



**John Keel, CPA**  
**State Auditor**

A Report on

**State of Texas Compliance with  
Federal Requirements for  
Selected Major Programs at the  
Water Development Board for  
the Fiscal Year Ended  
August 31, 2011**

February 2012  
Report No. 12-022



A Report on

# State of Texas Compliance with Federal Requirements for Selected Major Programs at the Water Development Board for the Fiscal Year Ended August 31, 2011

SAO Report No. 12-022  
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## Overall Conclusion

The State of Texas complied in all material respects with the federal requirements for the Capitalization Grants for Clean Water State Revolving Funds Program (Clean Water Program) and the Capitalization Grants for Drinking Water State Revolving Funds Program (Drinking Water Program) in fiscal year 2011.

As a condition of receiving federal funding, U.S. Office of Management and Budget (OMB) Circular A-133 requires non-federal entities that expend at least \$500,000 in federal awards in a fiscal year to obtain annual Single Audits. Those audits test compliance with federal requirements in 14 areas, such as allowable costs, cash management, and monitoring of non-state entities (subrecipients) to which the State passes federal funds. The requirements for 1 of those 14 areas vary by federal program and outline special tests that auditors are required to perform, such as requirements related to environmental reviews and financial commitments that the Water Development Board (Board) is required to make to its subrecipients. The Single Audit for the State of Texas included (1) all high-risk federal programs for which the State expended more than \$86,555,601 in federal funds during fiscal year 2011 and (2) other selected federal programs.

From September 1, 2010, through August 31, 2011, the State of Texas expended \$57.5 billion in federal funds for federal programs and clusters of programs. The State Auditor's Office audited compliance with requirements for the Clean Water Program and the Drinking Water Program at the Board, which spent \$118,493,468 in federal Clean Water Program funds and \$129,816,058 in federal Drinking Water Program funds during fiscal year 2011.

### The Capitalization Grants for Clean Water State Revolving Funds Program

The Capitalization Grants for Clean Water State Revolving Funds Program (Clean Water Program) provides states with a long-term source of financing for construction of wastewater treatment facilities and implementation of other water quality management activities.

### The Capitalization Grants for Drinking Water State Revolving Funds Program

The Capitalization Grants for Drinking Water State Revolving Funds Program (Drinking Water Program) provides states with a long-term source of financing to cover the costs of drinking water infrastructure.

The U.S. Environmental Protection Agency provides funding to the Water Development Board (Board), which then provides loans or grants to local entities to finance construction of wastewater treatment facilities, implementation of other water quality management activities, and drinking water infrastructure development projects. Repayments on the loans are made to the Clean and Drinking Water State Revolving Fund to finance additional projects.

*This audit was conducted in accordance with Single Audit Act Amendments of 1996 and Office of Management and Budget Circular A-133.*

*For more information regarding this report, please contact James Timberlake, Audit Manager, or John Keel, State Auditor, at (512) 936-9500.*

## Key Points

**The Board did not consistently base its payroll charges on actual work completed.**

For both the Clean Water Program and the Drinking Water Program, the Board based its payroll charges for certain employees expected to work on multiple activities on a predetermined level of effort estimate that it developed at the beginning of the fiscal year, rather than on an after-the-fact distribution of actual time worked. As a result, not all payroll charges were supported by actual timekeeping records. This was a material weakness for both the Clean Water Program and the Drinking Water Program (see text box for definitions of finding classifications).

### Finding Classifications

Control weaknesses are classified as either significant deficiencies or material weaknesses:

- A **significant deficiency** indicates that control weaknesses existed, but those weaknesses would not likely result in material non-compliance.
- A **material weakness** indicates that significant control weaknesses were identified that could potentially result in material non-compliance with the compliance area.

Similarly, compliance findings are classified as either non-compliance or material non-compliance, where material non-compliance indicates a more serious reportable issue.

**The Board could not always provide evidence that it consistently communicated required information to its subrecipients.**

The Board was unable to provide evidence that it communicated all required information to one subrecipient of the Clean Water Program and one subrecipient of the Drinking Water Program. This was a significant deficiency for both the Clean Water Program and the Drinking Water Program.

