



John Keel, CPA
State Auditor

A Report on

**State of Texas Compliance with
Federal Requirements for the
Highway Planning and
Construction Cluster of Federal
Programs and the Airport
Improvement Program
for the Fiscal Year Ended
August 31, 2010**

February 2011
Report No. 11-025



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Overall Conclusion

With the exception of certain non-compliance detailed in this report, the State of Texas complied in all material respects with the federal requirements for the Highway Planning and Construction cluster of federal programs in fiscal year 2010.

The State of Texas also complied in all material respects with the federal requirements for the Airport Improvement Program in fiscal year 2010.

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 audits. Those audits test compliance with federal requirements in 14 areas, such as allowable costs, procurement, reporting, and monitoring of non-state entities when the State passes federal funds through to those entities (subrecipients). Additionally, each program may outline special tests specific to the program that auditors are required to perform. The Single Audit for the State of Texas included (1) all high-risk federal programs for which the State expended more than \$85,612,909 in federal funds during fiscal year 2010 and (2) other selected federal programs.

From September 1, 2009, through August 31, 2010, the State of Texas expended \$56.9 billion in federal funds for federal programs and clusters of programs. The State Auditor's Office audited compliance with requirements for the Highway Planning and Construction cluster of federal programs and the Airport Improvement Program at the Department of Transportation (Department), which spent \$2,435,940,254 in federal Highway Planning and Construction cluster funds

The Highway Planning and Construction Cluster of Federal Programs

The Highway Planning and Construction cluster of federal programs, which are administered by the Federal Highway Administration, provides funds to assist state transportation agencies in the planning, design, development, improvement, and replacement of public roads and bridges, including the National Highway System.

The Airport Improvement Program

The Airport Improvement Program, which is administered by the Federal Aviation Administration, provides funds to assist sponsors of public-use airports in the development of a nationwide system of airports to meet the needs of civil aeronautics.

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

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

and \$79,363,405 in federal Airport Improvement Program funds during fiscal year 2010.

Auditors identified eight findings, including two material weaknesses with material non-compliance. Both of the material findings were related to the Highway Planning and Construction cluster of federal programs (see text box for definitions of finding classifications).

Key Points

The Department had material weaknesses in two areas auditors tested for the Highway Planning and Construction cluster of federal programs.

The Department did not communicate required award information to all subrecipients tested, and it did not always monitor its subrecipients to ensure they complied with federal requirements related to (1) the Davis-Bacon Act and (2) materials and workmanship specifications as outlined in the Department's quality assurance program.

While the Department has an approved quality assurance program, it did not ensure that it tested all materials as that program requires. The automated application the Department uses to administer its quality assurance program, SiteManager, does not prevent the same individual from both conducting and reviewing sample tests; SiteManager also has other control weaknesses.

The Department complied in all material respects with requirements for the remaining areas auditors tested for the Highway Planning and Construction cluster of federal programs. However, for three of the remaining areas tested, certain compliance and control weaknesses existed.

The Department did not always comply with the Davis-Bacon Act and reporting requirements. Specifically:

- The Department did not always ensure that its contractors submitted required payroll certifications in fiscal year 2010. Those certifications are evidence that the contractors paid their employees in compliance with federal requirements. The Department does not have a standardized process for tracking the certified payrolls that contractors submit.
- The Department has a significant backlog in the project completion (PR-20) reports that it must submit to the Federal Highway Administration. The

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 with the compliance area.
- 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.

Department also incorrectly reported expenditures to the federal government for two projects funded by the American Recovery and Reinvestment Act (Recovery Act).

Auditors also identified weaknesses in segregations of duties for the Department's Federal Project Authorization and Agreement system. Specifically, programmers had access to move system code into the production environment for that system.

The Department complied with all requirements for most areas tested for the Airport Improvement Program. However, auditors identified three areas with some instances of non-compliance.

The Department did not always comply with procurement, suspension and debarment; reporting; and revenue diversion requirements. Specifically, the Department:

- Did not always verify that its vendors or contractors were not suspended or debarred from federal procurements as required by federal regulations.
- Could not provide support for one financial report it submitted to the Federal Aviation Administration (FAA). On reports it submitted to the federal government, the Department also incorrectly listed certain airports as subrecipients of Recovery Act funds when the Department actually had made direct expenditures of funds for the benefit of those airports.
- Did not consistently monitor its airport sponsors in accordance with its FAA-approved policy to detect revenue diversion.

Auditors followed up on 13 findings from the prior fiscal year for the Highway Planning and Construction cluster of federal programs, the Airport Improvement Program, the Formula Grants for Other Than Urbanized Areas program, and the Highway Safety cluster of federal programs.

- The Department fully implemented recommendations for three findings.
- The Department partially implemented recommendations for four findings.
- The State Auditor's Office reissued six findings from prior fiscal years for the Highway Planning and Construction Cluster of federal programs and the Airport Improvement Program as fiscal year 2010 findings in this report.

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 Highway Planning and Construction cluster of federal programs and the Airport Improvement Program at the Department. As discussed above, auditors identified issues involving segregation of duties and other control weaknesses related to information technology systems.

Summary of Objectives, Scope, and Methodology

With respect to the Highway Planning and Construction cluster of federal programs and the Airport Improvement 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 major programs audited.

The audit scope covered federal funds the State spent for the Highway Planning and Construction cluster of federal programs and for the Airport Improvement Program from September 1, 2009, through August 31, 2010. Audit work included control and compliance work at the Department.

The audit methodology included developing an understanding of controls over each compliance area that was material to the program or cluster audited. Auditors conducted tests of compliance and of the controls identified for each compliance area and performed analytical procedures when appropriate.

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Independent Auditor's Report

*State of Texas Compliance with
Federal Requirements for the Highway
Planning and Construction Cluster of
Federal Programs and the Airport
Improvement Program for the
Fiscal Year Ended
August 31, 2010*

Report on Compliance with Requirements that Could Have a Direct and Material Effect on the Highway Planning and Construction Cluster and the Airport Improvement Program and on Internal Control Over Compliance in Accordance with U.S. Office of Management and Budget Circular A-133

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 Highway Planning and Construction Cluster and the Airport Improvement Program for the year ended August 31, 2010. Compliance with the requirements of laws, regulations, contracts, and grants applicable to the Highway Planning and Construction Cluster and the Airport Improvement 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 Highway Planning and Construction Cluster and the Airport Improvement 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 A-133 Audit for the year ended August 31, 2010. As such, the Highway Planning and Construction Cluster and the Airport Improvement Program were selected as major programs based on the State of Texas as a whole for the year ended August 31, 2010. 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 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.

As identified below and in the accompanying Schedule of Findings and Questioned Costs, the State did not comply with certain compliance requirements that are applicable to the Highway Planning and Construction Cluster. Compliance with such requirements is necessary, in our opinion, for the State to comply with requirements applicable to that program.

Agency	Cluster or Program	Compliance Requirement	Finding Number
Department of Transportation	Highway Planning and Construction Cluster	Procurement and Suspension and Debarment	11-144
	Highway Planning and Construction Cluster - ARRA	Subrecipient Monitoring Special Tests and Provisions - R3 - Subrecipient Monitoring	
Department of Transportation	Highway Planning and Construction Cluster	Special Tests and Provisions - Quality Assurance	11-146

In our opinion, except for the noncompliance described above, the State complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on the Highway Planning and Construction Cluster and the Airport Improvement Program for the year ended August 31, 2010. However, the results of our auditing procedures also disclosed other 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
Department of Transportation	Highway Planning and Construction Cluster	Davis-Bacon Act	11-142

Agency	Cluster or Program	Compliance Requirement	Finding Number
Department of Transportation	Highway Planning and Construction Cluster Highway Planning and Construction Cluster - ARRA	Reporting	11-145
Department of Transportation	CFDA 20.106 - Airport Improvement Program	Procurement and Suspension and Debarment	11-147
Department of Transportation	CFDA 20.106 - Airport Improvement Program CFDA 20.106 - Airport Improvement Program - ARRA	Reporting	11-148
Department of Transportation	CFDA 20.106 - Airport Improvement Program	Special Tests and Provisions - Revenue Diversion	11-149

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 Highway Planning and Construction Cluster and the Airport Improvement 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 Highway Planning and Construction Cluster and the Airport Improvement 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
Department of Transportation	Highway Planning and Construction Cluster Highway Planning and Construction Cluster - ARRA	Procurement and Suspension and Debarment Subrecipient Monitoring Special Tests and Provisions - R3 - Subrecipient Monitoring	11-144
Department of Transportation	Highway Planning and Construction Cluster	Special Tests and Provisions - Quality Assurance	11-146

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
Department of Transportation	Highway Planning and Construction Cluster	Davis-Bacon Act	11-142
Department of Transportation	Highway Planning and Construction Cluster	Period of Availability of Federal Funds	11-143
Department of Transportation	Highway Planning and Construction Cluster Highway Planning and Construction Cluster - ARRA	Reporting	11-145
Department of Transportation	CFDA 20.106 - Airport Improvement Program	Procurement and Suspension and Debarment	11-147
Department of Transportation	CFDA 20.106 - Airport Improvement Program CFDA 20.106 - Airport Improvement Program - ARRA	Reporting	11-148
Department of Transportation	CFDA 20.106 - Airport Improvement Program	Special Tests and Provisions - Revenue Diversion	11-149

Schedule of Program Expenditures

The accompanying Schedule of Program Expenditures for the Highway Planning and Construction Cluster and the Airport Improvement Program (Schedule) of the State for the year ended August 31, 2010, 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, 2010.

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 18, 2011

**Schedule of Program Expenditures for the
Highway Planning and Construction Cluster and the
Airport Improvement Program
for the State of Texas
For the Year Ended August 31, 2010**

Schedule of Program Expenditures Highway Planning and Construction Cluster			
Agency	Pass-through to Non-state Entities	Direct Expenditures	Total
Department of Transportation			
Other Than American Recovery and Reinvestment Act	\$121,091,078	\$1,478,503,507	\$1,599,594,585
American Recovery and Reinvestment Act	21,920,542	814,425,127	836,345,669
Total Audited Highway Planning and Construction Cluster	\$143,011,620	\$2,292,928,634	\$2,435,940,254
Note: Federal expenditures for the Highway Planning and Construction cluster of federal programs at state entities not included in the scope of this audit totaled \$6,172,702 for the year ended August 31, 2010.			

Schedule of Program Expenditures Airport Improvement Program			
Agency	Pass-through to Non-state Entities	Direct Expenditures	Total
Department of Transportation			
Other Than American Recovery and Reinvestment Act	\$577,594	\$69,985,014	\$70,562,608
American Recovery and Reinvestment Act	0	8,800,797	8,800,797
Total Audited Airport Improvement Program	\$577,594	\$78,785,811	\$79,363,405
Note: Federal expenditures for the Airport Improvement Program at state entities not included in the scope of this audit totaled \$3,400,507 for the year ended August 31, 2010.			

Schedule of Findings and Questioned Costs

*State of Texas Compliance with Federal
Requirements for the Highway Planning and
Construction Cluster of Federal Programs and the
Airport Improvement Program for the Fiscal Year
Ended August 31, 2010*

Summary of Auditors' Results

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, 2010*.

Federal Awards

Internal Control over major programs:

Material weakness(es) identified?	Yes
Significant deficiency(ies) identified?	Yes

Major programs with Significant Deficiencies:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
Cluster	Highway Planning and Construction (with ARRA)
20.106	Airport Improvement Program (with ARRA)

Major programs with Material Weaknesses:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
Cluster	Highway Planning and Construction (with ARRA)

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

Qualified:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
Cluster	Highway Planning and Construction (with ARRA)

Unqualified:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
20.106	Airport Improvement Program (with ARRA)

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>
Cluster	Highway Planning and Construction (with ARRA)
20.106	Airport Improvement Program (with ARRA)

Dollar threshold used to distinguish between type A and type B programs: \$85,612,909

Auditee qualified as low-risk auditee? No

Section 2:

Financial Statement Findings

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, 2010*.

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).

Department of Transportation

Reference No. 11-142

Davis-Bacon Act

(Prior Audit Issue 10-82)

Highway Planning and Construction Cluster

Award years – Multiple

Award numbers – Federal project HP 2008(045), STP 2009(699)ES, STP 2006(572)MM, and STP 2006(438)MM

Type of finding - Significant Deficiency and Non-Compliance

When required by the Davis-Bacon Act, the U.S. Department of Labor's (DOL) government-wide implementation of the Davis-Bacon Act, or by federal program legislation, all laborers and mechanics employed by contractors or subcontractors to work on construction contracts in excess of \$2,000 financed by federal assistance funds must be paid wages not less than those established for the locality of the project (prevailing wage rates) by the DOL (Title 40, United States Code (USC), Sections 3141-3144, 3146, and 3147 (formerly Title 40, USC, Sections 276a to 276a-7)).

