce: Okay this is Dave Bruce. I will take a stab at that. This would be something we would have to have conversations off-line about because of what you just mentioned there, the notion of scope changing. With regard to the Recovery Act in particular, we have to be very sensitive to that. So, in theory, if indirect costs were not already authorized upfront, that could present somewhat of a challenge but again we can have a conversation off-line to ensure that we are thinking this through.

Michael Kay: As a reminder we will provide the contact information for Mark, Dave and Fred at the conclusion of the webinar and it's also available in the presentation download.

Frederick Warner: This is Fred. I would like to comment that we don't want either the divisions or states to get a sense that anything is entirely and totally off the table so I would encourage the folks in Florida to have robust discussions with Mark and Dave and me and determine whether that could fit in somehow to the financial management improvement context and format. So, I don't want to say no. I'm a little more positive than Dave, understanding we have to be very, very sensitive about issues relating to ARRA.

Dave Bruce: This is Dave again, Fred is probably going to be getting into this, but we will probably need to talk about the best way to bring the technical questions to the front and it might be through Fred initially. I don't know if you will talk about that, Fred.

Fred: I am now.

Dave. Excellent.

Michael: Very good. With that segue, I think Fred will move on to talk about the processing time table.

Section 3: Process and Timetable

Slide 16: Schedule

Frederick Warner: Thank you Michael and I would like to thank I guess it got about 150 people connected so thank you so much for taking time out of your day to join us and hopefully this'll be a productive effort and hopefully we will see some proposals from states out there.

My name is Frederick Warner and I am a project finance manager with the office of Innovative Program Delivery in headquarters. Like Dave Bruce, I am located outside of the national capital region. I am located in lovely Atlanta Georgia, rather than Vermont. But, I am a headquarters employee. Before I was assigned to the headquarters office of Innovative Program Delivery, I spent 10 years with the Resource Center as a member of the innovative finance technical services team and prior to that I spent eight years in the Puerto Rico division as financial manager. So I have had the opportunity to see things from both the headquarters perspective as well as the field perspective and hopefully what I can bring to the table on the process is to marry the two perspectives and to bring different points of view together in a synergistic way.

My section is called process and time table which is basically how to do this. As we all know the devil is in the details. This may sound like a great concept or a great idea and they are, but basically you need to have a step-by-step approach to how you go about indicating your state interest in this initiative. Our first webinar, with Administrator Mendes was held internally within Federal Highway to give the Federal Highway division folks a heads up and to let them know they should be contacting states to demonstrate to indicate to emphasize the Administrators interest in this endeavor.

Today we are focusing on State DOTs and territorial DOTs, but bear in mind that folks from the Division will also be participating and we are more than happy to have you on the line or on the net as the case may be.

June 28 is the deadline for proposals, so we've got a little bit more than a month to develop proposals and submit them in accordance with the submission form I will be talking about a little bit later. August 15 is the announcement of proposals authorized for testing and evaluation, and that means that from June 28 through August 15, Mark Sullivan, Dave Bruce and his folks and I will be quite busy, I would say will be busier than over caffeinated bees looking at these proposals, assessing them and ranking them for the administrative consideration, and for our directors consideration, prior to sending them up to the Administrator. In November, on a date yet to be determined, there will be a Federal Highway award to the division office that sponsors the best idea and that's something we are hoping will engender a high level of interest in the field.

August 15 of next year is our target date to mainstream all innovations that demonstrate benefit and while we understand that some of these innovations may have a multiyear impact or multiyear innovation period, we are trying to identify and select those innovations that have a relatively quick turnaround. So, we did select the August 15 date and we are hopeful that the innovations can be mainstreamed quickly.

Now, let's go on to the submission form and as you can see on the left-hand side of your screen there is a submission form that is available if you want to look at that as I speak. Let's talk about the description section and I will be going section by section.