For one subrecipient of the Drinking Water Program, the Board did not issue a management decision on audit findings within six months of receipt of the subrecipient's audit report. This was a significant deficiency for the Drinking Water Program.

**Auditors followed up on two findings at the Board from the prior fiscal year related to the Drinking Water Program. The Board fully implemented the recommendations for both findings.**

## Summary of Management's Response

Management generally concurred with the audit findings. Specific management responses and corrective action plans are presented immediately following each finding in this report.

## ***Summary of Information Technology Review***

The audit work included a review of general and application controls for key information technology systems related to the Clean Water Program and the Drinking Water Program at the Board. Auditors did not identify any significant weaknesses related to the information technology systems reviewed.

## ***Summary of Objectives, Scope, and Methodology***

With respect to the Clean Water Program and the Drinking Water Program, the objectives of this audit were to (1) obtain an understanding of internal controls, assess control risk, and perform tests of controls unless the controls were deemed to be ineffective and (2) provide an opinion on whether the State complied with the provisions of laws, regulations, and contracts or grants that have a direct and material effect on the Clean Water Program and on the Drinking Water Program.

The audit scope covered federal funds that the State spent for the Clean Water Program and for the Drinking Water Program from September 1, 2010, through August 31, 2011. The audit work included control and compliance work at the Board.

The audit methodology included developing an understanding of controls over each compliance area that was material to the Clean Water Program and the Drinking Water Program. Auditors conducted tests of compliance and of the controls identified for each compliance area and performed analytical procedures when appropriate. Auditors assessed the reliability of data the Board provided and determined that the data provided was reliable for the purposes of expressing an opinion on compliance with the provisions of laws, regulations, and contracts or grants that have a direct and material effect on the Clean Water Program and the Drinking Water Program.

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# Independent Auditor's Report

*State of Texas Compliance with  
Federal Requirements for  
Selected Major Programs at the  
Water Development Board  
for the Fiscal Year Ended  
August 31, 2011*



John Keel, CPA  
State Auditor

Report on Compliance with Requirements that Could Have a Direct and Material Effect on  
The Capitalization Grants for Clean Water State Revolving Funds Program and  
The Capitalization Grants for Drinking Water State Revolving Funds Program and on  
Internal Control Over Compliance in Accordance with  
U.S. Office of Management and Budget Circular A-133  
Independent Auditor's Report

## Compliance

We have audited the State of Texas's (State) compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program for the year ended August 31, 2011. Compliance with the requirements of laws, regulations, contracts, and grants applicable to the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program is the responsibility of the State's management. Our responsibility is to express an opinion on the State's compliance based on our audit.

Except as discussed in the following paragraph, we conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program occurred. An audit includes examining, on a test basis, evidence about the State's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the State's compliance with those requirements.

This audit was conducted as part of the State of Texas Statewide Single Audit for the year ended August 31, 2011. As such, the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program were selected as major programs based on the State of Texas as a whole for the year ended August 31, 2011. The State does not meet the OMB Circular A-133 requirements for a program-specific audit and the presentation of the Schedule of Program Expenditures does not conform to the OMB Circular A-133 Schedule of Expenditures of Federal Awards. However, this audit was designed to be relied on for the State of Texas opinion on federal compliance, and in our judgment, the audit and this report satisfy the intent of those requirements. In addition, we have chosen not to comply with a reporting standard that

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specifies the wording that should be used in discussing restrictions on the use of this report. We believe that this wording is not in alignment with our role as a legislative audit function.

In our opinion, the State complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on the Capitalization Grants for Clean Water State Revolving Funds Program and on the Capitalization Grants for Drinking Water State Revolving Funds Program for the year ended August 31, 2011. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as items:

Agency	Cluster or Program	Compliance Requirement	Finding Number
Water Development Board	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds	Allowable Costs/Cost Principles	12-188
	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds - ARRA		
	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds	Subrecipient Monitoring	12-189
	CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds	Allowable Costs/Cost Principles	12-190
	CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds - ARRA		
	CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds	Subrecipient Monitoring	12-191

### Internal Control Over Compliance

The management of the State is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program. In planning and performing our audit, we considered the State's internal control over compliance with requirements that could have a direct and material effect on the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the State's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in the State's internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material

weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses and other deficiencies that we considered to be significant deficiencies.