Questioned Cost: \$ 0

U.S. Department of
Transportation – Federal
Highway Administration

Non-federal entities shall include in construction contracts that are subject to the Davis-Bacon Act a requirement that the contractor or subcontractor comply with the requirements of the Davis-Bacon Act and the DOL regulations (Title 29, Code of Federal Regulations (CFR), Sections 5.5-5.6). In addition, contractors or subcontractors are required to submit to the non-federal entity weekly, for each week in which any contract work is performed, a copy of the payroll and a statement of compliance (certified payrolls) (Title 29, CFR, Sections 3.3-3.4). This reporting is often done using optional form WH-347, which includes the required statement of compliance (Office of Management and Budget No. 1215-0149).

The Department of Transportation (Department) was not always able to provide documentation showing that it collected certified payrolls from its contractors. **For 4 (8 percent) of 50 projects tested, the contractors did not always submit payroll certifications for fiscal year 2010.** The total value of those four projects, including payroll and non-payroll costs, was \$7,471,792.

For three of the four projects discussed above, the contractors were supposed to submit certified payrolls using the Department's automated system, the Electronic Project Records System (EPRS). The Department can use EPRS to identify any unreported payroll certifications, but personnel in the Department's district offices did not consistently monitor EPRS information. For the fourth project discussed above, the contractor was required to submit certified payrolls through a manual process. According to management at a Department district office, a new district staff person became responsible for monitoring payroll certification submittals and determined that this contractor had not submitted payroll certifications for six months. The contractor subsequently submitted payroll certifications for all six months on one certification.

The Department does not have a standardized process for tracking certified payrolls that contractors submit. Each area office within each district office determines its own method for ensuring that contractors submit payroll certifications. As of December 8, 2010, the Department's 25 district offices had a total of 101 area offices.

When contractors do not consistently submit required payroll certifications, the Department cannot ensure that contractor and subcontractor employees are properly classified and being paid the appropriate wage rate in accordance with the Davis-Bacon Act.

In addition, the insufficient wage report that the Department can generate from EPRS does not identify contractor timesheets that report more than eight hours of “regular time” pay per day. By not including that information in the report, the Department could be unaware of instances in which contractors are not paying employees overtime rates based on the prevailing wages for that area.

Recommendations:

The Department should:

- Establish a consistent, statewide process to ensure that it collects and tracks payroll certifications from each contractor, whether manually or through EPRS, as required by the Davis-Bacon Act.
- Modify the existing insufficient wage paid report that EPRS generates to identify and report instances in which a contractor is not paying correct prevailing wage rates for employees' overtime hours.

Management Response and Corrective Action Plan:

The department concurs with the recommendations. The department will assemble a work group of division, district, and area office staff to develop a plan for an effective system for tracking of payrolls. Possible options may include manual systems or electronic.

The issue is that EPRS does not flag more than 8 hours per day. Working more than 8 hours a day does not necessarily constitute overtime as overtime is computed based on a 40 hour work week, not an 8 hour day. EPRS does flag a discrepancy for more than 40 hours per week on an individual project. The department uses the certification statement provided by the US Department of Labor (DOL). It will be determined if levels beyond that required by the DOL are warranted.

Implementation Date: December 2011

Responsible Person: Russel Lenz

Reference No. 11-143

Period of Availability of Federal Funds

(Prior Audit Issue 10-81)

Highway Planning and Construction Cluster

Award years – Multiple

Award numbers – Multiple

Type of finding – Significant Deficiency

Agencies shall maintain internal control over federal programs that provides reasonable assurance that agencies are managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements (Office of Management and Budget Circular A-133, Subpart C, Section 300 (b)).

Questioned Cost: \$ 0

U.S. Department of
Transportation – Federal
Highway Administration

The Department of Transportation (Department) uses the Federal Project

Authorization and Agreement (FPAA) system to process and track project approvals from the Federal Highway Administration. The FPAA system details when federal funds are authorized, which is the starting point for the period of availability of federal funds. The Department must obtain approval from the Federal Highway Administration prior to starting construction work on a project and expending federal funds (Title 23, Code of Federal Regulations, Section 630.106).

The Department did not appropriately restrict access to the FPAA system. Specifically, two programmers had access to move code into the production environment of FPAA. In general, programmers should not have access to migrate code changes to the production environment. Allowing programmers inappropriate access increases the risk of unauthorized changes and does not allow for adequate segregation of duties.

The Department's Finance Division manages the FPAA system, and that division does not enforce the same change management processes that the Department enforces for enterprise-wide systems. The Department asserted that there were no changes made to the FPAA system in fiscal year 2010.

Recommendation:

The Department should establish and enforce change management procedures for systems the Finance Division manages, including eliminating programmers' access to migrate code changes to the production environment and maintaining adequate documentation of changes made to systems.

Management Response and Corrective Action Plan:

The Department will continue to evaluate and improve controls over change management of the FPAA system. Currently the Department has assigned one individual the responsibility for the development of code changes to FPAA and two separate individuals the responsibility for change deployment. The Department also requires program personnel to submit a programming request form for all change requests to the FPAA system. This programming request form documents all information related to program changes including the programmer responsible for testing code changes and the individual responsible for moving code into production.

The Department is also in the process of implementing business process improvements to the FPAA system including utilizing a different platform to house the FPAA system. This platform change should enhance change management processes including improved access security. The Department plans to evaluate having the Technology Services Division host the FPAA system on the Department's enterprise server. This would allow the Finance Division to continue operating the FPAA system, and TSD the responsibility to move code into production. Any evaluation of controls performed will consider the cost of controls versus assessed risk for reasonableness and cost effectiveness.

Implementation Date: May 2010

Responsible Person: Mark Pollard

Reference No. 11-144

**Procurement and Suspension and Debarment
Subrecipient Monitoring
Special Tests and Provisions – R3 – Subrecipient Monitoring**
(Prior Audit Issues 10-84 and 09-80)

**Highway Planning and Construction Cluster
Highway Planning and Construction Cluster - ARRA
Award years – Multiple
Award numbers – Multiple
Type of finding – Material Weakness and Material Non-Compliance**

The Department of Transportation (Department) is required by Office of 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. In addition, the Department has the responsibility for the construction of all federal aid projects, and it is not relieved of such responsibility by authorizing performance of the work by a local public agency or other federal agency. State transportation departments are responsible for ensuring that such projects receive adequate supervision and inspection to insure that projects are completed in conformance with approved plans and specifications (Title 23, Code of Federal Regulations, Section 635.105(a)).

<p>Questioned Cost: \$ 0</p> <p>U.S. Department of Transportation – Federal Highway Administration</p>
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Pre-award Monitoring

At the time of the award, pass-through entities must identify to subrecipients the applicable compliance requirements and the federal award information, including the Catalog of Federal Domestic Assistance (CFDA) title and number, the federal award name and number, the name of the federal awarding agency, and whether the award is research and development (OMB Circular A-133 Compliance Supplement, Part 3, Section M).

Additionally, federal rules require that, when a non-federal entity enters into a covered transaction with an entity at a lower tier, the non-federal entity must verify that the entity is not suspended or debarred or otherwise excluded from federal contracts. This verification may be accomplished by checking the Excluded Parties List System (EPLS), collecting a certification from the entity, or adding a clause or condition to the covered transaction with that entity (Title 2, Code of Federal Regulations, Section 180.300). Covered transactions include all nonprocurement transactions (that is, subawards to subrecipients) irrespective of award amount (Title 2, Code of Federal Regulations, Sections 180.220 and 180.970).

Auditors tested 41 agreements executed between 1998 and 2010 and identified exceptions in all of the agreements tested. Specifically:

- For 38 (93 percent) of 41 subrecipient agreements tested, the Department did not properly identify federal award information to the subrecipient.
- For 32 (78 percent) of 41 subrecipient agreements tested, the Department did not require the subrecipient to certify that it was not suspended or debarred.
- For 2 (5 percent) of 41 subrecipient agreements tested, the Department did not notify the subrecipient of the requirement that invoices or requests for funds must be for expenses already incurred.
- For 4 (10 percent) of 41 subrecipient agreements tested, the Department did not notify the subrecipient of Single Audit requirements.

- For 5 (12 percent) out of 41 subrecipient agreements tested, the Department did not include an approved budget that listed allowed activities and costs.
- For 1 (2 percent) of 41 subrecipient agreements tested, the Department did not notify the subrecipient of OMB A-87 cost principles.
- For 1 (25 percent) of 4 subrecipient agreements signed after September 2009, the Department did not ensure that at least one of the subrecipient's staff had attended training on the local government project procedures required as part of its funding agreement, which the Department implemented to ensure that subrecipients are aware of project and grant requirements.

The Department did not properly identify federal award information and compliance requirements to the subrecipient consistently. While the Department uses a standard template for award agreements with subrecipients, the template did not consistently include identification of the federal award title and number or the CFDA title and number. The template also did not consistently identify the name of the federal awarding agency or compliance requirements. The template does, however, refer to the master advanced funding template agreement, which requires the subrecipient to comply with federal compliance requirements and provides other specific information regarding allowable costs and other requirements.

The template the Department used requires the subrecipient to refrain from doing business with other entities that are suspended or debarred; however, it does not require the subrecipient to certify that it is not suspended or debarred. Award templates dated after September 23, 2009, contained language that required the subrecipient to certify that it was not suspended or debarred.

Inadequate identification of federal awards by the Department may lead to improper reporting of federal funding on a subrecipient's Schedule of Expenditures of Federal Awards (SEFA). Additionally, when the Department does not verify that subrecipients are not suspended or debarred, this increases the risk that the Department will enter into an agreement with an entity that is not eligible to receive federal funding. Incomplete communication of federal compliance requirements in the Department's award documents increases the risk that subrecipients will not follow federal guidelines related to administering subrecipient awards.

Subrecipients of Recovery Act Funding

The American Recovery and Reinvestment Act (Recovery Act) of 2009 required recipients to (1) maintain records that identify adequately the source and application of Recovery Act funds; (2) separately identify to each subrecipient, and document at the time of subaward and at the time of disbursement of funds, the federal award number, the CFDA number, and the amount of Recovery Act funds; and (3) require their subrecipients to include on their SEFA information to specifically identify Recovery Act funding (Title 2, Code of Federal Regulations, Section 176.210).

Recipients of Recovery Act awards are also 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 Department did not consistently comply with Recovery Act requirements with respect to its subrecipients. Specifically, for seven Recovery Act subrecipient awards tested:

- 5 (71 percent) did not contain evidence that the Department verified that subrecipients had obtained a DUNS number or were registered with CCR prior to award.

- 6 (86 percent) did not contain evidence that the Department, at the time of the award, notified the subrecipients of the requirement to include appropriate identification of Recovery Act funds in their SEFAs.
- 1 (14 percent) did not contain evidence that the Department ensured that the budget proposed to the subrecipient separately identified Recovery Act funds.
- 5 (71 percent) did not contain evidence that the Department separately identified to each subrecipient, and documented at the time of disbursement of funds, the Federal award number, CFDA number, and the amount of Recovery Act funds.

While the Department uses a standard template for award agreements with subrecipients, that template does not include identification of the federal award title and number, CFDA title and number, or name of the federal awarding agency. Additionally, at the time of testing, the Department did not have a process to ensure that subrecipients were registered with CCR and had obtained a DUNS number, or to notify subrecipients of required Recovery Act award notifications at time of disbursement of funds.

Inadequate identification of Recovery Act awards by the Department may lead to improper reporting of federal funding on a subrecipient's SEFA. During fiscal year 2010 the Department passed-through \$21,920,542 in Recovery Act funds to subrecipients.

During-the-award Monitoring

The Department does not have standardized processes to ensure adequate during-the-award monitoring of subrecipients by its district offices. As a result, there are different levels and types of monitoring across the district offices.

District offices provided documentation of their during-the-award monitoring for 47 subrecipients tested. This documentation included reviews of invoices for allowability, period of availability, and reporting. However, auditors identified the following issues at the district offices:

- For 7 (27 percent) of 26 subrecipients tested for which Davis-Bacon Act requirements applied, the Department was unable to provide evidence that it monitored the subrecipients' compliance with Davis-Bacon Act requirements.
- For 2 (7 percent) of 27 subrecipients tested for which quality assurance requirements applied, the Department was unable to provide evidence that it monitored the subrecipients' compliance with quality assurance requirements.

Although the Department provides monitoring guidelines to district and regional offices for the monitoring of subrecipients through its *Local Government Project Procedures Manual*, implementation of the guidelines and processes for monitoring are determined by the region and district level staff. In addition, the Department does not have a standard process for reviewing each district office's procedures and activities related to subrecipient monitoring.