Slide 17: Submission Form – Description

The description section is section A. The proposal should be transmitted using this form and the reason we say that is sometimes we get applications for TE-045 in a narrative format and while we're certainly

interested in new ideas and we encourage new ideas, it would be helpful to channel your innovation and your energy into this form to ensure consistency and to ensure speed. We are trying to facilitate the evaluation of proposals and speed that evaluation up to the extent possible.

The proposal should not exceed five pages, including the form itself but excluding exhibits. I know that might be a challenge for some folks because we want to fully describe what we plan to do. But, if you could try to limit the proposal to five pages, that would be helpful to us.

And, it would be helpful to you because we can get to them faster and complete the review as quickly as we would like to. The description should include the purpose of the innovation, various elements and mechanics of operation, and any cost associated with its implementation. When we are talking about costs, we are talking about all resource cost, including staff time. The description should identify the existing Federal Highway regulation, guidance, policy or practice that the proposal would revise. And, here we are talking about formal and informal barriers to doing what you feel would be appropriate for your state. The formal barriers obviously are the regulation, policy; and informal barriers are practice. I remember from my days as financial manager down in Puerto Rico, many times I would call our old Region 1 office in Albany and I would be told “well, we just don't do that,” and sometimes there would be a regulatory basis and sometimes it would be practice. We want to perhaps not break those barriers but certainly challenge them and consider whether they should be broken. The proposal should be clear and yet succinct. And I know that's difficult for us because we like to make sure everyone has all of the information necessary to evaluate the proposal, but again: clear and succinct.

Slide 18: Submission Form – Participants

The next session is Participants and that is section B. During the process we expect close and continuing cooperation between division office and State DOT. And cooperation will be required throughout the process. Through the application process, that is between today and June 28, through the application evaluation process from June 28 to August 15, to the implementation and evaluation phases from August 15 of this year through August 15 of next year. So, we're talking about a close and continuing cooperation. The people who are identified need to make a commitment to this effort and need to have the time to do a serious job and a good job at it. Key contacts with requisite authority for decisions that they are going to be making should be identified.

Slide 19: Submission Form – Potential Benefit

Potential benefit and this is section C. I think of Puerto Rico we call this “the ham and the sandwich.” This is really what it's all about. You need to, if you are in the state, or the division working with in partnership with the state, you really need to focus on a reduction in costs and acceleration in project delivery dates, or an optimization of the state cash flow.

Now, let's work at reduction in overall cost. We're all trying to do more with less and I know that's a little trite, but the bottom line is will this proposal reduce Federal-Aid, state or local costs? Or some combination of costs? We are not saying that it HAS to reduce costs, but that would be a big plus and we would be happy to see that. Now if the proposal indicates that costs are going to be reduced, we would like it to show exactly how the proposed innovation will generate cost savings.

How would the applicant qualify and calculate these savings and what support or documentation can the applicant provide? Again, number one big, big factor here is reduction in overall cost. The next factor to consider would be acceleration in project delivery dates. Would project delivery dates be accelerated? And if so, how would the proposed innovation do that? How does the proposed innovation generate time savings? Now, how are the savings quantified or calculated? And again, what support can the applicant provide?

The third major area would be optimization of state cash flow. Would it be improved or enhance? And if so, again this sounds like I am playing a broken record because I am. Specifically how would the proposed innovation improve or enhance the cash flow? And how would the applicant quantify or calculate the improvement? What support or documentation can the applicant provide to back up the claim?

Slide 20: Submission Form – Other

And the next category is Other. We don't want to limit or constrain in any way the creativity of the folks on the line or on the net. So, if there is a benefit that can be demonstrated, we want to see that as well. Now, bearing in mind as we fill out the potential benefits form, or section of the form rather, bearing in mind third party impact, we would like the proposal to state whether there is an adverse impact or effect on any third-party such as a non-Federal Highway, non-State DOT entity. If so, describe.