A *deficiency in internal control over compliance* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the following deficiencies in internal control over compliance which are described in the accompanying Schedule of Findings and Questioned Cost to be material weaknesses.

Agency	Cluster or Program	Compliance Requirement	Finding Number
Water Development Board	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds	Allowable Costs/Cost Principles	12-188
	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds - ARRA		
	CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds	Allowable Costs/Cost Principles	12-190
	CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds - ARRA		

A *significant deficiency in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the following deficiencies in internal control over compliance which are described in the accompanying Schedule of Findings and Questioned Costs to be significant deficiencies:

Agency	Cluster or Program	Compliance Requirement	Finding Number
Water Development Board	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds	Subrecipient Monitoring	12-189
	CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds	Subrecipient Monitoring	12-191

### Schedule of Program Expenditures

The accompanying Schedule of Program Expenditures for the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program (Schedule) of the State for the year ended August 31, 2011, is

presented for purposes of additional analysis. This information is the responsibility of the State's management and has been subjected only to limited auditing procedures and, accordingly, we express no opinion on it. However, we have audited the Statewide Schedule of Expenditures of Federal Awards in a separate audit, and the opinion on the Statewide Schedule of Expenditures of Federal Awards is included in the *State of Texas Federal Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2011*.

The State's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the State's responses and, accordingly, we express no opinion on the responses.

This report is intended for the information and use of the Governor, the Members of the Texas Legislature, the Legislative Audit Committee, the management of the State, KPMG LLP, federal awarding agencies, and pass-through entities. However, this report is a matter of public record, and its distribution is not limited.

John Keel, CPA  
State Auditor

February 21, 2012

**Schedule of Program Expenditures for**  
**The Capitalization Grants for Clean Water State Revolving Funds Program and**  
**The Capitalization Grants for Drinking Water State Revolving Funds Program**  
**For the State of Texas**  
**For the Year Ended August 31, 2011**

Schedule of Program Expenditures Capitalization Grants for Clean Water State Revolving Funds Program			
Agency	Pass-through to Non-state Entity	Direct Expenditures	Totals
Water Development Board			
Other than American Recovery and Reinvestment Act	\$ 1,645,453	\$ 20,427,371	\$ 22,072,824
American Recovery and Reinvestment Act	95,280,361	1,140,283	96,420,644
<b>Total for Clean Water State Revolving Funds Program</b>	<b>\$96,925,814</b>	<b>\$21,567,654</b>	<b>\$118,493,468</b>

Schedule of Program Expenditures Capitalization Grants for Drinking Water State Revolving Funds Program			
Agency	Pass-through to Non-state Entity	Direct Expenditures	Totals
Water Development Board			
Other than American Recovery and Reinvestment Act	\$ 48,347,663	\$3,633,384	\$ 51,981,047
American Recovery and Reinvestment Act	76,650,485	1,184,526	77,835,011
<b>Total for Drinking Water State Revolving Funds Program</b>	<b>\$124,998,148</b>	<b>\$4,817,910</b>	<b>\$129,816,058</b>
Note: Federal expenditures for the Capitalization Grants for Drinking Water State Revolving Funds Program at state entities not included in the scope of this audit totaled \$11,131,443 for the year ended August 31, 2011.			

# Schedule of Findings and Questioned Costs

*State of Texas Compliance with  
Federal Requirements for  
Selected Major Programs at the  
Water Development Board  
for the Fiscal Year Ended  
August 31, 2011*

## Summary of Auditor's Results

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### Financial Statements

Issued under separate cover. See State Auditor's Office report entitled *State of Texas Financial Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2011*.

### Federal Awards

Internal Control over major programs:

Material weakness(es) identified?                      Yes

Significant deficiency(ies) identified?              Yes

### Major programs with Significant Deficiencies:

CFDA Number	Name of Federal Program or Cluster
66.458	Capitalization Grants for Clean Water State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds

### Major programs with Material Weaknesses:

CFDA Number	Name of Federal Program or Cluster
66.458	Capitalization Grants for Clean Water State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds

Type of auditor's report issued on compliance for major programs: See below.