By not providing direct oversight or review of monitoring procedures and activities used in each district office or region, the Department is not able to ensure that sufficient monitoring occurs at the statewide level. This also increases the risk that the Department would not detect non-compliance by subrecipients administering federally funded projects.

Recommendations:

The Department should:

- Ensure existing award documentation and award documentation templates with subrecipients include all required award notification and information according to federal requirements including CFDA title and number, federal award name and number, whether the award is research and development, name of the federal awarding agency, and applicable compliance requirements.
- Develop and implement a process to, at the time of award, notify its subrecipients of the requirement to provide appropriate identification of Recovery Act funds in their SEFAs.
- Develop and implement a process to, at time of award, verify that all subrecipients that receive Recovery Act funding are registered with the CCR and have obtained a DUNS number.
- Develop and implement a process to separately identify to each subrecipient, and document at the time of disbursement of funds, the federal award number, CFDA number, and amount of Recovery Act funds.
- Develop and implement a standardized process for conducting during-the-award monitoring of subrecipients statewide.
- Develop and implement a statewide, standardized process for reviewing district offices to ensure that they are properly monitoring subrecipient compliance with federal requirements, including compliance with Davis-Bacon Act and quality assurance requirements.

Management Response and Corrective Action Plan:

Current templates contain the CFDA title and number, the name of the federal awarding agency, and applicable compliance requirements. Additional steps will be implemented to ensure that the most current version of each template is always used.

We will revise all existing templates to ensure that they include an explicit statement of whether the award is research and development. At the time a contract is entered, no federal award name and number has been assigned. Therefore, we will also include language providing that a copy of the Federal Project Authorization and Agreement documentation will be provided to the subrecipient when it is approved by the Federal Highway Administration. This documentation will ensure that the subrecipient is informed of the federal award name and number as soon as it is reasonably available.

At this time it is not anticipated that additional Recovery Act funds will be awarded.

We will revise all existing templates to require that subrecipients are registered with the CCR and have obtained a DUNS number.

We will attempt to identify all existing subrecipients and to notify them by letter of necessary federal requirements.

Implementation Date: December 2011

Responsible Person: Janice Mullinex

We have fully implemented a process to separately identify and document to each ARRA subrecipient, at the time of disbursement of funds, the federal award number, CFDA number, and amount of Recovery Act funds. An automated e-mail is sent to ARRA subrecipients upon disbursement of funds.

Implementation Date: October 2010

Responsible Person: Russel Lenz

Monitoring of subrecipient projects occurs throughout the department. The department will explore options to standardize and improve monitoring of subrecipients using a department wide approach.

Implementation Date: Unknown

Responsible Person: Steve Simmons

Reference No. 11-145

Reporting

(Prior Audit Issue 10-83)

Highway Planning and Construction Cluster

Highway Planning and Construction Cluster - ARRA

Award years – Multiple

Award numbers – Multiple – ARRA 2010(669) and ARRA 2010(578)

Type of finding – Significant Deficiency and Non-Compliance

Recovery Act Section 1512 Reports

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)).

Questioned Cost: \$ 0

U.S. Department of
Transportation - Federal
Highway Administration

Two (4 percent) of 51 Recovery Act Section 1512 reports tested at the Department of Transportation (Department) were not supported by applicable accounting records. For these reports, Department staff incorrectly transposed two Department project numbers with two federal project numbers in the database it uses to create the reports. As a result, the Department underreported the amount of Recovery Act funds spent by \$29,994.

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 Department submits an inaccurate report, this decreases the reliability of the information intended for the federal government and the general public.

PR-20 Reports

Office of Management and Budget (OMB) Circular A-133 Compliance Supplement requires the Department to submit a PR-20, Voucher for Work Under Provisions of the Federal-Aid and Federal Highway Acts, as Amended (OMB No. 2125-0507). The PR-20 is required to report the total expenditures for a project that received federal aid from the Federal Highway Administration (FHWA). The report should be completed and submitted promptly after the close-out of a project.

The Department has a significant backlog of PR-20 reports it must submit to the FHWA. Auditors identified this issue in the prior audit period, and the Department implemented a corrective action plan to reduce the backlog

of reports. In fiscal year 2010, the Department submitted 1,455 PR-20 reports, a significant increase from the 600 PR-20 reports it submitted in fiscal year 2009. However, as of August 31, 2010, the Department had not submitted PR-20 reports for 1,147 projects that had been closed for more than 90 days. The projects for which the Department must still submit PR-20 reports date back to September 1992. The FHWA relies on the Department to submit PR-20 reports to close out funding and records on funded projects. Auditors tested a sample of 25 PR-20 reports the Department submitted during the year and did not identify any compliance errors.

Recommendations:

The Department should:

- Develop and implement procedures to ensure the accuracy and completeness of data it enters into the database it uses to create Recovery Act Section 1512 reports.
- Continue to follow its corrective action plan for reducing the backlog of PR-20 reports it must submit to FHWA.

Management Response and Corrective Action Plan:

In this instance, two federal-aid project numbers were transposed between two department control-section-job (CSJ) numbers. This error occurred on a 1511 certification so it was carried forward until it had been corrected. Controls were in place to prevent over-reporting of expenditures, but this type of error had not been envisioned. System control will be modified to notify staff of this type of discrepancy.

Implementation Date: April 2011

Responsible Person: Russel Lenz

The Department will continue to follow its corrective action plan for reducing the backlog of PR-20 reports it must submit to FHWA.

Implementation Date: Currently implemented.

Responsible Person: Brian Ragland

Reference No. 11-146

Special Tests and Provisions – Quality Assurance

(Prior Audit Issues 10-87)

Highway Planning and Construction Cluster

Award years – Multiple

Award numbers – Multiple

Type of finding – Material Weakness and Material Non-Compliance

Control Weaknesses in SiteManager

Agencies shall maintain internal control over federal programs that provides reasonable assurance that the institutions are managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements (Office of Management and Budget Circular A-133, Subpart C, Section 300 (b)).

Questioned Cost: \$ 0

U.S. Department of
Transportation – Federal
Highway Administration

The Department of Transportation (Department) uses SiteManager as its system of record for quality assurance testing on its highway construction projects. However, **SiteManager does not have sufficient controls to ensure that (1) only certified testers are able to enter and sign off on test records and (2) a tester does not also sign off as the reviewer.**

For 39 (23 percent) of 171 quality assurance samples tested, the tester and reviewer were the same individual. Department staff assert that, due to staff sizes and resource requirements, the Department is unable to ensure that each test is performed and signed off on by separate individuals. Not segregating these duties or allowing uncertified testers to complete test records may result in insufficient quality assurance testing or deficiencies in projects that cost the Department time and money to correct.

Additionally, **Department staff can turn off the “sample deficiency indicator” in SiteManager without documenting a justification in SiteManager.** Staff had turned off this indicator for 3 (8 percent) of 40 projects tested. The Department provided auditors with justification for turning off the indicator for these three projects, but this information was not included in SiteManager and Department management was not monitoring this information. The indicator tracks deficiencies in quality assurance testing and notifies project management each time an estimate is created in SiteManager when sample testing deficiencies exist. The indicator also prevents final payment to contractors if there are any testing deficiencies outstanding on a project. When the indicator is turned off for a project, SiteManager no longer tracks deficiencies in sample testing for that project.

Quality Assurance Program

Title 23, Code of Federal Regulations (CFR), Chapter 205, requires that each state transportation department “shall develop a quality assurance program which will assure that the materials and workmanship incorporated into each federal-aid highway construction project on the [National Highway System] NHS are in conformity with the requirements of the approved plans and specifications, including approved changes. The program must meet the criteria in Title 23, CFR 637, Chapter 207, and be approved by the [Federal Highway Administration] FHWA.” Additionally, Title 23, CFR 637, Chapter 209, requires that only qualified personnel conduct sampling and testing to be used in the acceptance decision.

The Department did not always comply with the quality assurance program approved by the FHWA. Specifically:

- **Quality assurance tests for 1 (3 percent) of 40 projects tested did not comply with the requirements for each type of material as specified in the Department’s *Guide Schedule for Sampling and Testing*.** This quality assurance test included a blank test documented in SiteManager and a project in SiteManager for which the required test could not be found.

- **Quality assurance tests for 6 (15 percent) of 40 projects tested were conducted by an individual who was not a certified tester.**

Additionally, **documentation for 15 (9 percent) of 171 quality assurance samples tested was not located in SiteManager.** The Department's district offices rely on SiteManager to document the results of material sampling and testing. However, district offices did not consistently retain documentation of the testing information after entering data into SiteManager. District offices still use manual methods, in conjunction with SiteManager, to document quality assurance testing, and sometimes the manually documented tests are not entered into SiteManager. Not documenting all tests in SiteManager may result in insufficient quality assurance testing.

Recommendations:

The Department should:

- Continue implementing statewide procedures to ensure consistency in the use of SiteManager, including prohibiting the use of blank tests.
- Implement controls in SiteManager to ensure that there is appropriate segregation of duties between personnel conducting sample testing and personnel reviewing sample testing.
- Implement controls in SiteManager to ensure that certified testers complete sampling tests.
- Evaluate the process for turning off the sample deficiency indicator in SiteManager to ensure that staff consistently document a justification and the appropriate authorization.

Management Response and Corrective Action Plan:

The department concurs with the recommendations and will:

- *Implement policy or system changes to require the approval of at least two different individuals for test samples.*
- *Implement policy or system changes to require the entry of the name of the certified tester performing the test along with the effective and expiration dates of their certification.*
- *Implement policy or system changes to require justification for turning off the sample indicator. Authorization for this function is currently limited to the District Director of Construction and their staff and the department believes this is the appropriate level of authority.*

Implementation Date: December 2011

Responsible Person: Russel Lenz

Reference No. 11-147

Procurement and Suspension and Debarment**CFDA 20.106 - Airport Improvement Program**

Award year – September 1, 2009 to August 31, 2010

Award numbers – 3-48-SBGP-46-2008, 3-48-SBGP-41-2007, 3-48-SBGP-45-2007, 3-48-SBGP-36-2006, 3-48-SBGP-37-2006, 3-48-SBGP-54-2009

Type of finding – Significant Deficiency and Non-Compliance

Federal rules require that, when a non-federal entity enters into a covered transaction with an entity at a lower tier, the non-federal entity must verify that the entity is not suspended or debarred or otherwise excluded from federal contracts. This verification may be accomplished by checking the Excluded Parties List System (EPLS), collecting a certification from the entity, or adding a clause or condition to the covered transaction with that entity (Title 2, Code of Federal Regulations, Section 180.300). Covered transactions include procurement contracts for goods and services that are expected to equal or exceed \$25,000 and all non-procurement transactions (that is, subawards to subrecipients) irrespective of award amount (Title 2, Code of Federal Regulations, Sections 180.210 and 180.220).

Questioned Cost: \$ 0

U.S. Department of
Transportation - Federal
Aviation Administration

For 7 (18 percent) of 40 procurements tested, the Department of Transportation (Department) did not verify that the vendor or contractor was not suspended or debarred from federal procurements. These seven procurements were design contracts, and the Department's standard contract template for design/engineer/consultant contracts did not include a clause for vendor certification of suspension and debarment status.

In 2009, the Department redesigned its standard contract template to include a suspension and debarment clause. However, the Department did not verify that vendors or contractors on its pre-existing design/engineer/consultant contracts were not suspended or debarred. Contracts for the seven procurements noted above were issued prior to the redesign of the contract template. Auditors reviewed the EPLS and verified that the vendors for the seven procurements were not currently suspended or debarred. The value of the seven contracts totaled \$1,270,115.

When the Department does not verify that contractors are not suspended or debarred, this increases the risk that it will enter into an agreement with an entity that is not eligible for federal procurements.

Recommendation:

The Department should verify and document that all vendors or contractors on active design/engineer/consultant contracts issued prior to the redesign of the contract template are not suspended or debarred from federal procurement.

Management Response and Corrective Action Plan:

On January 25, 2011, a report from the Excluded Parties List System was run for all Texas contractors that would include any entity the Aviation Division may have contracted for services. The report was reviewed and there were no vendors or contractors that had contracted with the Aviation Division on the debarment list.

Implementation Date: January 2011

Responsible Person: David Fulton

Reference No. 11-148

Reporting

(Prior Audit Issues 10-90 and 09-77)

CFDA 20.106 – Airport Improvement Program

CFDA 20.106 – Airport Improvement Program - ARRA

Award year – September 1, 2009 to August 31, 2010

Award number – 3-48-SBGP-39-2005, 3-48-SBGP-058-2009 (ARRA), 3-48-SBGP-059-2009 (ARRA), 3-48-SBGP-060-2009 (ARRA), 3-48-SBGP-061-2009 (ARRA), 3-48-SBGP-062-2009 (ARRA), 3-48-SBGP-063-2009 (ARRA),

Type of finding – Significant Deficiency and Non-Compliance

Standard Form 272 and 425 Reports

The Federal Aviation Administration’s (FAA) *Airport Improvement Program Handbook* (Handbook) and Program Guidance Letters (PGL) provide specific guidance for the administration of Airport Improvement Program block grants. According to this guidance, prior to October 1, 2009, grantees were required to submit the Standard Form 272 (SF-272) quarterly for each block grant and submit a final SF-272 when grants were completed (Handbook, Sections 1301 and 1314(a), and PGL 05-02). Effective October 1, 2009, the FAA replaced the SF-272 report with the SF-425 report (PGL 10-01).

