

# STATE OF NORTH CAROLINA

**DEPARTMENT OF TRANSPORTATION**

**RALEIGH, NORTH CAROLINA**

**STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES**

**FOR THE YEAR ENDED JUNE 30, 2013**

**OFFICE OF THE STATE AUDITOR**

**BETH A. WOOD, CPA**

**STATE AUDITOR**

**DEPARTMENT OF TRANSPORTATION**

**RALEIGH, NORTH CAROLINA**

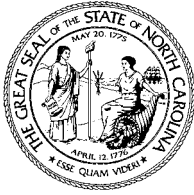
**STATEWIDE FEDERAL COMPLIANCE AUDIT PROCEDURES**

**FOR THE YEAR ENDED JUNE 30, 2013**

**ADMINISTRATIVE OFFICERS**

**ANTHONY J. TATA, SECRETARY**

**MARK L. FOSTER, CHIEF FINANCIAL OFFICER**



**Beth A. Wood, CPA**  
State Auditor

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**AUDITOR'S TRANSMITTAL**

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The Honorable Pat McCrory, Governor  
Members of the North Carolina General Assembly  
Anthony J. Tata, Secretary  
Department of Transportation

As part of our audit of the State of North Carolina's compliance with requirements applicable to its major federal programs, we have completed certain audit procedures at the Department of Transportation for the year ended June 30, 2013. Our audit was performed by authority of Article 5A of Chapter 147 of the *North Carolina General Statutes*. We conducted the audit 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 State Auditor expresses an opinion on the State's compliance with requirements applicable to its major federal programs in the State's *Single Audit Report*.

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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**INDEPENDENT AUDITOR'S 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**

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Anthony J. Tata, Secretary  
and Management of the Department of Transportation

Report on 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, 2013, 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:

- CFDA 20.205 Highway Planning and Construction Cluster
- CFDA 20.319 High-Speed Rail Corridors and Intercity Passenger Rail Service – Capital Assistance Grants
- CFDA 20.509 Formula Grants for Rural 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.

Management's Responsibility

Management is responsible for compliance with laws, regulations, contracts, and grants applicable to federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the State of North Carolina's major federal programs based on our audit of the types of compliance requirements

**INDEPENDENT AUDITOR'S 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)**

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referred to above, which we issue in the State's *Single Audit 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 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. However, our audit does not provide a legal determination of the Department's compliance with those requirements.

Opinion on Each Major Federal Program

As stated above, our opinion on compliance for each of the State of North Carolina's major federal programs is included in the State's *Single Audit Report*.

Other Matters

The results of our audit procedures at the Department of Transportation disclosed instances of noncompliance that are required to be reported in accordance with OMB Circular A-133 and which are described in findings 1, 3, 4, 7, 8, and 10 in the Audit Findings and Responses section of this report.

Report on Internal Control Over Compliance

Management is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered internal control over compliance with the types of requirements that could have a direct and material effect on a major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program 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

**INDEPENDENT AUDITOR'S REPORT ON  
COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND  
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IN ACCORDANCE WITH OMB CIRCULAR A-133 (CONCLUDED)**

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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 material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, we consider the deficiencies described in findings 1, 3, 4, 7, 8, and 10 in the Audit Findings and Responses section of this report to be material weaknesses in internal control over compliance. Furthermore, we consider the deficiencies described in findings 2, 5, 6, and 9 in the Audit Findings and Responses section of this report to be significant deficiencies in internal control over compliance.

Purpose of Report on Internal Control Over Compliance

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this communication is not suitable for any other purpose.

Management's Responses to Audit Findings

Management's responses to the findings identified in our audit are included in the Audit Findings and Responses section of this report. The responses were not subjected to the auditing procedures applied in the audit of compliance or consideration of internal control over compliance, and accordingly, we express no opinion on them.



Beth A. Wood, CPA  
State Auditor

Raleigh, North Carolina

March 14, 2014

## AUDIT FINDINGS AND RESPONSES

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### Matters Related to Federal Compliance Objectives

#### CFDA 20.205 HIGHWAY PLANNING AND CONSTRUCTION CLUSTER

##### 1. QUALITY ASSURANCE PROCEDURES NOT FOLLOWED

The Department of Transportation did not consistently perform its quality assurance procedures for testing concrete used to pave bridges. As a result, the Department did not comply with federal quality assurance requirements.

Federal regulations require the Department to follow an approved quality assurance program to validate the quality of the products used in highway construction. The Department's quality assurance program for concrete used in bridge paving requires that acceptance testing and independent assurance tests be conducted at specified intervals for all concrete used on a project. Both the acceptance tests and the assurance tests are to be executed by qualified sampling technicians and compression strength testers.

We tested 60 contracts for bridge concrete to determine if the Department followed its quality assurance procedures and noted the following:

- While the proper number of acceptance tests was performed, the Department did not meet its standards for independent assurance tests for 20 of the contracts. No independent assurance tests were conducted for 16 contracts, and in four additional cases the tests did not meet the Department's minimum requirements. Although the Department monitored to assess if the required number of independent assurance tests had been performed, they did not follow-up when the minimum number was not met.
- The Department did not have a formal policy defining what skills and training staff must have to be deemed a qualified compression strength tester. As a result the Department could not provide documentation to demonstrate that its 22 compression strength testers were qualified. In contrast, the Department requires sampling technicians to obtain a specific certification, and we found the Department had documentation that the certifications were attained for those in our test.