Unqualified:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
66.458	Capitalization Grants for Clean Water State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? Yes

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
66.458	Capitalization Grants for Clean Water State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds

Dollar threshold used to distinguish between type A and type B programs: \$86,555,601

Auditee qualified as low-risk auditee? No

Section 2:

## ***Financial Statement Findings***

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Issued under separate cover. See State Auditor's Office report entitled *State of Texas Financial Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2011*.

Section 3:

## Federal Award Findings and Questioned Costs

This section identifies significant deficiencies, material weaknesses, and instances of non-compliance, including questioned costs, as required to be reported by Office of Management and Budget Circular A-133, Section 510(a).

### Water Development Board

Reference No. 12-188

#### Allowable Costs/Cost Principles

**CFDA 66.458 – Capitalization Grants for Clean Water State Revolving Funds**

**CFDA 66.458 – Capitalization Grants for Clean Water State Revolving Funds - ARRA**

**Award years – October 1, 2009 to September 30, 2012 and October 1, 2008 to August 31, 2014**

**Award numbers – CS-48000210 and 2W-96692401 (ARRA)**

**Type of finding – Material Weakness and Non-Compliance**

In accordance with Title 2, Code of Federal Regulations (CFR), Part 225, Appendix B, when employees are expected to work solely on a single federal award or cost objective, charges for their salaries and wages must be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications must be prepared at least semi-annually and signed by the employee or supervisory official having firsthand knowledge of the work performed by the employees. For employees who are expected to work on multiple activities or cost objectives, a distribution of their salaries or wages must be supported by personnel activity reports or equivalent documentation that:

Questioned Cost: \$2,817

U.S. Environmental Protection Agency

- Reflect an after-the-fact distribution of the actual activity of each employee.
- Account for the total activity for which each employee is compensated.
- Are prepared at least monthly and must coincide with one or more pay periods.
- Are signed by the employee.

Budget estimates that are developed before services are performed do not qualify as support for charges to federal awards but may be used for interim purposes, provided that at least quarterly comparisons of actual costs to budgeted amounts are made and any adjustments are reflected in the amounts billed to the federal program. Costs charged to federal awards to reflect adjustments made as a result of the activity actually performed may be recorded annually if the quarterly comparisons show that the differences between budgeted and actual costs are less than 10 percent.

**For 12 (57 percent) of the 21 payroll charges tested, the Water Development Board (Board) did not base its payroll charges on actual work completed.** For certain employees expected to work on multiple activities, the Board determined payroll charges based on a predetermined level of effort estimate developed at the beginning of the fiscal year rather than an after-the-fact distribution of actual time worked. The Board allocated \$2,817 of the payroll charges tested to Capitalization Grants for Clean Water State Revolving Funds (Clean Water), non-ARRA, based on predetermined estimates.

In addition, the Board determined that \$1,124,929 charged to Clean Water (non-ARRA) and \$223,993 charged to Clean Water - ARRA was attributed to fiscal year 2011 payroll charges that were not based on an after-the-fact determination. Determining payroll charges based on factors other than an after-the-fact distribution of actual time worked could result in overcharging the federal award.

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## WATER DEVELOPMENT BOARD

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### Recommendation:

The Board should develop and implement processes to ensure that all payroll costs it charges to federal programs are allocable to the federal award and that it bases its allocation methods on an after-the-fact distribution of actual time worked.

### Management Response and Corrective Action Plan:

*TWDB concurs with the recommendation and will review the relevant charges to the Capitalization Grants for Clean Water State Revolving Funds (CWSRF) ARRA and non-ARRA programs for fiscal year (FY) 2011 and make the necessary adjustments, in accordance with OMB A-87.*

*Additionally, TWDB has significantly reduced the number of employees utilizing predetermined cost estimates to charge the CWSRF ARRA and non-ARRA. Going forward, management will review actual work effort for these employees and adjust payroll charges to federal awards in accordance with OMB A-87.*

*Implementation Date: March 2012*

*Responsible Person: Renita Bankhead*

Reference No. 12-189

### **Subrecipient Monitoring**

**CFDA 66.458 – Capitalization Grants for Clean Water State Revolving Funds**

**Award years – October 1, 2008 to September 30, 2014 and October 1, 2009 to September 30, 2012**

**Award numbers – CS-48000209 and CS-48000210**

**Type of finding – Significant Deficiency and Non-Compliance**

As a pass-through entity, the Water Development Board (Board) is required by Office of Management and Budget (OMB) Circular A-133, Section .400(d), and the OMB Circular A-133 Compliance Supplement, Part 3, Section M, to identify to the subrecipient, at the time of the subaward, federal award information, including the Catalog of Federal Domestic Assistance (CFDA) title and number, award name and number, whether the award is research and development, name of federal awarding agency, and applicable compliance requirements.