Questioned Cost: \$ 0

U.S Department of
Transportation - Federal
Aviation Administration

One (13 percent) of 8 reports tested was not adequately supported by data in the Department of Transportation’s (Department) accounting system. The Department did not include one of its draws in the reported amounts. While Department management reviewed this report prior to submission, this review was not sufficient to detect the omission. As a result, the Department understated its cash draws by \$161,482. The Department corrected this error when auditors brought it to the Department’s attention.

The Department transitioned to the SF-425 report in October 2009 as required by the FAA. Auditors did not identify any exceptions in SF-425 reports tested for fiscal year 2010.

Recovery Act Section 1512 Reports

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)).

For each of the six Recovery Act reports the Department submitted for the period ending June 30, 2010, the Department listed the airports to which it passed funding as subrecipients. However, in September 2010, the Department determined that those airports were not subrecipients, and it reclassified the expenditures associated with those airports as direct expenditures. It did not submit corrected reports to the FAA.

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. Failure to make necessary corrections decreases the reliability of the information intended for the federal government and the general public.

Recommendations:

The Department should:

- Ensure that the financial reports it submits are accurate and supported by data in its accounting system.
- Ensure that it properly classifies entities on its Recovery Act Section 1512 reports.

Management Response and Corrective Action Plan:

Action Plan for SF 425 finding (first bullet above):

The SF 272 report that included the cash draw that was inadvertently omitted was completed before implementation of the new procedures instituted as a result of the previous 2009 audit. As a result of SAO Report 10-339, Reference No. 10-90, the corrective action taken was the development of a report from the Finance Division (FIN) that listed all draws within FIMS. This ensured that no draws were omitted from the reports. That FIN report was developed in January 2010 and is utilized today. This audit finding was for a SF 272 completed prior to January 2010 and even before conversion to the SF 425. The report from FIN is utilized today, as it has been since January 2010, and thus, is the corrective action needed for this audit finding.

Implementation Date: January 2010

Action Plan for Recovery Act Section 1512 Reports (second bullet above):

At the time the June 2010 ARRA 1512 reports were submitted, TxDOT was classifying airport grantees as subrecipients so the reports were and are correct for that time period. The 1512 report cannot be corrected because the federal reporting system does not allow changes and modifications to those previous reporting periods. Following initial entry, there is a very short time period for corrections but that is for only days. TxDOT is not able to modify the reports to show for the June 2010 time frame that grantees were vendors because they were considered subrecipients in June and the federal reporting system does not allow changes after submission.

Implementation Date: Not applicable

Responsible Person: David Fulton

Reference No. 11-149

Special Tests and Provisions – Revenue Diversion**CFDA 20.106 - Airport Improvement Program**

Award year – September 1, 2009 to August 31, 2010

Award numbers – Multiple

Type of finding – Significant Deficiency and Non-Compliance

In February 2009, the Federal Aviation Administration (FAA) concurred on a policy for the Department of Transportation (Department) to monitor general aviation airport sponsors for revenue diversion. That policy requires the Department to monitor annual financial reports (AFR) and airport sponsor self-certification forms submitted by the airport sponsors. To monitor AFRs, the Department stated that it would (1) request copies of sponsor AFRs in the sponsor agreements, (2) review 25 percent of AFRs on a random basis, (3) notify the FAA if it identifies potential revenue diversion based on its AFR review, and (4) follow up as directed by the FAA. To monitor self-certification forms, the Department stated that it would (1) send self-certification forms to

Questioned Cost: \$ 0

U.S. Department of
Transportation - Federal
Aviation Administration

25 percent of sponsors, (2) review returned forms, (3) notify the FAA if it identifies potential revenue diversion, and (4) follow up as directed by the FAA.

The Department did not consistently monitor its airport sponsors in accordance with its FAA-approved policy. Specifically, for 3 (9 percent) of 32 airport sponsors tested that were listed as submitting an AFR, the Department could not provide evidence that it received or reviewed the AFRs. For each of these three airport sponsors, the Department received an Office of Management and Budget Circular A-133 audit report or letter certifying that an A-133 audit was not required, but it did not receive an AFR.

The Department tracks its receipt and review of AFRs using a spreadsheet, but that spreadsheet contained errors. Specifically, for 3 (10 percent) of the 29 AFRs tested that the Department received, the Department did not document its review of the AFRs on the spreadsheet. As a result, **auditors could not verify whether the Department had reviewed 25 percent of AFRs as required by its monitoring policy.**

In addition, for 2 (15 percent) of the 13 airport sponsors tested, the Department did not review the self-certification forms because the airport sponsors did not return the forms the Department sent to them. While the Department's agreement may not specifically require receipt and review of the forms it sends out, it is reasonable to assume that this is the intent of the self-certification requirement. The Department also did not consistently use its monitoring spreadsheet to track its review of sponsor airport self-certification forms. Specifically, for 2 (18 percent) of the 11 self-certification forms tested that the Department received, the Department did not document its receipt and review of the forms in its monitoring spreadsheet. As a result, **auditors could not determine whether the Department reviewed self-certification forms from 25 percent of airport sponsors as required by its monitoring policy.**

Insufficient monitoring for revenue diversion poses a risk that airport sponsors could be diverting revenue from airport activities toward unallowable activities. By not reviewing information related to revenue diversion as required by its monitoring agreement with the FAA, the Department may be unable to detect revenue diversion and report it to the FAA as its agreement requires.

Recommendation:

The Department should develop and implement a documented process to receive, review, track, and follow up on AFRs and self-certification forms that it requires airport sponsors to submit.

Management Response and Corrective Action Plan:

Revenue diversion for general aviation airports has historically been rare at best. By nature of their operation, it is unfortunately rare that a general aviation airport generates sufficient revenue to fully fund their operations. Only commercial service airports that receive their funding directly from the Federal Aviation Administration historically generate revenue greater than operations costs, thus providing a risk for revenue diversion at that level of airport. In most all instances, local governments that own general aviation airports must provide other revenue sources to fund their airport. Therefore revenue diversion for general aviation airports has not been a concern for or has been identified as a risk by the Federal Aviation Administration. Regardless, TxDOT has performed the services for these issues in the same manner as the Federal Aviation Administration does for the grants they manage themselves for commercial service airports. However, we do agree that existing documentation does not fully show actions taken. While the appropriate actions are taken for receipt, review, tracking and follow-up, the current spreadsheet does not necessarily reflect those actions. The tracking spreadsheet will be modified to add appropriate areas to show dates for the above listed monitoring actions.

Implementation Date: March 2011

Responsible Person: David Fulton

Summary Schedule of Prior Year Audit Findings

Federal regulations (Office of Management and Budget Circular 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 2009 Schedule of Findings and Questioned Costs.
- Each finding in the 2009 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, 2009) has been prepared to address these responsibilities.

Department of Transportation

Reference No. 10-81

Activities Allowed or Unallowed
Allowable Costs/Cost Principles
Special Tests and Provisions - Project Approvals

Highway Planning and Construction Cluster
Award years - Multiple
Award numbers - Multiple
Type of finding - Significant Deficiency

Agencies shall maintain internal control over federal programs that provides reasonable assurance that agencies are managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements (Office of Management and Budget Circular A-133, Subpart C, Section 300 (b)).

Initial Year Written: 2009
 Status: Partially Implemented

U.S. Department of Transportation –
 Federal Highway
 Administration

The Department of Transportation (Department) uses the Federal Project Authorization and Agreement (FPAA) system to process and track project approvals from the Federal Highway Administration. These approvals are required prior to starting construction work on a project and expending federal funds.

The Department’s Finance Division manages the FPAA system, and that division does not enforce the same change management processes that the Department enforces for enterprisewide systems. As a result, adequate segregation of duties does not exist for making code changes for the FPAA system and migrating those changes to the production environment. One programmer had access to migrate code changes for the FPAA system to the production environment. For 2 (33 percent) of 6 code changes tested, that programmer both made the code change and moved the code change into the production environment. Additionally, that division does not maintain adequate documentation of changes it makes to the FPAA system, including documentation of testing, authorization, and migrating the changes to the production environment. Three (50 percent) of 6 code changes tested did not have adequate documentation of the changes made.

When a programmer has access to migrate code into the production environment, this increases the risk that unauthorized changes could be made to the system without proper approvals. Without adequate

documentation of testing, authorization, and migration of code to the production environment, there is an increased risk that changes may have unintended effects on the reliability of data in the system.

Although the general control weakness described above applies to activities allowed or unallowed, allowable costs/cost principles, and special tests and provisions - project approvals, auditors identified no compliance issues regarding these compliance requirements

Corrective Action:

This finding was reissued as current year reference number: 11-143.

Reference No. 10-82
Davis-Bacon Act

Highway Planning and Construction Cluster
Award years - Multiple

Award numbers - Federal project IM 03564(410), STP 2008(148), IM 0448(14), STP 2009(171), STP 2005(675)MM, STP 2008(76), BR 2007(268), STP 2008(877)HES, STP 2009(554)ES, HP 2009(333), IM 0106(93), HP 2007(324), and NH 2008(293)

Type of finding - Significant Deficiency and Non-Compliance

When required by the Davis-Bacon Act, the U.S. Department of Labor's (DOL) government-wide implementation of the Davis-Bacon Act, or by federal program legislation, all laborers and mechanics employed by contractors or subcontractors to work on construction contracts in excess of \$2,000 financed by federal assistance funds must be paid wages not less than those established for the locality of the project (prevailing wage rates) by the DOL (Title 40, United States Code (USC), Sections 3141-3144, 3146, and 3147 (formerly Title 40, USC, Sections 276a to 276a-7)).

Initial Year Written: 2009
Status: Partially Implemented

U.S. Department of
Transportation - Federal
Highway Administration

Non-federal entities shall include in construction contracts that are subject to the Davis-Bacon Act a requirement that the contractor or subcontractor comply with the requirements of the Davis-Bacon Act and the DOL regulations (Title 29, Code of Federal Regulations, Part 5, Labor Standards Provisions Applicable to Contracts Governing Federally Financed and Assisted Construction). This includes a requirement for the contractor or subcontractor to submit to the non-federal entity weekly, for each week in which any contract work is performed, a copy of the payroll and a statement of compliance (certified payrolls) (Title 29, Code of Federal Regulations, Sections 5.5 and 5.6). This reporting is often done using Optional Form WH-347, which includes the required statement of compliance (Office of Management and Budget No. 1215-0149).

Additionally, the Department of Transportation's (Department) *Construction Contract Administration Manual* requires that the Department conduct at least three labor compliance interviews of contractor and subcontractor project employees for each project per quarter when work was performed during the quarter. The Department uses these interviews to identify non-compliance with the Davis-Bacon Act and to ensure that contractors and subcontractor employees are properly classified and are being paid the appropriate wage rate in accordance with the Davis-Bacon Act.

All projects tested had standardized contracts that contained the required prevailing wage rate clause. However, the Department does not have a statewide standard process for ensuring that it collects the weekly certified payrolls for all projects or that it conducts and documents the required wage rate interviews.

Auditors requested payroll certifications for all weekly payrolls in fiscal year 2009. The Department was not always able to provide documentation that it collected the certified payroll from its contractors and subcontractors or conducted wage rate interviews. Specifically:

- Four (10 percent) of 40 projects tested did not provide all payroll certifications for payroll submitted in the fiscal year. These four projects had total contractor payments, including payroll and non-payroll costs, of \$590,515.15 for fiscal year 2009.
- Eleven (37 percent) of 30 projects tested did not have documentation to show that the Department conducted employee interviews.

Without submission of the required payroll certification and documentation of these interviews, the Department cannot ensure that contractor and subcontractor employees are properly classified and being paid the appropriate wage rate in accordance with the Davis-Bacon Act.

Corrective Action:

This finding was reissued as current year reference number: 11-142.

Reference No. 10-83

Reporting

Highway Planning and Construction Cluster

Award years - Multiple

Award numbers - Multiple

Type of finding - Significant Deficiency

The Department of Transportation (Department) is required by Office of Management and Budget (OMB) Circular A-133 to submit a PR-20, *Voucher for Work Under Provisions of the Federal-Aid and Federal Highway Acts, as Amended* (OMB No. 2125-0507). The PR-20 is required to report the total expenditures for a project that received federal aid from the Federal Highway Administration. The report should be completed and submitted promptly after the close-out of a project.