*Federal Award Information:* CFDA 20.205 Highway Planning and Construction Cluster 2013.

*Recommendation:* The Department should ensure the required number of independent assurance tests is performed. The Department should develop and implement procedures that clearly demonstrate personnel are qualified to perform concrete compression strength tests.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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*Department Response:* This finding is the result of transitioning to a new Independent Assurance Program in partnership with the North Carolina Federal Highway Administration (FHWA). In 2012, the Department designed a new approach that is allowed by the Code of Federal Regulations. FHWA encouraged the Department to pilot this approach before full implementation. In April 2013, the Department began the pilot and was to continue the previously FHWA approved approach. However, the approach in effect for fiscal 2013 was not always properly performed.

NCDOT received concurrence from FHWA to fully implement the new approach effective in January 2014. With this new approach, the Materials and Tests Unit has a technician who is responsible for monitoring all Independent Assurance activities and notifies the field employees and their management of the status of compliance through formal reports sent via email monthly (office specific) and quarterly (overall effectiveness). The target for calendar year 2014 is to assess 80 percent of all actively testing technicians.

The Department will institute a formal policy defining the expected training and qualifying laboratory technicians inclusive of the expected documentation process. In December 2013, a portion of the personnel (nine technicians) responsible for compressive strength testing received training and obtained the American Concrete Institute's Concrete Strength Testing Technician Level I certification. Another session will be held in March 2014 to certify ten of the remaining technicians. Others will be trained in the same fashion as needed. This exceeds the requirements of the CCRL for this particular test. Also, the five Materials and Tests Regional laboratories will obtain AMRL and CCRL accreditation by December 31, 2014. This will ensure that annual documentation of the testing protocol/procedure by each technician is maintained properly.

Anticipated Completion Date: Changes will be fully implemented by December 2014.

### 2. JUSTIFICATION FOR AWARDING CONTRACTS NOT DOCUMENTED

The Department of Transportation did not adequately document the rationale for awarding consultant contracts when the selected firms were not identified as the best qualified. As a result, there was an increased risk of noncompliance with federal procurement requirements.

We tested 45 contracts funded fully or partially with Highway Planning and Construction Cluster funds, which included 34 consultant contracts. We identified four consultant contracts awarded to firms that were not identified as the best qualified firm based on Department selection criteria. The total value of the four contracts was \$10 million, with current year federal expenditures of \$1.9 million.

For consultant contracts, the Department uses a centralized selection committee to evaluate and rank qualified firms based on past performance, applicable work experience, present workload, and other factors. Each committee member ranks the firms and then



## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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they meet to discuss the rankings and make a final selection. In most cases the top ranked firm will be awarded the contract, but if the committee makes a different selection, the rationale for the decision was not documented.

The OMB Circular A-133 Compliance Supplement requires states to use the same state policies and procedures they use for procurements from non-federal funds. *North Carolina General Statute* 143-64.31 requires state agencies to select firms qualified to provide services on the basis of demonstrated competence and qualification. The Department's internal "Policies and Procedures for Major or Specialized Service Contracts" requires that the results of the selection committee meeting be maintained.

*Federal Award Information:* CFDA 20.205 Highway Planning and Construction Cluster 2013. This finding also applies to CFDA 20.319 High Speed Rail Corridors and Intercity Passenger Rail Service – Capital Assistance Grants.

*Recommendation:* The Department should fully document the rationale for procurement decisions.

*Agency Response:* Since the audited period, a leadership change has been made in the Director of Technical Services position. The Department of Transportation will prepare formal documentation that summarizes the results of the selection committee meetings and outlines the rationale/justification of the selections.

Completion Date: March 1, 2014

### **CFDA 20.319 HIGH-SPEED RAIL CORRIDORS AND INTERCITY PASSENGER RAIL SERVICE - CAPITAL ASSISTANCE GRANTS**

#### 3. BUY AMERICAN PROVISIONS EXCLUDED FROM CONTRACT TERMS

The Department of Transportation did not ensure all the Buy-American provisions were included in its ARRA-funded contracts for the maintenance or repair of a public building. As a result the Department did not comply with this federal requirement and there is an increased risk that the manufactured goods used in these projects were not produced in the United States.

The Department awarded four ARRA-funded contracts, with a total contract value of \$6.6 million, to maintain or repair rail stations. None of the four contracts included the Buy-American provision for manufactured goods. Per Department personnel, the initial contracts that involved construction, alteration, maintenance, or repair only included a clause that the steel and iron products used for a project be produced in the United States. The Department did not update the standard contract provisions to include manufactured goods.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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Title 2 CFR section 176.140 requires a contract using ARRA funds for the construction, alteration, maintenance, or repairs of a public building or work include an award clause that all of the iron, steel, and manufactured goods used in the project be produced in the United States.