Questioned Cost: \$ 0

U.S. Environmental Protection Agency

**The Board was unable to provide evidence that it communicated the CFDA number and other required information to 1 (14 percent) of 7 subrecipients tested.** Although the Board asserted that it sent that information to the subrecipient, it could not provide a copy of that communication. Inadequate identification of federal awards could lead to improper reporting of federal funding on a subrecipient's Schedule of Expenditures of Federal Awards.

### Recommendation:

The Board should communicate required award information, including the CFDA number, to all subrecipients and maintain evidence of that communication.

### Management Response and Corrective Action Plan:

*Management concurs that while a letter was sent to the entity on October 5, 2010 it did not contain all of the required elements. On March 1, 2011, TWDB enhanced its procedures with the implementation of an Award Letter Policy for entities subject to Single Audits, and an award letter template, which includes all the requirements, for use by staff.*

**WATER DEVELOPMENT BOARD**

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*Implementation Date: March 2011*

*Responsible Person: Piper Montemayor*

Reference No. 12-190

**Allowable Costs/Cost Principles**

**CFDA 66.468 – Capitalization Grants for Drinking Water State Revolving Funds**

**CFDA 66.468 – Capitalization Grants for Drinking Water State Revolving Funds - ARRA**

**Award years – September 1, 2009 to August 31, 2014, September 1, 2010 to August 31, 2015, and February 1, 2009 to August 31, 2014**

**Award numbers – FS-99679513, FS-99679514, and 2F-96692301 (ARRA)**

**Type of finding – Material Weakness and Non-Compliance**

In accordance with Title 2, Code of Federal Regulations (CFR), Part 225, Appendix B, when employees are expected to work solely on a single federal award or cost objective, charges for their salaries and wages must be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications must be prepared at least semi-annually and signed by the employee or supervisory official having firsthand knowledge of the work performed by the employees. For employees who are expected to work on multiple activities or cost objectives, a distribution of their salaries or wages must be supported by personnel activity reports or equivalent documentation that:

Questioned Cost: \$ 30,190  
U.S. Environmental Protection Agency

- Reflect an after-the-fact distribution of the actual activity of each employee.
- Account for the total activity for which each employee is compensated.
- Are prepared at least monthly and must coincide with one or more pay periods.
- Are signed by the employee.

Budget estimates that are developed before services are performed do not qualify as support for charges to federal awards but may be used for interim purposes, provided that at least quarterly comparisons of actual costs to budgeted amounts are made and any adjustments are reflected in the amounts billed to the federal program. Costs charged to federal awards to reflect adjustments made as a result of the activity actually performed may be recorded annually if the quarterly comparisons show that the differences between budgeted and actual costs are less than 10 percent.

**For 24 (67 percent) of the 36 non-ARRA payroll charges tested and 7 (28 percent) of the 25 ARRA payroll charges tested, the Water Development Board (Board) did not base its payroll charges on actual work completed.** For certain employees expected to work on multiple activities, the Board determined payroll charges based on a predetermined level of effort estimate it developed at the beginning of the fiscal year, rather than an after-the-fact distribution of actual time worked. The Board allocated \$13,092 of the payroll charges tested to Capitalization Grants for Drinking Water State Revolving Funds (Drinking Water) and \$17,098 of the payroll charges tested to Drinking Water - ARRA. The following table identifies known questioned costs by award number.

<u>Program</u>	<u>Questioned Costs</u>	<u>Award Number</u>
CFDA 44.468 Drinking Water	\$ 738	FS-99679513
CFDA 44.468 Drinking Water	\$12,354	FS-99679514
CFDA 44.468 Drinking Water –ARRA	\$17,098	2F-96692301

The Board determined that \$763,083 charged to Drinking Water and \$263,614 charged to Drinking Water - ARRA in fiscal year 2011 was attributed to payroll charges that were not based on an after-the-fact determination.