Initial Year Written: 2009
Status: Partially Implemented

U.S. Department of
Transportation - Federal
Highway Administration

The Department did not submit PR-20 reports in a prompt or orderly manner. The Department does not have a standard procedure for how it determines which reports to submit, and it asserted that a lack of dedicated staff over several years has contributed to this issue.

Auditors reviewed a list of projects that have been closed in the Department's financial system, but for which the Department had not yet submitted a PR-20. Based on the information on that list, the Department had not submitted PR-20s for 1,914 projects with close-out dates as early as August 1998.

The Department provided to auditors 600 PR-20 reports that it submitted to the Federal Highway Administration in fiscal year 2009. Auditors tested a sample of 40 PR-20 reports and did not identify any compliance errors. However, because of the lack of a standardized process for submitting reports, auditors could not determine whether the reports provided represent all reports submitted for the fiscal year.

The Federal Highway Administration relies on the Department to submit PR-20 reports in order to close out funding and records on funded projects.

Corrective Action:

This finding was reissued as current year reference number: 11-145.

Reference No. 10-84

Subrecipient Monitoring

(Prior Audit Issue - 09-80)

Highway Planning and Construction Cluster

Award years - Multiple

Award numbers - Multiple

Type of finding - Material Weakness and Material Non-Compliance

As a pass-through entity, the Department of Transportation (Department) is required by Office of Management and Budget (OMB) Circular A-133, March 2009 Compliance Supplement Part 3, Section M Subrecipient Monitoring, to monitor subrecipients' use of federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that subrecipients administer federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

Initial Year Written: 2008
Status: Partially Implemented

U.S. Department of Transportation -
Federal Highway Administration

Identification of Subrecipients

The Department was not able to identify a complete and accurate list of subrecipients for the Highway Planning and Construction Cluster. The Department's Finance Division identifies subrecipients through reports it generates by querying the Uniform Statewide Accounting System (USAS) for payments for federal construction activities. The Department then manually removes payments to vendors and other state agencies and uses the resulting payments as its population of subrecipients to report on its Schedule of Expenditures of Federal Awards. However, this process incorrectly identifies some entities as subrecipients instead of vendors. For example, this process results in local entities that provide "force services" such as law enforcement presence at a road construction site being incorrectly identified as subrecipients instead of vendors.

Auditors were not able to quantify the number of entities the Department had incorrectly identified as subrecipients. However, auditors selected a sample for testing and determined that 5 (11 percent) of 47 entities selected were originally identified by the Department as subrecipients but were actually vendors. The payments to these vendors were generally low-dollar transactions due to the nature of the services they provided. Therefore, the Department's incorrect identification of these vendors as subrecipients had a more significant effect on the number of subrecipients the Department reported than on the total dollar amount of subrecipient pass-through expenditures.

Pre-Award Monitoring

At the time of the award, pass-through entities must identify to subrecipients the applicable compliance requirements and the federal award information, including the Catalog of Federal Domestic Assistance (CFDA) title and number, the award name and number, and the name of federal awarding agency (Office of Management and Budget (OMB) Circular A-133 Compliance Supplement, Part 3, Section M).

The Department did not properly identify federal award information and compliance requirements to the subrecipient. While the Department uses a standard template for award agreements with subrecipients, this

template does not include identification of the federal award title and number or the CFDA title and number. It also does not identify the name of the federal awarding agency. The template does, however, refer to the Master Advanced Funding Template Agreement, which requires the subrecipient to comply with federal compliance requirements and provides other specific information regarding allowable costs and other requirements.

The template the Department uses requires the subrecipient to refrain from doing business with other entities that are suspended or debarred; however, it does not require the subrecipient to certify that it is not suspended or debarred.

Auditors identified the following:

- For 2 (5 percent) of 41 subrecipient agreements tested, the Department's district office overseeing the subrecipients provided no award documentation; as a result, auditors could not determine whether these awards contained required information.
- For the remaining 39 subrecipient awards tested, the award documentation the Department provided to the subrecipient did not identify the federal award or CFDA titles or numbers.

Inadequate identification of federal awards by the Department may lead to improper reporting of federal funding on the subrecipient's Schedule of Expenditures of Federal Awards. Additionally, when the Department does not verify that subrecipients are not suspended or debarred, this increases the risk that the Department will enter into an agreement with an entity that is not eligible to receive federal funding.

During-the-Award Monitoring

The Department does not have standardized processes to ensure adequate during-the-award monitoring by Department district offices. As a result, there are different levels and types of monitoring throughout the district offices. For example, some district offices provided documentation that included evidence of on-site monitoring visits, while other district offices used invoice reviews as their primary monitoring tool.

District offices provided documentation of their during-the-award monitoring for 41 subrecipients tested. This documentation included reviews of invoices for allowability, period of availability, and reporting. However:

- District offices that oversaw 2 (5 percent) of 41 subrecipients tested did not provide sufficient evidence of key monitoring, including review of invoices. Therefore, auditors could not determine whether the district offices monitored those subrecipients' compliance with federal requirements.
- For 3 (10 percent) of 29 subrecipients with matching requirements, the district offices did not provide evidence that they reviewed the invoices to ensure that the subrecipients complied with local matching requirements.

The Department also conducts other monitoring of subrecipients' compliance with the Davis-Bacon Act and requirements regarding equipment, procurement, real property acquisition, and quality assurance. However, the Department's documentation of this monitoring was not consistently provided to auditors. Specifically, based on the documentation the Department provided to auditors:

- For 15 (41 percent) of 37 subrecipients tested, the district offices did not provide documentation that they reviewed the subrecipients' cash management practices for compliance.
- For 9 (64 percent) of 14 subrecipients tested, the district offices did not provide documentation of monitoring the subrecipients' compliance with Davis-Bacon Act requirements.
- For 5 (45 percent) of 11 subrecipients tested, the district offices did not provide documentation of monitoring the subrecipients' compliance with equipment and real property management requirements.

- For 6 (19 percent) of 32 subrecipients tested, the district offices did not provide documentation of monitoring the subrecipients' compliance with federal and state procurement requirements.
- For 1 (50 percent) of 2 subrecipients tested, the district office did not provide documentation of monitoring the subrecipient's real property acquisitions.
- For 5 (45 percent) of 11 subrecipients tested, the district offices did not provide documentation of monitoring the subrecipients' quality assurance testing, project extensions, or project approvals.

Without a standardized process for during-the-award monitoring, the Department cannot determine whether its district offices adequately monitor the Department's subrecipients and, therefore, cannot determine whether subrecipients comply with federal requirements.

A-133 Single Audit Requirements

The Department must ensure that subrecipients expending federal funds of \$500,000 or more obtain an OMB Circular A-133 Single Audit and provide a copy of the audit report to the Department. The Department is required to review the audit report and to issue a management decision, if applicable.

The Department does not have a standardized process to ensure that all subrecipients that expend more than \$500,000 in federal funding in a fiscal year obtain an A-133 Single Audit as required by OMB Circular A-133. The Department's External Audit Office, which monitors A-133 Single Audits, does not consistently receive certifications from subrecipients that do not provide A-133 Single Audit reports when they expended less than \$500,000 in federal funds in the fiscal year.

For 15 (37 percent) of 41 subrecipients tested, the Department did not provide an A-133 Single Audit report or a certification from the subrecipient that an audit was not required. For 7 (47 percent) of those 15 subrecipients, auditors determined that the subrecipient submitted an A-133 Single Audit report to the Federal Audit Clearinghouse, indicating that the Department should have received an A-133 Single Audit report from these subrecipients.

The External Audit Office tracks and reviews A-133 Single Audit reports submitted by subrecipients. It also uses an audit checklist to facilitate review of the audits and forwards issues that it identifies to the appropriate division when the External Audit Office determines that follow-up is necessary.

Auditors identified the following:

- For 13 (52 percent) of the 25 A-133 Single Audit reports received by the External Audit Office, the External Audit Office did not provide the review checklist it used to review the audit.
- For 1 (4 percent) of the 25 A-133 Single Audit reports received by the External Audit Office, the review did not identify an issue related to the subrecipient's reporting of Highway Planning and Construction Cluster reimbursements.
- For 1 (4 percent) of the 25 audits received by the External Audit Office, the External Audit Office did not provide documentation that it followed up on a finding regarding the subrecipient's compliance with Davis-Bacon Act requirements.

These issues increase the risk that the Department will not be able to determine whether subrecipients comply with federal requirements and whether subrecipients having issues not detected through the subrecipient monitoring process.

Corrective Action:

This finding was reissued as current year reference number: 11-144.

Reference No. 10-85

Special Tests and Provisions - Use of Other State or Local Government Agencies

Highway Planning and Construction Cluster

Award years - Multiple

Award numbers - Various

Type of finding - Material Weakness and Material Non-Compliance

The Department of Transportation (Department) may use other public land acquisition organizations to conduct real property acquisitions for federal aid projects. The other organizations must comply with the Department's policies and practices for acquisition. The Department must monitor the real property acquisition activities of the other organizations to ensure compliance with state and federal law and requirements (Title 23, Code of Federal Regulations, Section 710.201(h)).

Initial Year Written: 2009
Status: Implemented

U.S. Department of Transportation - Federal Highway Administration
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To ensure that the other organizations comply with state and federal laws and regulations for real property acquisitions, the Department reviews land acquisition documentation and requires the other organizations to provide a certification of compliance to act in accordance with state and federal Laws prior to reimbursement.

The Department did not ensure that four local public agencies (LPA) conducted land acquisitions in accordance with the acquisition agreements prior to reimbursing the LPAs for the acquisition. The acquisition agreements state that the LPA must conduct the acquisition in accordance with federal and state acquisition laws. However, the Department was unable to provide documentation that it verified that the LPA complied with federal and state acquisition laws for 21 (53 percent) of the 40 acquisitions tested for 4 LPAs. The cost of those 21 acquisitions totaled \$1,794,539. However, auditors confirmed that these acquisitions were for real property used for highway construction. Specifically, auditors noted the following errors in the 21 projects:

- The Department was unable to provide the LPA's certification of compliance and was unable to provide documentation that it reviewed the land acquisition documentation for 13 (33 percent) of the 40 acquisitions tested.
- The Department was unable to provide the LPA's certification of compliance for 5 (13 percent) of the 40 acquisitions tested.
- The Department was unable to provide documentation that it reviewed the land acquisition documentation for 3 (8 percent) of the 40 acquisitions tested.

Without adequate monitoring, the Department cannot ensure that the LPA complies with state and federal laws and regulations.

Corrective Action:

Corrective action was taken.

Reference No. 10-86

Special Tests and Provisions - Project Extensions

Highway Planning and Construction Cluster

Award years - Multiple

Award number - MG 2004(394)

Type of finding - Significant Deficiency and Non-Compliance

The Department of Transportation (Department) is required by Office of Management and Budget Circular A-133 and Title 23, Code of Federal Regulations, Section 635.121, to obtain approval from the Federal Highway Administration (FHWA) for project extensions affecting project costs or the amount of liquidated damages, except in projects administered by the Department as identified by Title 23, United States Code, Section 106(c).

Initial Year Written: 2009
Status: Implemented

U.S. Department of
Transportation - Federal
Highway Administration

The Department uses change orders from SiteManager, its construction administration system, to initiate the process for submitting a federal letter of authority to obtain approval for a project extension from the FHWA.

Auditors tested change orders that required federal approval. For one of nine change order totaling \$777,931, the Department was not able to provide documentation that it completed the change order or obtained approval from the FHWA.

The FHWA requires timely, correct, and complete information from the Department on projects that the FHWA administers. When the Department does not submit the required approval requests to the FHWA, the FHWA is unable to make informed management decisions on projects.

Corrective Action:

Corrective action was taken.

Reference No. 10-87

Special Tests and Provisions - Quality Assurance

Activities Allowed or Unallowed

Allowable Costs/Cost Principles

(Prior Audit Issue - 09-81)

Highway Planning and Construction Cluster

Award years - Multiple

Award numbers - Multiple

Type of finding - Significant Deficiency and Non-Compliance

Control Weaknesses in SiteManager

Agencies shall maintain internal control over federal programs that provides reasonable assurance that the institutions are managing federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements (Office of Management and Budget Circular A-133, Subpart C, Section 300 (b)).

Initial Year Written: 2008
Status: Partially Implemented

U.S. Department of
Transportation - Federal
Highway Administration

SiteManager, the Department of Transportation's (Department) construction administration system, does not adequately ensure that appropriate Department personnel review and approve contractor transactions prior to payment. In addition, Department district offices are able to set up and define the personnel who are allowed to review and approve each transaction in SiteManager. SiteManager also allows assigned users to both approve an estimate and submit the estimate for payment. This increases the risk of payments to contractors for unallowable costs.