Slide 21: Submission Form – Implementation

The next section is section D on Implementation. We are looking for an implementation timetable including milestone dates, to be included as part of the submission form package. If the implementation is affected by upcoming Federal or state deadlines, that should be noted. And how would the state determine, (this is critical, this is key), how would the state determine the potential of innovation to become standard practice within the one-year period? Either in its state or nationwide. Again, I will say this again, because this is of critical importance. How would the state or territory determine the potential innovation to become standard practice, either in that state or nationwide?

Slide 22: Submission Form – Controls

The next section of the application of the submission form is Controls. The applicant should consider the proposed innovation effect on division's oversight and monitoring responsibility. Would the innovation make an undue burden or make it an undue request of the divisions monitoring capability and responsibility? This section should consider the effectiveness of state internal controls and the ability to comply with the appropriate accounting standards.

What is the impact of the proposed innovation on state internal controls and ability to comply with these standards? And, what is the proposed innovation's effect on audit vulnerability at both Federal Highway and at the state? I think we're all willing to accept a little bit of additional risk as long as we know what it is and as long as we can sit down with our auditors and have a conversation to explain any potential vulnerabilities.

Slide 23 Other information

There are some additional sections of so-called other information, contact information and signature and we are hoping that information is self-explanatory and that folks don't really need clarification on how to fill those sections out. If there are questions on the submission form or if there are questions on the financial management improvement initiatives in general, we encourage folks to contact Mark Sullivan, contact Dave Bruce, or contact me, either telephonically or through e-mail to resolve those questions as quickly as possible. If there are questions that we need to discuss off-line or that means in my way of thinking anyway, before the submission form is completed, if the proposed innovation seems little out there, a little too out there we would encourage you to set up some calls, set up some e-mail correspondence to discuss whether we feel that it can be channeled, focused, and can be in fact included on the submission form for the financial management improvement initiative. And, Dave, I don't know if that addressed your concern? It was pretty quick and pretty general but do you think the technical assistance issue has been addressed?

Dave Bruce: Yes. I just thought it would be important for folks to know who they should be contacting here. Thinking about managing workload to make sure everybody's expectations are met is my big concern.

Frederick Warner: I believe I am listed as the contact on the submission form for questions, on the form itself and that is fine. I happy to address any kinds of questions or concerns. I think Mark Sullivan and Dave Bruce are also good options especially for the next week or so because I will be on annual leave., After that it would be able to respond to questions pretty quickly, I think. And now, I turn it back to Michael Kay.

Questions

Michael Kay: Great. Thanks a lot, Fred we appreciate it. I want to read everyone's contact information. Again, if you are able to download the presentation, you can have this archived locally on your computer, but there of course is Mark Sullivan's contact information, he would be happy to field your inquiries and next is Dave Bruce, with the office of the CFO, and Frederick Warner and as he mentioned, his contact information is also provided on the submission form itself.

Dave Bruce: I would just like to add a little bit of additional information on who to contact. Because this is really a joint effort between the State DOT and FHWA division office, I would strongly encourage the state, with any questions they might have, to work closely with their division office and especially the financial manager, as maybe an initial point of contact. Because I think those folks in the divisions are well-equipped to handle a lot of the basic information regarding financial management and they can also help funnel those questions as well. I just have that additional thought.

Frederick Warner: That's a great point, day. I apologize for not mentioning that. We prefer, we are not going to turn away any call or e-mail, but we prefer to have issues and concerns addressed through the division offices and in fact, if I receive a call from the state of Saskatchewan for example, I would call the Saskatchewan division to make sure that we properly coordinate the reply.

Michael Kay: And with that we will turn to our final Q&A segment. I will go ahead and modify our view slightly to expand upon our chat box. Again, now is the time to submit any last questions you have for the presenters. We are happy to stick around until such time as we answer all of your questions. Again please do that to the chat box or by pressing star 1 on your telephone.

Operator: There are no phone questions at this time.