**WATER DEVELOPMENT BOARD**

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Determining payroll charges based on factors other than an after-the-fact distribution of actual time worked could result in overcharging the federal award.

Recommendation:

The Board should develop and implement processes to ensure that all payroll costs it charges to federal programs are allocable to the federal award and that it bases its allocation methods on an after-the-fact distribution of actual time worked.

Management Response and Corrective Action Plan:

*TWDB concurs with the recommendation and will review the relevant charges to the Capitalization Grants for Drinking Water State Revolving Funds (DWSRF) ARRA and non-ARRA programs for fiscal year (FY) 2011 and make the necessary adjustments in accordance with OMB A-87.*

*Additionally, TWDB has significantly reduced the number of employees utilizing predetermined cost estimates to charge to the DWSRF ARRA and non-ARRA. Management will review actual work effort for these employees and adjust payroll charges to federal awards in accordance with OMB A-87.*

*Implementation Date: March 2012*

*Responsible Person: Renita Bankhead*

Reference No. 12-191

**Subrecipient Monitoring**

**CFDA 66.468 – Capitalization Grants for Drinking Water State Revolving Funds**  
**Award years – September 27, 2005 to September 15, 2011 and February 1, 2009 to August 31, 2014**  
**Award numbers – FS-99679509 and 2F-96692301**  
**Type of finding – Significant Deficiency and Non-Compliance**

As a pass-through entity, the Water Development Board (Board) is required by Office of Management and Budget (OMB) Circular A-133, Section .400(d), and the OMB Circular A-133 Compliance Supplement Part 3, Section M, to identify to the subrecipient, at the time of the subaward, the federal award information, including the Catalog of Federal Domestic Assistance (CFDA) title and number, award name and number, whether the award is research and development, name of federal awarding agency, and applicable compliance requirements. The Board also is required to issue a management decision on audit findings within six months after receipt of the subrecipient’s audit report and ensure that the subrecipient takes timely and appropriate corrective action on all audit findings (OMB Circular A-133, Section .400(d)).

Questioned Cost: \$ 0  U.S. Environmental Protection Agency
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Pre-award Monitoring

**The Board was unable to provide evidence that it communicated the CFDA number and other required information to 1 (20 percent) of 5 subrecipients tested.** Although the Board asserted that it sent the information to the subrecipient, it could not provide a copy of the communication. Inadequate identification of federal awards could lead to improper reporting of federal funding on a subrecipient’s Schedule of Expenditures of Federal Awards.

A-133 Single Audit Compliance Monitoring

**The Board did not issue a management decision on audit findings within 6 months after receipt of a subrecipient’s audit report for 1 (50 percent) of 2 subrecipients tested that had single audit findings.** Not meeting the six-month requirement for issuing management decisions on audit findings could result in delays in subrecipients’ development and implementation of corrective action plans and continued non-compliance.

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## WATER DEVELOPMENT BOARD

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Excluding findings from the Board's tracking tool could result in the Board delaying or not conducting follow-up on findings, delays in subrecipients' development and implementation of corrective action plans, and continued non-compliance.

Recommendations:

The Board should:

- Communicate required award information, including the CFDA number, to all subrecipients and maintain evidence of the communication.
- Issue a management decision on audit findings within six months after receipt of a subrecipient's audit report.

Management Response and Corrective Action Plan:

*Management concurs that while a letter was sent to the entity on September 22, 2009 it did not contain all of the required elements. On March 1, 2011, TWDB enhanced its procedures by implementing an Award Letter Policy for entities subject to Single Audits, and a letter template which includes all the required elements for use by staff.*

*Procedures will be updated and implemented to issue management findings within six months after receipt of the sub-recipient's audit report by March 31, 2012.*

*Implementation Date: March 2011 and March 2012*

*Responsible Person: Piper Montemayor*

## Summary Schedule of Prior Year Audit Findings

Federal regulations (OMB Circular A-133) state, “the auditee is responsible for follow-up and corrective action on all audit findings.” As part of this responsibility, the auditee reports the corrective action it has taken for the following:

- Each finding in the 2010 Schedule of Findings and Questioned Costs.
- Each finding in the 2010 Summary Schedule of Prior Audit Findings that was not identified as implemented or reissued as a current year finding.