In addition, SiteManager does not have sufficient controls to ensure that (1) only authorized testers are able to enter test records and (2) deficiencies are cleared appropriately prior to contractor payment.

Special Tests and Provisions- Quality Assurance Program

Title 23, Code of Federal Regulations (CFR), Chapter 205, requires that each state transportation department "shall develop a quality assurance program which will assure that the materials and workmanship incorporated into each federal-aid highway construction project on the [National Highway System] NHS are in conformity with the requirements of the approved plans and specifications, including approved changes. The program must meet the criteria in Section 637.207 and be approved by the FHWA." Additionally, Title 23, CFR 637, Chapter 209, requires that only qualified personnel conduct sampling and testing to be used in the acceptance decision.

Although the Department had some controls in place for its quality assurance programs, it does not have a standardized process for documentation of sampling and testing. The Department's district offices rely on SiteManager to document the results of its material sampling and testing. District offices do not consistently retain documentation of the testing information after data entry into SiteManager. Therefore, auditors relied on the information in SiteManager for testing but auditors also reviewed additional documentation the Department provided.

The Department did not always comply with the quality assurance program approved by the Federal Highway Administration. Specifically:

- 8 (20 percent) of 40 tests did not comply with the requirements for each type of material as specified in the Department's *Guide Schedule for Sampling and Testing*. These eight tests included blank tests documented in SiteManager and projects in SiteManager for which the required test could not be found.
- 5 (13 percent) of 38 tests completed were conducted by an individual who was not a certified tester.

Additionally, for 5 (13 percent) of 40 projects that auditors reviewed in SiteManager, the Department did not have the "Deficient Sample Indicator" turned on. This indicator prevents payment to the contractor when a sample tested does not meet the Department's material requirements. For these five projects, auditors could not determine whether the Department paid the contractor prior to resolving any deficiencies.

Control weaknesses in SiteManager and a lack of standardized process for adherence to the Department's approved quality assurance program increase the risk that the Department will not identify deficiencies that adversely affect the quality of federally funded highway projects.

Activities Allowed or Unallowed and Allowable Costs/Cost Principles

Although the SiteManager control weaknesses described above apply to activities allowed or unallowed and allowable costs/cost principles, auditors identified no compliance issues regarding these compliance requirements.

Corrective Action:

This finding was reissued as current year reference number: 11-146.

Reference No. 10-88

Subrecipient Monitoring

Highway Safety Cluster

Award years - Multiple

Award numbers - Multiple

Type of finding - Significant Deficiency and Material Non-Compliance

Award Identification

At the time of the award, pass-through entities must identify to subrecipients the applicable compliance requirements and the federal award information, including the Catalog of Federal Domestic Assistance (CFDA) title and number, the award name and number, and the name of federal awarding agency (Office of Management and Budget (OMB) Circular A-133 Compliance Supplement, Part 3, Section M). Additionally, when a non-federal entity enters into a subaward agreement, the non-federal entity must verify that the entity is not suspended or debarred or otherwise excluded from federal contracts. This verification may be accomplished by checking the Excluded Parties List System (EPLS), collecting a certification from the entity, or adding a clause or condition to the covered transaction with that entity (Title 2, Code Federal Regulations, Section 180.300).

Initial Year Written: 2009 Status: Partially Implemented
U.S. Department of Transportation - National Highway Safety Traffic Administration

For all 40 subrecipients tested for the Highway Safety Cluster, the Department of Transportation (Department) did not provide the CFDA title and number, the award name and number, the name of the federal agency, or the applicable compliance requirements to subrecipients at the time of award. The Department's standard grant agreement for fiscal year 2009 did not contain CFDA-related information.

For 4 (10 percent) of the 40 subrecipients tested for the Highway Safety Cluster, the Department also did not notify the subrecipient of OMB Circular A-133 audit requirements or verify that the subrecipient was not suspended or debarred from federal procurements. These four awards were for incentive grants awarded to law enforcement agencies for their participation in safety belt and impaired driving enforcement efforts. The Department's standard award agreement for this type of award did not contain clauses regarding OMB A-133 audit requirements or suspension and debarment.

In fiscal year 2009, the Department reported \$26,569,288 in federal pass-through to local entities. Not communicating the required award information and federal requirements to subrecipients increases the risk that subrecipients may not be informed and not comply with federal requirements. The absence of clear communication related to the federal award also increases the potential for misreporting of federal awards by the Department and the subrecipients on the Schedule of Expenditures of Federal Awards.

A-133 Single Audit Monitoring

According to OMB Circular A-133, Compliance Supplement Part 3, Section M, the Department must ensure that subrecipients expending federal funds of \$500,000 or more obtain an OMB Circular A-133 Single Audit and provide a copy of the audit report to the Department. The Department is required to review the audit report and to issue a management decision, if applicable. OMB Circular A-133, March 2009 Compliance Supplement Part 3, Section M, requires the Department to issue a management decision on audit findings within six months after receipt of a subrecipient's audit report. In cases of

continued inability or unwillingness of a subrecipient to obtain the required audits, the Department must take appropriate action using sanctions.

Twenty-nine (76 percent) of 38 subrecipients tested either did not have an A-133 Single Audit on record with the Department for fiscal year 2008 when an audit was required or did not have confirmation on file that the audit was not required. According to the Federal Audit Clearinghouse, 8 (28 percent) of these 29 subrecipients had submitted an A-133 Single Audit report for fiscal year 2008. The audit report for one of these entities contained a finding related to the data collection form not being submitted in a timely manner to the OMB-designated federal clearinghouse. The Department was not aware of the issue because it did not obtain the audit report from the subrecipient. The Department did not have a process to ensure that it maintained a log of audit reports received or audit findings that required follow-up. Additionally, the Department did not have a sanction policy for subrecipients of Highway Safety Cluster awards that do not adhere to A-133 Single Audit requirements. Weak monitoring results in diminished oversight and increases the potential of program funds not being spent as intended.

Recommendations:

The Department should:

- Communicate the required elements of award information and specifics related to federal compliance requirements by including that information in the award agreement.
- Require subrecipients to certify that they will obtain an A-133 Single Audit if they meet the threshold or certify that they are not required to obtain an A-133 Single Audit.
- Create a list of subrecipients that submit A-133 Single Audit reports and subrecipients that are not required to submit A-133 Single Audit reports.
- Review A-133 Single Audit reports that subrecipients submit, keep a log of findings in those reports, and follow up as appropriate.
- Develop a sanctions policy for subrecipients that repeatedly do not submit required A-133 Single Audit reports and for subrecipients that do not correct findings in those reports.

Management Response and Corrective Action Plan 2009:

Award Identification Finding

Recommendation:

“Communicate the required elements of award information and specifics related to federal compliance requirements by including that information in the award agreement.”

Corrective Action

- *By the end of March 2010, the eGrants system will include the Catalog of Federal Domestic Assistance (CFDA) information for the current grant lifecycle (FY 2010) projects and visible on the Proposal Task Number page.*
- *Starting with the upcoming grant lifecycle (FY 2011), the CFDA information will also be included on the Grant Agreements.*
- *Starting immediately, all new incentive grants awarded to law enforcement agencies participating in the safety belt and impaired driving enforcement efforts will contain clauses in the Terms and Conditions regarding OMB A-133 audit requirements or suspension and debarment as recommended.*

A-133 Single Audit Monitoring

The last four recommendations deal with A-133 Single Audit monitoring. Subrecipients are supposed to obtain an A-133 Single Audit if they meet the threshold or certify that they are not required to obtain an A-133 Single Audit.

Recommendation:

“Require subrecipients to certify that they will obtain an A-133 Single Audit if they meet the threshold or certify that they are not required to obtain an A-133 Single Audit.”

Corrective Action

- *Starting immediately, the Traffic Safety Section, in conjunction with the Audit Office, will utilize the eGrants system to notify subrecipients about A-133 Single Audit requirements.*
- *Starting with the upcoming grant lifecycle (FY 2011), the Traffic Safety Section, in conjunction with the Audit Office, will make modifications to the eGrants system to require subrecipients to certify that they will obtain an A-133 Single Audit if they meet the threshold or certify that they are not required to obtain an A-133 Single Audit.*

Recommendation:

“Create a list of subrecipients that submit A-133 Single Audit reports and subrecipients that are not required to submit A-133 Single Audit reports.”

Corrective Action

- *By the end of 2010, the Audit Office, in conjunction with the Traffic Safety Section, will create a list of subrecipients that submit A-133 Single Audit reports and subrecipients that are not required to submit A-133 Single Audit reports.*
- *By the end of 2010, the Traffic Safety Section, in conjunction with the Audit Office, will make modifications to the eGrants system to support this action.*

Recommendation

“Review A-133 Single Audit reports that subrecipients submit, keep a log of findings in those reports, and follow up as appropriate.”

Corrective Action

- Starting immediately, the Audit Office will review all Single Audit Reports for the Traffic Safety subrecipients and will keep a log of all audit findings contained in these reports.
- Starting immediately, the Traffic Safety Section will follow up on these audit findings as appropriate.
- By the end of 2010, the Traffic Safety Section, in conjunction with the Audit Office, will make modifications to the eGrants system to support this action.

Recommendation

“Develop a sanction policy for subrecipients that repeatedly do not submit required A-133 Single Audit reports and for subrecipients that do not correct findings in those reports.”

Corrective Action

- By the end of 2010, the Traffic Safety Section, in conjunction with the Audit Office, will develop a sanctions policy for subrecipients that repeatedly fail to submit the required A-133 Single Audit reports and for subrecipients that do not correct findings in those reports. This sanctions policy will be included in the 2010 update of the Traffic Safety Program Manual.

Management Response and Corrective Action Plan 2010:Award Identification:

TxDOT has revised our eGrants system to now include on our traffic safety grant agreements the CFDA number, fund source description, and name of our federal funding agency as requested by the State Audit Office. Attached are screen shots from eGrants that captures the fund source and demonstrates how the CFDA numbers and titles are linked (see Attachment A). Also attached (Attachment B) is a screen shot of what the first page of our new traffic safety grants for FY2011 look like. Starting in FY2011, the Click It or Ticket Incentive grants and the Impaired Driving Mobilization Incentive grants now include the full set of terms and conditions just like the other traffic safety grants (this includes the A-133 audit requirement or suspension and debarment conditions, see Attachment C – example of an executed incentive grant).

A-133 Single Audit Monitoring:

TRF-TS is using eGrants to assist with notifying subrecipients about the A-133 Single Audit Requirements. Beginning in October 2010, a new process was implemented in order for traffic safety subrecipients to receive a grant. They have to read and agree to a statement in the Texas eGrants system that they will either submit the A-133 Single Audit Report or the letter if they do not meet the threshold. Attached (Attachment D) is a screen shot to show where the agencies and organizations agree to provide TxDOT with appropriate documents relating to the A-133 Audit requirements. The instructions for completing the information in eGrants are also included in Attachment D. Attachment E is a listing of FY2011 subrecipients that have agreed to the statement. By January 31, 2011, TRF will also develop a process to create a list of subrecipients that identifies those that submitted an A-133 Single Audit Report, a letter if they do not meet the threshold, or indicate if a report or letter is delinquent. These reports or letters will apply to the year currently due (i.e., as of December 2010, the reports or letters due are for FY2009). This report will be provided to the National Highway Traffic Safety Administration (NHTSA) semiannually starting in 2011 on the following dates: March 1 and October 1. TRF will utilize eGrants to remind agencies that either the Single Audit Reports or Letters are due.

The TxDOT AUD office is reviewing all Single Audit Reports for Traffic Safety subrecipients and keeps a log of audit findings contained in these reports. There are no traffic safety audit findings at this time. If the AUD Office identifies a traffic safety audit finding, TRF-TS will immediately follow up with the subrecipient on any findings. TxDOT has made modifications to the eGrants system (see Attachment F) to document any audit findings for a subrecipient.

TxDOT is drafting a sanctions policy for recipients that repeatedly fail to submit the required A-133 Single Audit reports and for subrecipients that do not correct findings. The sanctions policy will be included in the update of the Traffic Safety Program Manual (TSPM). The final version of the TSPM is scheduled to be issued formally by March 31, 2011.

Implementation Date: 1/31/11 for creating the detailed subrecipient list and 3/31/11 for finalizing the sanctions in the Traffic Safety Program Manual.

Responsible Person: Terry Pence

During-the-Award Monitoring

A pass-through entity is responsible for monitoring the subrecipient's use of federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that the subrecipient administers federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved (OMB Circular A-133 Compliance Supplement, Part 3, Section M).

The Department monitors subrecipient grant performance to verify compliance with state and federal requirements, as well as to verify that project objectives and performance measures are being achieved. Project monitoring is conducted in a number of ways, including the regular review of project performance reports and request for reimbursements and on-site monitoring reviews of project operations, management, and financial records and system.

