



STATE OF NORTH CAROLINA

DEPARTMENT OF TRANSPORTATION

STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES

FOR THE YEAR ENDED JUNE 30, 2011

OFFICE OF THE STATE AUDITOR

BETH A. WOOD, CPA

STATE AUDITOR

DEPARTMENT OF TRANSPORTATION

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State Auditor

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AUDITOR'S TRANSMITTAL

The Honorable Beverly Eaves Perdue, Governor
Members of the North Carolina General Assembly
Mr. Eugene A. Conti, Jr., Secretary
Department of Transportation

We have completed certain audit procedures at the Department of Transportation related to the State of North Carolina reporting entity as presented in the *Single Audit Report* for the year ended June 30, 2011. Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*.

In the *Single Audit Report*, the State Auditor presents the results of tests of internal control and compliance with laws, regulations, contracts, and grants applicable to the State's major federal programs. Our audit procedures were conducted 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*.

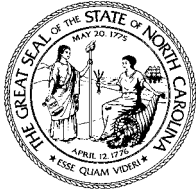
Our audit objective was to render an opinion on the State of North Carolina's, and not the Department's, administration of major federal programs. However, the report included herein is in relation to our audit scope at the Department and not to the State of North Carolina as a whole.

The audit findings referenced in the report are also evaluated to determine their impact on the State's internal control and the State's compliance with rules, regulations, contracts, and grants. If determined necessary in accordance with *Government Auditing Standards* or the OMB Circular A-133, these findings are reported in the State's *Single Audit Report*.

North Carolina General Statutes require the State Auditor to make audit reports available to the public. Copies of audit reports issued by the Office of the State Auditor may be obtained through one of the options listed in the back of this report.

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor



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**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133**

Mr. Eugene A. Conti, Jr., Secretary
and Management of the Department of Transportation

Compliance

As part of our audit of the State of North Carolina's compliance with the types of requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of its major programs for the year ended June 30, 2011, we have performed audit procedures at the Department of Transportation. Our report on the State of North Carolina's compliance with requirements that could have a direct and material effect on each major program and on internal control over compliance in accordance with OMB Circular A-133 is included in the State's *Single Audit Report*. Our federal compliance audit scope at the Department of Transportation included the following:

- Highway Planning and Construction Cluster
- Formula Grants for Other Than Urbanized Areas

The audit results described below are in relation to our audit scope at the Department and not to the State of North Carolina as a whole.

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 a major federal program occurred. An audit includes examining, on a test basis, evidence about 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 Department's compliance with those requirements.

**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONTINUED)**

The results of our audit procedures at the Department of Transportation disclosed an instance of noncompliance that is required to be reported in accordance with OMB Circular A-133 and which is described in finding 2 in the Audit Findings and Responses section of this report.

Internal Control Over Compliance

Management is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the 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 internal control over compliance.

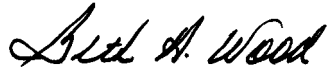
A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement 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. *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.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses, and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, we consider the deficiency described in finding 2 in the Audit Findings and Responses section of this report to be a material weakness in internal control over compliance, as defined above. Furthermore, we consider the deficiency described in finding 1 in the Audit Findings and Responses section of this report to be a significant deficiency in internal control over compliance, as defined above.

**REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONCLUDED)**

Management's responses to the findings identified in our audit are included in the Audit Findings and Responses section of this report. We did not audit the responses, and accordingly, we express no opinion on them.

This report is intended solely for the information and use of management, Secretary Conti, others within the entity, the Governor, the General Assembly, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



Beth A. Wood, CPA
State Auditor

March 9, 2012

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AUDIT FINDINGS AND RESPONSES

Matters Related to Federal Compliance Objectives

The following findings and recommendations were identified during the current audit and discuss conditions that represent deficiencies in internal control and/or noncompliance with laws, regulations, contracts, or grants.

1. MATERIALS PURCHASED FROM A NONCERTIFIED SUPPLIER

The Department did not ensure that materials used in contracts funded by the Highway Planning and Construction grant were purchased from approved suppliers. The failure to purchase from approved suppliers limits the Department's ability to ensure that materials used conform to the approved specifications.

We tested three of the 15 federally funded contracts that used emulsified asphalt, a binding agent for use in road construction, and found that one subcontractor had purchased this product from a plant that was not on the Department's approved supplier's list.

Title 23 CFR section 637.205 requires the Department to have a testing program for construction projects to ensure that materials and workmanship conform to approved plans and specifications. Before a supplier is added as an approved supplier for emulsified asphalt it is required to have an approved in-house Quality Control (QC) Asphalt Emulsion plan and an approved laboratory. The Department will review the QC Plan and perform an on-site inspection where it will be determined with reasonable assurance that the laboratory and its equipment and technicians are capable of complying with the standards. The technicians must also be certified by the Department's Materials and Tests Chemical Laboratory personnel for sampling and testing. If the supplier passes the certification process it will be added to the Department's public website as an Approved Producer/Supplier.

Federal Award Information: Highway Planning and Construction Grant 2011

Recommendation: The Department should ensure that it and its subcontractors are acquiring emulsified asphalt and all materials from suppliers that have been approved by the Department.

Agency Response: The Department agrees with this finding. In this particular case the producer who supplied the material was an approved producer but the plant was not an approved plant. To correct this in the future, the Minimum Sampling Guide will be changed to require that an Alternate ID is entered into our Highway Construction and Materials data base (HiCAMS). Because NCDOT requires Asphalt Emulsion suppliers to enter a unique batch number on each Bill of Lading, the batch number will serve as the Alternate ID. This will ensure that the Resident Engineer or staff member checks to make sure that the proper Bill of Lading has been submitted. This will also allow for a quick reference to verify testing information for the material.

AUDIT FINDINGS AND RESPONSES (CONCLUDED)

2. SUBRECIPIENTS NOT MONITORED IN ACCORDANCE WITH PLAN

The Department did not monitor its subrecipients in the time period required in its state management plan. The failure to conduct site visits increases the risk that the improper use of funds by subrecipients would not be detected.

The Department's state management plan states that each subrecipient will receive an on-site monitoring visit at least once every three years. Our review of the Department's list showing when site visits were performed revealed that 17 of the 85 subrecipients had not received a site visit in the last three years. No site visits were performed during the audit period while 68 on-site visits were conducted in 2010. Prior to 2010, the last on-site monitoring took place in 2005.

OMB Circular A-133 requires pass-through entities to monitor the activities of subrecipients as necessary to ensure that federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

Federal Award Information: NC-18-X028 FY 2009, NC-18-X032-00 FY 2010, NC-18-X034-00 FY 2011

Recommendation: The Department should ensure that monitoring site visits are being completed in accordance with the state plan.

Agency Response: The Public Transportation Division has developed a Professional Services 3-Year Work Plan that includes conducting compliance reviews of transit systems. This plan estimates the performance of thirty-one (31) subrecipient monitoring site visits of transit systems for each fiscal year 2012 through 2014 and will bring the Division into compliance with the state management plan and OMB Circular A-133.

ORDERING INFORMATION

Audit reports issued by the Office of the State Auditor can be obtained from the web site at www.ncauditor.net. Also, parties may register on the web site to receive automatic email notification whenever reports of interest are issued. Otherwise, copies of audit reports may be obtained by contacting the:

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