The Summary Schedule of Prior Audit Findings (year ended August 31, 2011) has been prepared to address these responsibilities.

### Water Development Board

Reference No. 11-192

#### Reporting

**CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds - ARRA**

**Award year – February 1, 2009 to August 31, 2014**

**Award number – 2F-96692301 (ARRA)**

**Type of finding – Significant Deficiency and Non-Compliance**

Section 1512 of the American Recovery and Reinvestment Act (Recovery Act) requires that recipients submit quarterly reports to the federal government. Information required to be submitted includes (1) the amount of Recovery Act funds received; (2) the amount of Recovery Act funds received that were expended; (3) a detailed list of all projects or activities for which Recovery Act funds were expended; (4) an estimate of the number of jobs created or retained; and (5) detailed information on any subcontracts or subgrants awarded by the recipient, including the data elements required to comply with the Federal Funding Accountability and Transparency Act of 2006 (Public Law 109-282) (Recovery Act Section 1512(c)). The prime recipient of Recovery Act funds is responsible for the reporting of all data required by Recovery Act Section 1512 for its subrecipients. As the prime recipient of Recovery Act funds, the Water Development Board (Board) obtains this information from its subrecipients and submits it to the federal government.

Initial Year Written: 2010  
Status: Implemented

U.S. Environmental Protection  
Agency

**The report the Board submitted for the quarter ending June 30, 2010, for the Capitalization Grants for Drinking Water State Revolving Funds program did not include all activity in the reporting period and was not supported by the Board's accounting records.** Errors related to three subrecipients resulted in the understatement of expenditures by \$624,493, which was 2 percent of the \$29,027,062 expenditures for all subrecipients included in the report. The Board did not detect the errors because it does not have a review process prior to submitting the report.

Quarterly reports are submitted to the federal government to comply with Recovery Act Section 1512 reporting requirements and provide transparency regarding Recovery Act funds spent. When the Board submits an inaccurate report, this decreases the reliability of the information intended for the federal government and the general public.

#### Corrective Action:

Corrective action was taken.

**WATER DEVELOPMENT BOARD**

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Reference No. 11-193

**Subrecipient Monitoring**

**CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds**

**CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds - ARRA**

**Award years – September 21, 2004 to December 31, 2010, September 27, 2005 to September 15, 2011, and February 1, 2009 to August 31, 2014**

**Award numbers – FS-996795-08, FS-996795-09, and 2F-96692301 (ARRA)**

**Type of finding – Significant Deficiency and Non-Compliance**

The Water Development Board (Board) is required by Office and Management and Budget (OMB) Circular A-133, Section .400, to monitor subrecipients to ensure compliance with federal rules and regulations, as well as the provisions of the contracts or grant agreements.

Initial Year Written:	2010
Status:	Implemented
U.S. Environmental Protection Agency	

Pre-award Monitoring

Recipients of American Recovery and Reinvestment Act (Recovery Act) awards are required to ensure that the subrecipients that receive Recovery Act funds maintain active registrations in the Central Contractor Registration (CCR) and obtain a Dun and Bradstreet Data Universal Numbering System (DUNS) number (Title 2, Code of Federal Regulations, Section 176.50, and Recovery Act, Section 1512(h)). This information is needed to allow the recipient to properly monitor subrecipient expenditures of Recovery Act funds and for oversight by the federal awarding agencies, offices of inspector general, and the U.S. Government Accountability Office.

The Board must review and perform periodic checks to confirm that subrecipients receiving Recovery Act funds have current CCR registrations before and during the award period. To accomplish this, the Board requests CCR information as part of the subrecipient application process and uses a checklist to ensure that the subrecipient provided that information. **For 6 (24 percent) of 25 subrecipients tested, the subrecipient did not include CCR information on the application or the Board did not complete a checklist.** In addition, there was no evidence that the Board (1) verified CCR registrations upon the receipt of the application and prior to the first award disbursement or (2) monitored the registration throughout the year. Although the Board indicated that it made those checks, it had no procedures to document that it made those checks.

