



July 27, 2018

VIA ELECTRONIC MAIL

Ms. Mary Mitchelson  
Inspector General  
Corporation for Public Broadcasting  
401 Ninth Street NW  
Washington, D.C. 20004

Dear Ms. Mitchelson,

RE: Viability of Indirect Administrative Support Basic Method Option – Other Matters Report  
Number L-ACJ1706-1805

We disagree with your conclusions and recommendations largely as they are based on a sample of two joint licensee, “judgmentally” selected essentially because they reported more indirect administrative support (IAS) using the basic methodology than other stations. Accordingly, these results are not a statistically reliable sample since there are 164 television and radio stations that use this method. While any audit may yield instructive information, a 2.4 percent sample size is not a sufficient basis to determine that the allocation is not reasonable or to support the other conclusions in the report.

Other concerns we have with the report follow.

*Impact of the Misreporting: less than 1%*

To understand the implications of the report, it is important to note that public media stations raised \$2,376,767,457 in non-federal financial support in 2016 of which the misreporting in these two audits accounts for less than 1 percent. The resulting overpayments in each station’s community service grants (CSG) are shown below.

Moreover, the audit of KPBS found that 60 percent of the errors were the result of costs that were incorrectly included as both indirect and direct costs and that it had not reviewed its accounting for these costs or our instructions explaining how to calculate IAS i.e. our Financial Reporting Guidelines (Guidelines) in at least 15 years. Similarly, the other station audited acknowledged that it had not reviewed the Guidelines in eight years. These errors are evidence that the Guidelines were not the source of the misreporting.

	NFFS	CSG	Overpayment
KPBS Television & Radio	\$27,433,432	\$3,175,722	\$123,706 <sup>1</sup>
Houston Television & Radio	\$19,721,159	\$2,338,322	\$198,104 <sup>2</sup>

*Basic Method Includes Mission Costs*

You provide no evidence to prove that the basic method results in a misallocation when compared to the federal method for calculating indirect costs. We designed the basic method to recognize only “mission” costs when calculating IAS. Mission costs are defined in the Guidelines as instruction, research and public service, net of capital outlays. We deliberately excluded non-mission costs, such as football and other sports teams, academic support, auxiliary services and student services. In addition, mission costs may not be included unless they meet several conditions, primarily that they provide an “essential and continuous benefit” to the station. With this approach and consistent with our objectives, the station’s indirect costs are limited and in direct proportion to its licensee’s mission costs. To illustrate, if we increased the KPBS licensee’s net direct activities costs \$25,000,000 higher than the station reported, the rate would decrease only slightly: from 5.8 to 5.36 percent for television and 2.32 to 2.15 percent for radio (see Exhibit A, attached).

*Basic Methodology Effective 22 Years*

Since we introduced the basic method over the past 22 years, we are not aware of any audits until recently that questioned the effectiveness of this methodology nor expressed any concerns about the Guidelines. Your prior audits cited the Guidelines to support your findings. Therefore, we strongly disagree with your conclusions.

Additionally, to ensure accurate reporting we require the station’s IAS calculation be reviewed and attested to by its independent auditor when it submits that information to CPB. The underlying principles are well-known to independent accountants and we are not certain why they did not detect the errors. While we welcome any suggestions on how to improve the Guidelines, there is no evidence in either audit that proves that the Guidelines played a role in the misreporting. We believe our approach continues to be sound.

Lastly, you note that the basic methodology is complicated and on that we agree. We are in the process of evaluating all appropriate methodologies for calculating indirect costs to improve the consistency and accuracy of reporting those costs which may be time consuming, in part because we anticipate it will involve a system consultation.

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<sup>1</sup> The amount differs slightly from that reported by the OIG because the actual incentive rate of return was unavailable.

<sup>2</sup> The amount differs slightly from that reported by the OIG because CPB recognized a small portion of auxiliary costs that were disallowed by the OIG, which reduced the CSG overpayment.

Regards,



Jackie J. Livesay  
Assistant General Counsel & Vice President, Compliance

**CC: VIA ELECTRONIC MAIL**

Michael Levy, Executive Vice President & Chief Operating Officer, CPB  
Steven J. Altman, Executive Vice President & Chief Policy & Business Affairs Officer, CPB  
J. Westwood Smithers, Jr., Senior Vice President & General Counsel, CPB  
William P. Tayman, Jr., Chief Financial Officer & Treasurer, CPB  
Ted Krichels, Senior Vice President Station Development & Media Strategy, CPB  
Kathy Merritt, Senior Vice President, Journalism & Radio, CPB  
Erika Pulley-Hayes, Vice President, Radio, CPB  
Greg Schnirring, Vice President, CSG & Station Initiatives, CPB  
Katherine Arno, Director, TV CSG Policy & Review, CPB  
Andrew Charnik, Director, Radio CSG Policy & Administration, CPB  
Nadine Feaster, Director, Grants Administration, CPB

## Exhibit A

### Basic Methodology vs. Proposed Methodology

Using KPBS as an example, if its licensee's net direct expenses are increased by a hypothetical \$25 million, the rates for television and radio are slightly reduced. This rate is one of two components (i.e. it is combined with the physical plant support component).

<b>Net Direct Expenses</b>	<b>Basic Methodology</b>	<b>Proposed Methodology</b>
Television:		
Station's Net Direct	\$17,496,287	\$17,496,287
Divided by: Licensee's Net Direct	\$301,446,102	\$326,446,102
<b>Rate</b>	<b>5.80%</b>	<b>5.36%</b>
Radio:		
Station's Net Direct	\$7,003,540	\$7,003,540
Divided by Licensee's Net Direct	\$301,446,102	\$326,446,102
<b>Rate</b>	<b>2.32%</b>	<b>2.15%</b>