For 3 (9 percent) of 32 subrecipients tested that were required to receive on-site monitoring, the Department did not provide documentation that it conducted such monitoring. For one additional subrecipient tested, the Department did not have evidence in eGrants, the Web-based system the Department uses to manage grant projects, that it performed the required monitoring. For this subrecipient, the Department provided other documentation that it performed on-site monitoring. By the Department not maintaining documentation of on-site monitoring, there is no reasonable assurance that such monitoring occurred and that issues identified through monitoring are appropriately addressed to ensure subrecipient compliance with federal laws and regulations.

The Department's Traffic Safety Section has a policy that requires subrecipients to enter and submit a performance report for review by the Department prior to allowing the subrecipient to request reimbursement for all or a part of the report period. Due to a user misconfiguration of the eGrants setting meant to support this policy, in the sample of subrecipients tested, 1 (3 percent) of 37 subrecipients entered a performance report but did not submit the report for review. Although the report was not submitted, the subrecipient submitted the accompanying request for reimbursement and the Department approved the request for reimbursement. The entered performance report was substantially complete. The Department was in compliance with this requirement. While the misconfiguration was detected and corrected by the Department, 11 performance report submissions in 2009 (out of the 2,229 that had been submitted up to the time of correction) bypassed the policy due to the misconfiguration.

Corrective Action:

Corrective action was taken.

Reference No. 10-89

Subrecipient Monitoring

Special Tests and Provisions - R3, Subrecipient Monitoring-Applicable to all Major Programs with Expenditures of ARRA Awards

CFDA 20.106 - Airport Improvement Program

CFDA 20.106 - Airport Improvement Program - ARRA

Award years - Multiple

Award numbers - Multiple

Type of finding - Significant Deficiency and Material Non-Compliance

As a pass-through entity, the Department of Transportation (Department) is required by Office of Management and Budget (OMB) Circular A-133, March 2009 Compliance Supplement Part 3, Section

Initial Year Written: 2009
Status: Implemented

U.S. Department of Transportation -
Federal Aviation Administration

M Subrecipient Monitoring, to monitor subrecipients' use of federal awards through reporting, site visits, regular contact, or other means to provide reasonable assurance that subrecipients administers federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved. The Department must also identify to first-tier subrecipients the requirement to register in the Central Contractor Registration (CCR) system, including obtaining a Dun and Bradstreet Data Universal Numbering System (DUNS) number, and keep that information current (American Recovery and Reinvestment Act (ARRA), Section 1512(h), , and Title 2, Code of Federal Regulations, Section 176.50c).

Pre-Award Monitoring

The Department attempts to comply with the requirements related to communicating award identification elements to its subrecipients by including the required information in its project participation agreements with subrecipients. However, those agreements did not always include the required information. Specifically, for 40 (95 percent) of 42 subrecipient files tested for the Airport Improvement Program, the Department was unable to provide evidence that it communicated the CFDA number to its subrecipients. The templates the Department used for award documentation did not contain CFDA numbers. This increases the risk that subrecipients could report program expenditures incorrectly on the schedule expenditures of federal awards and periodic reports required by the program. In addition, the lack of program identification may result in subrecipients not being informed of compliance requirements that are specific to the program, which increases the risk of non-compliance. For fiscal year 2009, the Department passed-through \$71,384,983 in federal funds.

In addition, for 1 (33 percent) of 3 subrecipients tested that received ARRA awards, the Department did not provide evidence that it verified the subrecipient's CCR registration prior to the award. The Department disbursed \$23,421.50 in ARRA funding to this subrecipient during fiscal year 2009. This could create inefficiencies in reporting ARRA information in a timely and accurate manner. In fiscal year 2009, the Department reported \$1,019,156.86 in federal pass-through ARRA funds to local entities.

During-the-Award Monitoring

The Department is required to monitor the activity of subrecipients that acquire real property. The Department's aviation unit has a land acquisition manager who handles the appraisal process, issues letters of intent, and performs site visits of the properties to speak with property owners.

For 1 (14 percent) of 7 subrecipients tested for the Airport Improvement Program, the Department did not provide evidence that it sent letters of intent or written appraisals to property owners. According to the Department, an outside firm was hired to conduct this service for one airport project due to the large number of property owners involved. However, the Department did not receive or retain copies of letters of intent or letters of written appraisals sent to property owners by the outside firm. This increases the risk that property owners are not provided information required by laws and regulations and exposes the Department to potential liability.

A-133 Audit Requirements

The Department must ensure that subrecipients that spend \$500,000 or more in federal funds obtain an OMB Circular A-133 Single Audit and provide a copy of the audit report to the Department. The Department is required to review the audit report and to issue a management decision, if applicable. OMB Circular A-133, March 2009 Compliance Supplement Part 3, Section M, requires the Department to issue a management decision on audit findings within six months after receipt of a subrecipient's audit report. In cases of continued inability or unwillingness of a subrecipient to obtain the required audits, the Department must take appropriate action using sanctions.

For 32 (76 percent) of 42 subrecipients tested for the Airport Improvement Program, the Department did not provide evidence that it verified the subrecipients had obtained Single Audits.

The Department provides award documentation through project participation agreements. These agreements state that each airport should have an annual audit conducted. However, the agreements do not specify the requirement to obtain a Single Audit if the subrecipient has spent more than \$500,000 in federal funds. In addition, the Department has no process to track subrecipients' Single Audit reports. Some subrecipients send audit reports to the Department, but the Department does not track the reports or keep a list of subrecipients that do not provide audit reports. For subrecipients that submit Single Audit reports, the Department does not track audit findings and management responses, and it does not administer sanctions for continued non-compliance. In prior periods, the Department considered airports that received program benefits from the Department as vendors, as these relationships had both vendor and subrecipient characteristics. However, for fiscal year 2009, the Department classified the relationships with these entities as subrecipients. The reclassification of these entities as subrecipients contributed significantly to the control weaknesses described above. Weak monitoring results in diminished oversight and increases the potential of program funds not being spent as intended.

Corrective Action:

Corrective action was taken.

Reference No. 10-90

Reporting

(Prior Audit Issue - 09-77)

CFDA 20.106 - Airport Improvement Program

Award years - Multiple

Award numbers - 348SBGP33-2005 and 348SBGP53-2008

Type of finding - Significant Deficiency and Non-Compliance

Recipients are responsible for managing, monitoring, and reporting performance for each project, program, subaward, function, or activity supported by the award. Recipients use the *Financial Status Report* (FSR) SF-269 (Office of Management and Budget (OMB) No. 0348-0039) or SF-269A (OMB No. 0348-0038) to report the status of funds for all non-construction projects and for construction projects when the FSR is required in lieu of the SF-271 (Title 49, Code of Federal Regulations, Section 18.41).

Initial Year Written: 2008 Status: Partially Implemented

U.S. Department of Transportation - Federal Aviation Administration

The Federal Aviation Administration's (FAA) *Airport Improvement Program Handbook* (Handbook) and Program Guidance Letters (PGL) provide specific guidance for the administration of the Airport Improvement Program block grants. According to the Handbook and PGL, grantees are required to submit the Standard Form 272 (SF-272) quarterly for each block grant and submit a final SF-272 when grants are completed (Handbook, Sections 1301 and 1314(a), and PGL 05-02).

Two (5 percent) of 40 reports tested for the Airport Improvement Program were not adequately supported by data in the Department of Transportation's (Department) accounting system. The Department did not resolve these discrepancies. For both reports, the Department did not include one of its draws in the reported amounts. Department management reviewed all reports tested prior to report submission, but this review was not sufficient to ensure that all information in the reports was accurate. By not ensuring that all draws are included in the reports, the accuracy of reporting is affected, and adjustments may be required on subsequent reports. The total difference between the reported amounts and amounts in the Department's accounting system data was \$9,900.

Corrective Action:

This finding was reissued as current year reference number: 11-148.

Reference No. 10-91

Reporting

CFDA 20.509 - Formula Grants for Other Than Urbanized Areas

Award year - October 1, 2008 to September 30, 2009

Award number - TX-18-X028-02, TX-18-X029-04, TX-18-X030-01, and TX-18-X031-02

Type of finding - Significant Deficiency and Non-Compliance

Recipients are responsible for managing, monitoring, and reporting performance for each project, program, subaward, function, or activity supported by the award. Recipients use the *Financial Status Report* (FSR) SF-269 (Office of Management and Budget (OMB) No. 0348-0039) or SF-269A (OMB No. 0348-0038) to report the status of funds for all non-construction projects and for construction projects when the FSR is required in lieu of the SF-271 (Title 49, Code of Federal Regulations, Section 18.41). Federal Transit Administration Circular 9040.1F requires recipients to submit an FSR annually on an accrual basis documenting costs incurred and available balances.

Initial Year Written: 2009
Status: Partially Implemented

U.S. Department of
Transportation - Federal
Transit Administration

For 5 (83 percent) of 6 FSRs tested for the Formula Grants for Other Than Urbanized Areas program, the Department of Transportation (Department) reported non-federal share amounts that were not supported by its accounting records. The Department did not use or have accounting records to determine non-federal outlays and the non-federal share of unliquidated obligations. The Department serves as a pass-through for this program and did not track the local source amount of the non-federal share. The Department is capable of tracking the state source amount of the non-federal share; however, it did not use state accounting records to determine the non-federal amounts it reported on its FSRs. The Department determined non-federal outlay and unliquidated obligation amounts by multiplying the federal outlay amounts by the mandated matching requirements, instead of using actual non-federal costs incurred.

Recommendation:

The Department should develop a process that would facilitate the collection of information related to actual non-federal costs incurred by subrecipients.

Management Response and Corrective Action Plan 2009:

The Department will develop and implement a process by which it can collect information from its subrecipients regarding the reporting of the non-federal match on the FSRs. This collected information will be used in completing the FSRs. The Department will also work with the State Comptroller as it develops the new financial system ("Project One") for state agencies and notify the Comptroller of the requirement to collect this information.

Management Response and Corrective Action Plan 2010:

The Public Transportation Division of TxDOT is working on developing new billing forms to start effective September 1, 2010 to collect local match information. Billing form information will be used to complete FSR's. The Project One is in the design phase and schedule is directed by the Comptroller's Office.

Implementation Date: April 1, 2011

Responsible Person: Eric Gleason

Reference No. 10-92

Subrecipient Monitoring

CFDA 20.509 - Formula Grants for Other Than Urbanized Areas

CFDA 20.509 - Formula Grants for Other Than Urbanized Areas - ARRA

Award year - October 1, 2008 to September 30, 2009

Award numbers - TX-18-X029-00, TX-18-X030-02, TX-18-X031-02, TX-18-X032-00, and TX-86-X001-01 (ARRA)

Type of finding - Material Weakness and Material Non-Compliance

The Department of Transportation (Department) as a pass-through entity is responsible for monitoring subrecipients' use of federal awards. The Department currently monitors 39 rural transit districts and several intercity bus providers to ensure they comply with the requirements for the Formula Grants for Other Urbanized Areas program. Monitoring is accomplished through the Department's 25 district public transportation coordinators who oversee various federal programs within their jurisdictions. Public transportation coordinators perform numerous duties including quarterly on-site visits, annual compliance on-site reviews, review of financial records, approval of monthly invoices, tracking of procurement activities, reviews of reports, issuance of improvement action plans when deficiencies are noted, discussion of problems encountered or need for technical assistance, and monitoring of compliance with federal regulations and provisions of grant agreements.

Initial Year Written: 2009
Status: Partially Implemented

U.S. Department of
Transportation - Federal
Transit Administration

Pre-award Documentation

At the time of the award, pass-through entities must identify to subrecipients the applicable compliance requirements and the federal award information, including the Catalog of Federal Domestic Assistance (CFDA) title and number, the award name and number, and the name of federal awarding agency (Office of Management and Budget (OMB) Circular A-133 Compliance Supplement, Part 3, Section M). However:

- For all 41 subrecipient agreements tested, the Department did not include the federal award number on the award documentation it provided to the subrecipient. The Department uses a standard template for subrecipient awards, but it did not include the federal award number in that template.
- For 6 (15 percent) of 41 subrecipient agreements tested, the Department also did not notify subrecipients of the federal awarding agency's name; for 4 of those 6, it also did not include the CFDA number for the grant. These subrecipient agreements were all for intercity bus providers. The standard agreement for this type of subrecipient did not contain the awarding agency's name or CFDA number.

These issues increase the risk of subrecipients misreporting program expenditures on their schedule of expenditures of federal awards.