Michael Kay: Thank you Amber. We will wait around a few minutes but in the meantime I will provide another reminder about the file download box on the middle left of the screen where you can get the presentation, action memo, DOT press release and finally the submission form in both Microsoft Word and PDF format. I think most of you will find the PDF format more user-friendly especially if you have an updated version of Acrobat and can automatically fill in the fields. So, please do submit that. Use that if you are able to. I do see that we have at least one division typing in at the moment. I did want to open it back up to Mark, Dave or Fred if you have any additional comments?

Dave Bruce: I guess while we are waiting for the message to get on the screen here, just follow up a little bit again regarding the TE-045 question posed on the chat pod here and in line with Fred's initial thoughts, we are not wanting to say no on the webinar to any particular proposal. We encourage any ideas you have. Get together with your division office, have your conversations with them and pose the question and we will definitely be happy to entertain any and all of these ideas. Thanks.

Michael Kay: Thanks a lot, Dave. And the question has come in from the Oregon division. Will the proposals go through the divisions or directly to IPD? That is for Fred.

Frederick Warner: My assumption, and Mark correct me if I'm wrong, but my assumption is that the proposals will go through the divisions to IPD.

Mark Sullivan: Fred, you skipped right over that part of your presentation when you said we will not talk about the signatures. I'm sure you can all figure that out. In fact, the form calls for both the division office and the State DOT to provide signatures of the responsible parties, to ensure this thing would happen as planned, so it's definitely going to be a submission by two parties in agreement as to the innovation they are looking to jointly implement.

Dave Bruce: I have one other comment. Fred talked about the internal controls discussion and the impact on monitoring and everything, so any idea that is presented, if it involves additional resources at the division office level, there definitely needs to be coordination, putting any concerns to rest or couching those concerns to so that's another reason to work out the details ahead of time.

Frederick Warner: I would like to offer another perspective on why a number of TE-045 requested proposals dropped off markedly after 2003. I think in the early 2000s, we were very much into implementation of a lot of innovative finance concepts and that coincides with when the resource Center and technical services team was out there and there was so much effort and so much confusion about the innovative finance techniques that have been deployed that I think that is where state and

division tension was temporarily placed. That is my personal take on that, but we've had a good long resting time and I think it's ready for more innovation and more creativity.

Michael Kay: That's all right, Fred. I don't see any other questions in the chat box so, I think we are about to conclude here. I did want to check for more time with Mark, Dave and Fred if they have any last minute parting words for us otherwise we are about to complete for the day.

Mark Sullivan: Thanks, Michael. As always I want to thank the folks for sticking it out and staying until the end of the webinar and I hope your minds are buzzing away, working on some ideas. We really look forward to shepherding them through the process.

Dave Bruce: Mark, this is Dave. One question, maybe it was already covered and I missed it, but June 28 is the deadline for providing this proposal but we will be encouraging people to make early submittals as well, correct?

Mark Sullivan: Indeed we will. We didn't emphasize that.

Dave Bruce: The early bird gets the worm...

Mark Sullivan: Well, no one is really advantaged or disadvantaged for submitting early.

Dave Bruce: Potentially for resource management - just wanted to throw that idea out.

Mark Sullivan: I think that well worth saying.

Dave Bruce: We have a question in the chat pod been formed.

Michael Kay: We do indeed. We will wait around 30 seconds to see if it comes in. Would be possible to get a copy of the California TE-045 application?

Mark Sullivan: I would think so... I am not hearing any objection from Dave or Fred. I think that is a yes. Just for courtesy, I would want to make sure that is okay with the folks in California, but I would be happy to post that in this project library as an example of a recent request.

Michael Kay: We will be posting the audio for the webinar and several other documents online, not only on our internal DOT Staffnet site, but I believe we will find a place on an external website from which you can download these materials. We will be back in touch after the webinar with some follow-up information on how you can access this information.

Michael Kay: For those of you on the call, the California division is supportive [of releasing their request]. Real-time decision-making... how do you like that?

Mark Sullivan: We will get that posted and Dave, let's check with Vermont too.

Michael Kay: Thanks, everybody hope you have a wonderful afternoon.