A-133 Single Audit Compliance Monitoring

According to OMB Circular A-133, the Board must ensure that each subrecipient that expends more than \$500,000 in federal funds obtain an OMB Circular A-133 Single Audit and provide a copy of the audit report to the Board within 9 months of the end of the subrecipient’s fiscal year (OMB Circular A-133, Sections 320 and 400). In addition, the Board must issue a management decision on audit findings within six months after receipt of a subrecipient’s audit report (OMB Circular A-133, Section 400). In cases of continued inability or unwillingness of a subrecipient to obtain the required audits, the Board must take appropriate action using sanctions (OMB Circular A-133 Sections 225).

**For 2 (12 percent) of 17 subrecipients originally tested, the Board did not ensure that the subrecipient either obtained a Single Audit or provided a certification that it was exempt from Single Audit requirements.** Further analysis of the subrecipient population identified one more subrecipient that did not obtain a Single Audit or provide a certification that it was exempt. The Board provided documentation indicating that it made some effort to collect that information. **In addition, the Board did not ensure that 9 (8 percent) of 109 subrecipients submitted audit reports within nine months of the end of their fiscal year.**

These issues increase the risk that the Board will not be aware of instances in which subrecipients fail to comply with federal requirements and increase the potential of program funds not being spent as intended.

Corrective Action:

Corrective action was taken.

# Appendix

## Objectives, Scope, and Methodology

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### Objectives

With respect to the Capitalization Grants for Clean Water State Revolving Funds Program (Clean Water Program) and the Capitalization Grants for Drinking Water State Revolving Funds Program (Drinking Water Program), the objectives of this audit were to (1) obtain an understanding of internal controls, assess control risk, and perform tests of controls unless the controls were deemed to be ineffective and (2) provide an opinion on whether the State complied with the provisions of laws, regulations, and contracts or grants that have a direct and material effect on the Clean Water Program and the Drinking Water Program.

### Scope

The audit scope covered federal funds that the State spent for the Clean Water Program and for the Drinking Water Program from September 1, 2010, through August 31, 2011. The audit work included control and compliance work at the Water Development Board (Board).

### Methodology

The audit methodology included developing an understanding of controls over each compliance area that was material to the Clean Water Program and the Drinking Water Program. Auditors conducted tests of compliance and of the controls identified for each compliance area and performed analytical procedures when appropriate. Auditors assessed the reliability of data the Board provided and determined that the data provided was reliable for the purposes of expressing an opinion on compliance with the provisions of laws, regulations, and contracts or grants that have a direct and material effect on the programs identified above.

Information collected and reviewed included the following:

- Board expenditure, procurement, reporting, cash revenue, required matching, program income, and subrecipient data.
- Federal notices of award and award proposals.
- Transactional support related to expenditures, procurement, and revenues.
- Board-generated reports and data used to support reports, revenues, and other compliance areas.

- Information system support for Board assertions related to general controls over information systems that support the control structure related to federal compliance.

Procedures and tests conducted included the following:

- Analytical procedures performed on expenditure data to identify instances of non-compliance.
- Compliance testing for samples of transactions for each direct and material compliance area.
- Tests of design and effectiveness of key controls and tests of design of controls to assess the sufficiency of the Board's control structure.
- Tests of design and effectiveness of general controls over information systems that support the control structure related to federal compliance.

Criteria used included the following:

- The Code of Federal Regulations.
- Office of Management and Budget Circulars A-87, A-102, and A-133.
- The American Recovery and Reinvestment Act.
- Federal notices of award and award proposals.
- Board policies and procedures.

## **Project Information**

Audit fieldwork was conducted from August 2011 through December 2011. Except as discussed above in the Independent Auditor's Report, we conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

The following members of the State Auditor's staff performed the audit:

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- Pamela A. Bradley, CPA (Assistant Project Manager)
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- Lilia Christine Srubar, CPA (Assistant Project Manager)
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- Rebecca Franklin, CFE, CGAP, CISA (Prior Year Finding Coordinator)
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The Honorable Harvey Hilderbran, House Ways and Means Committee

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The Honorable Rick Perry, Governor

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Members of the Water Development Board

Mr. Edward G. Vaughan, Chairman  
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