During the Award Monitoring

The Department monitors its subrecipients compliance with federal requirements through several methods. As part of the monitoring process, the Department's Public Transportation Coordinators conduct monthly invoice reviews to ensure matching, cash management, period of availability, and program income requirements are being met. The review does not include a review for the allowability of items purchased with federal funds. However, the Department does conduct quarterly on-site visits, which include a limited review of transactions for allowable costs and activities. Additionally, the Department conducts an annual compliance review of its subrecipients, which includes nine program areas. A review of Charter Services and School Bus Operations to ensure compliance with applicable federal regulations related to this Special Test.

Public Transportation Coordinators perform additional duties, which include monitoring and documenting the subrecipients compliance with federal procurement guidelines multiple times throughout the year and performing biannual equipment inventories.

The Department does not consistently conduct annual compliance reviews and other periodic monitoring, including review of Charter Services or school bus operations. Specifically:

- For 8 (20 percent) of 41 subrecipients tested, the Department did not perform an annual compliance review or annual review of Charter Services and School bus operations for fiscal year 2009.
- For 15 (42 percent) of 36 subrecipients tested, auditors could not verify that the Public Transportation Coordinator had performed its required biennial equipment inventory due to insufficient documentation.
- For 3 (16 percent) of 19 subrecipients tested, the Department's Public Transportation Coordinator did not document the procurement of equipment by subrecipients to ensure compliance with federal requirements. Total cost of the three pieces of equipment was \$164,368.

The Department does not consistently perform quarterly on-site reviews to determine the allowability of the subrecipient's costs. Specifically:

- For 6 (15 percent) of 41 subrecipients tested, the Department did not perform any quarterly on-site reviews to review allowable costs for fiscal year 2009.
- For 2 (5 percent) of the 41 subrecipients tested, the Department did not perform its required second quarter review for allowable costs.
- Additionally, the Department's process for reviewing allowable costs in its quarterly review is to select two expenditures, to review for allowability. However, the Department does not perform a monthly review of all expenditures of the subrecipient.

The Department does not consistently review monthly invoices to determine its subrecipient's compliance with matching, cash management, program income, and period of availability requirements. Specifically:

- For 13 (32 percent) of 41 subrecipients tested, the federal match amount on monthly invoices could not be verified due to lack of supporting documentation.
- For 12 (32 percent) of 37 subrecipients tested, the program income amount on monthly invoices could not be verified due to lack of supporting documentation.
- For 1 (3 percent) of 41 subrecipients tested, farebox revenue was not subtracted from operating expense prior to determining the federal share amount for reimbursement. This resulted in an overcharge of \$1,312 to the federal share of operating expenses on the monthly invoice causing the miscalculation of the federal match amount.

- For 1 (2 percent) of 41 subrecipients tested, the subrecipient charged 70 percent of operating assistance expenses to the 5311 Rural and Small Areas program instead of the required 50 percent. This resulted in an overcharge of \$4,052 to the federal share of operating expenses on the monthly invoice.
- For 1 (2 percent) of 41 subrecipients tested, the subrecipient charged \$5,476 of expense incurred by the 5307 Large Urban Cities program to the 5311 Rural and Small Areas program. The total invoice amount of \$6,200 also was miscoded as well. The \$6,200 were operating expenses, however, the Public Transportation Coordinator charged the operating expenses to the administrative account since the operating account was fully expended.

By not reviewing monthly invoices for match and program income requirements, the Department could be charging the incorrect amount of federal funds to the 5311 program and subrecipients could profit at the federal government's expense. In addition, by not properly conducting on-site visits both quarterly and annually, the Department is increasing the risk of significant non-compliance with federal rules and regulations including non-compliance with allowable activities and special tests and provisions. Furthermore, the Department by not verifying subrecipients are following federal procurement guidelines and performing inventory of purchased equipment with federal funds could result in the subrecipient purchasing unallowable items or disposing of vehicles without the Department's approval and knowledge. Each of the issues identified above may also bring sanctions and recoup future payments to the Department.

Recommendations:

The Department should:

- Follow established policy and procedures and perform complete annual compliance reviews for all subrecipients.
- Follow established policy and procedures and perform quarterly on-site monitoring visits for all subrecipients.
- Implement a monthly monitoring process to verify allowable activities and costs for subrecipients.
- Implement a monthly monitoring process to verify the subrecipients meet match and program income requirements.
- Follow established policy and procedures for documentation of inventories of equipment.
- Maintain adequate supporting documentation for the procurement of equipment and follow established policy and procedures for documentation of compliance with procurement requirements.
- Include all required federal award information in award documentation provided to subrecipients.

Management Response and Corrective Action Plan 2009:

The Department agrees with the recommendations and has already taken some action to correct. Prior to June 2009, the public transportation monitoring function was decentralized to TxDOT's 25 district offices. Staff assigned to these duties was in most cases also responsible for numerous other non-public transportation tasks. Effective June 1, 2009, TxDOT reorganized so that district personnel performing public transportation duties report directly to the division. The consolidation of the functions and staff into the Public Transportation Division provides direct oversight for the field functions including how policies and procedures are carried out.

In regard to monthly monitoring processes to verify allowable activities and costs and verification of match and program income requirements, the Department will seek out resources, such as the Texas Transportation Institute and TxDOT's Audit Office, to prepare a guidance document for the Department that will provide information on supporting documentation for billings and allowable expenditures for both TxDOT staff and subrecipients.

In regard to award documentation provided to subrecipients, for new grant agreements the Code of Federal Domestic Assistance (CFDA) number, federal agency and federal grant numbers will be identified in the project grant agreements. The standard template for federally funded agreements will be amended, if needed, to include any missing required information. No federally funded grant agreement will be executed without the required information.

Management Response and Corrective Action Plan 2010:

Pre-award monitoring – The Public Transportation Division (PTN) of TxDOT has corrected the agreement templates to include all required federal information on the agreement forms as of 7/15/2010.

Implementation Date: July 15, 2010

Responsible Person: Eric Gleason

During the Award Monitoring – PTN has policies in place requiring monitoring and will review annually to ensure all field staff are conducting scheduled monitoring as of 2/10/2010.

Implementation Date: February 10, 2010

Responsible Person: Eric Gleason

Audit and Sanction Monitoring

The Department must ensure that subrecipients expending federal funds of \$500,000 or more obtain an OMB Circular A-133 Single Audit and provide a copy of the audit report to the Department. The Department is required to review the audit report and to issue a management decision, if applicable. However:

- One (3 percent) of 35 subrecipients tested that were required to obtain an audit did not obtain the audit completed within the required time frame.
- For 4 (67 percent) of 6 subrecipients that were not required to obtain an audit, the Department did not perform an annual compliance review of the subrecipients.
- For 2 (6 percent) of 32 subrecipient A-133 Single Audits reports the Department received, the Department did not forward the findings to the Public Transportation Division or External Audit, which is the office that monitors subrecipients' Single Audit reports, for management decision and follow up. One of these audit reports specifically listed a Davis-Bacon finding for the Formula Grants program, while the other audit report listed a finding that encompassed all major federal programs.

There is also a control weakness within the Single Audit report reviews that the Department's External Audit Office performs. External Audit is unaware of which subrecipients are required to submit Single Audit reports. Currently External Audit does not perform any type of confirmation with subrecipients to verify whether they are or are not required to submit a Single Audit report. Furthermore, External Audit's review practice is to only forward findings to divisions if it determines the findings should be forwarded. Auditors identified one instance in which External Audit did not forward a finding specifically for the Formula Grants for Other Than Urbanized Areas Program to a division for review and follow up. External Audit also does not formally document Single Audit report issues or how those issues were resolved.

These issues increase the risk that the Department will not be able to determine whether subrecipients comply with federal law and whether subrecipients having issues is not detected through the subrecipients monitoring process.

Corrective Action:

Corrective action was taken.

Reference No. 10-93

Subrecipient Monitoring

Special Tests and Provisions - R3, Subrecipient Monitoring-Applicable to all Major Programs with Expenditures of ARRA Awards

CFDA 20.509 - Formula Grants for Other Than Urbanized Areas – ARRA

Award year - October 1, 2008 to September 30, 2009

Award number - TX-86-X001-01 and TX-86-X002-00

Type of finding - Significant Deficiency and Non-Compliance

The American Recovery and Reinvestment Act (ARRA) of 2009 required recipients to separately identify to each subrecipient--and document at the time of sub-award and at the time of disbursement of funds--the federal award number, Catalog of Federal Domestic Assistance (CFDA) number, and amount of ARRA funds. In addition, recipients must require their subrecipients to (1) agree to maintain records that identify adequately the source and application of ARRA awards; (2) separately identify to each subrecipient and document at the time of subaward and disbursement of funds, the federal award number, CFDA number, and amount of ARRA funds; and (3) provide identification of ARRA awards in their schedule of expenditures of federal awards (SEFA) and require subrecipients to do the same (Title 2, Code of Federal Regulations, Section 176.210). Recipients of ARRA awards also are required to ensure subrecipients that receive ARRA 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). This information is needed to allow the recipient to properly monitor subrecipient expenditures of ARRA funds and for oversight by the federal awarding agencies, offices of inspector general, and the Government Accountability Office.

Initial Year Written: 2009 Status: Partially Implemented U.S. Department of Transportation - Federal Transit Administration

The Department of Transportation (Department) did not consistently comply with ARRA requirements with respect to its subrecipients for the Formula Grants for Other Than Urbanized Areas program. Specifically:

- For all 45 ARRA project grant agreements tested, the Department did not notify the subrecipient of the federal award number at the time of the award. The Department's standard agreement for subrecipient awards did not contain the federal award number.
- For 39 (87 percent) of 45 ARRA project grant agreements tested, the Department did not notify the subrecipient at the time of award of the requirement that subrecipients provide identification of ARRA awards in their SEFAs. The Department executed the agreements prior to additional clarification from the U.S. Office of Management and Budget regarding ARRA requirements.
- For all five subrecipients who received ARRA disbursements during the fiscal year, the Department did not notify the subrecipient at the time of ARRA disbursement of the federal award number, CFDA number, amount of ARRA funds disbursed, requirement to maintain records that identify adequately

the source and application of ARRA awards, and provide identification of ARRA awards in their SEFAs.

The Department was not aware of the ARRA requirement for pre-award identification and disbursement notification at the time of the initial execution of the ARRA grant agreements because it executed ARRA grant agreements prior to guidance being established for ARRA disbursement requirements. During fiscal year 2009, the Department executed 47 ARRA project grant agreements and passed through \$982,277 to five ARRA subrecipients.

Recommendations:

The Department should:

- Ensure ARRA project grant agreements with subrecipients contain all of the required federal award information.
- Provide subrecipients all of the required federal award notifications at the time of each disbursement of ARRA funds.

Management Response and Corrective Action Plan 2009:

The Department agrees with the recommendations and has already taken some action to correct.

For new grant agreements the Code of Federal Domestic Assistance (CFDA) number, federal agency, federal grant numbers, and the SEFA requirements will be identified in the project grant agreements. For current grant agreements, amendments have been/will be processed adding missing information. Finally, the standard template for federally funded agreements will be amended, if needed, to include any missing required information. No federally funded grant agreement will be executed without the required information.

Staff will also update the billing reimbursement request form with the required information and provide subrecipients with the revised form. This may be done electronically for existing reimbursement forms already in use by the subrecipient, but will be included in any reimbursement forms not yet sent out. The subrecipient signature (required) on this form will serve as the notification.

Management Response and Corrective Action Plan 2010:

The Public Transportation Division (PTN) has corrected the agreement template to include all required federal information on the agreement forms as of 7/1/2010. PTN is working to modify all ARRA billing forms effective September 1, 2010 to include the required payment notification.

Implementation Date: September 1, 2010

Responsible Person: Eric Gleason

Appendix

Objectives, Scope, and Methodology

Objectives

With respect to the Highway Planning and Construction cluster of federal programs and the Airport Improvement 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 major programs audited.

Scope

The audit scope covered federal funds that the State spent for the Highway Planning and Construction cluster of federal programs and for the Airport Improvement Program from September 1, 2009, through August 31, 2010. Audit work included control and compliance work at the Department of Transportation (Department).

Methodology

The audit methodology included developing an understanding of controls over each compliance area that was direct and material to the Highway Planning and Construction cluster of federal programs and the Airport Improvement Program at the Department. Auditors conducted tests of compliance and of the controls identified for each compliance area and performed analytical procedures when appropriate.

Information collected and reviewed included the following:

- Department expenditure, procurement, reporting, cash revenue, required matching, program income, subrecipient, quality assurance testing, and project approval data.
- Federal notices of award and award proposals.
- Transactional support related to expenditures, procurement, and revenues.
- Department-generated reports and data used to support reports, revenues, and other compliance areas.
- Information system support for Department 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 of 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 Department'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.
- Department policies and procedures.

Project Information

Audit fieldwork was conducted from June 2010 through January 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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Department of Transportation

Members of the Texas Transportation Commission
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