*Federal Award Information:* This finding affects funds administered under the American Recovery and Reinvestment Act award FR-HSR-0006-10-01 for the award period of May 24, 2010 – September 30, 2017.

*Recommendation:* The Department should update the standard contract language to include all Buy-American provisions.

*Department Response:* There were four contracts issued without the Buy American provision for rail station projects. As the Piedmont Improvement Program developed, with coordination between the Rail Division and Contract Standards and Development, all other contracts included the Buy American provision. Measures are in place to ensure the provision will be in all contracts going forward.

The Rail Division has informed the Federal Railroad Administration (FRA). A memo will be prepared outlining the affected projects and the approximate dollar values of the applicable materials per project. The memo will be copied to FRA's attention with a request for guidance on additional information and approval requirements.

Anticipated Completion Date: March 31, 2014

#### 4. FEDERAL REPORTS CONTAINED ERRORS

The Department of Transportation's federal reports for the High Speed Rail Corridors and Intercity Passenger Rail Service – Capital Assistance Grant did not include all activity of the reporting period, and the errors were not detected and corrected by the Department. Errors in federal reports reduce the usefulness of the data to users and may result in noncompliance with federal reporting requirements.

There are two quarterly reports for the grant. Both reports contain similar financial data and were prepared by a consulting firm hired by the Rail Division to provide program management and support. Division staff did not review the reports to ensure they were prepared in accordance with Department policy. We found the reports did not match each other nor did they contain the correct financial data for the reporting period. Specifically, we noted the following:

- The cumulative cash receipts amount reported in line 10(a) of the SF-425 for the quarter ended June 2013 was overstated by \$3.97 million.
- The cumulative cash disbursements amount reported in line 10(b) of the SF-425 for the quarter June 2013 was understated by \$5.38 million.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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- The cumulative federal share of expenditures reported in line 10(e) of the SF-425 for the quarter June 2013 was overstated \$1.89 million.
- The cumulative federal amount of ARRA expenditures reported in the 1512 report for the quarter ended June 2013 was understated by \$1.19 million.

The federal reports contained errors because the preparer was not aware of the Department's federal revenue and expenditure recognition policy or what accounting reports the Department uses to prepare federal reports.

The OMB Circular A-133 Compliance Supplement requires federal reports to include all activity of the reporting period, be supported by applicable accounting or performance records, and be fairly presented in accordance with governing requirements.

*Federal Award Information:* This finding affects funds administered under the American Recovery and Reinvestment Act award FR-HSR-0006-10-01 for the award period of May 24, 2010 – September 30, 2017.

*Recommendation:* The Department should ensure that federal reports are complete and accurate. Individuals responsible for preparing federal reports may need training on Department policy and what accounting system reports should be used to help determine the expenditures and revenues to be include in federal financial reports. Work to prepare the reports should be reviewed thoroughly prior to report submission.

*Department Response:* The difference in federal reports (OMB 1512 vs. SF-425) was due to timing issues and the Department's use of different financial reports capturing reimbursements during a given period of time. Due to the timing, OMB 1512 was created prior to the completion of the month-end closeout and the SF-425 was created after completion of the month-end closeout. The Rail Division has implemented a procedure to create monthly snapshots of information that will be archived for future reference. The Rail Division has implemented a procedure to utilize the Department's preferred query to help ensure federal reports are properly created.

Anticipated Completion Date: January 31, 2014

### 5. JUSTIFICATION FOR AWARDING CONTRACTS NOT DOCUMENTED

The Department of Transportation did not adequately document the rationale for awarding consultant contracts when the selected firms were not identified as the best qualified. As a result, there was an increased risk of noncompliance with federal procurement requirements.

We identified three out of 15 consultant contracts that were awarded to firms that were not identified as the best qualified firm based on Department selection criteria. The total value of the three contracts was \$1.3 million, with current year federal expenditures of \$1 million.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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For consultant contracts, the Department uses a centralized selection committee to evaluate and rank qualified firms based on past performance, applicable work experience, present workload, and other factors. Each committee member ranks the firms and then they meet to discuss the rankings and make a final selection. In most cases the top ranked firm will be awarded the contract, but if the committee makes a different selection, the rationale for the decision was not documented.

The OMB Circular A-133 Compliance Supplement requires states to use the same state policies and procedures they use for procurements from non-federal funds. *North Carolina General Statute* 143-64.31 requires state agencies to select firms qualified to provide services on the basis of demonstrated competence and qualification. The Department's internal "Policies and Procedures for Major or Specialized Service Contracts" requires that the results of the selection committee meeting be maintained.

*Federal Award Information:* This finding affects funds administered under the American Recovery and Reinvestment Act award FR-HSR-0006-10-01 for the award period of May 24, 2010 – September 30, 2017. This finding also applies to CFDA 20.205 Highway Planning and Construction Cluster.

*Recommendation:* The Department should fully document the rationale for procurement decisions.

*Department Response:* Since the audited period, a leadership change has been made in the Director of Technical Services position. The Department of Transportation will prepare formal documentation that summarizes the results of the selection committee meetings and describes the rationale/justification of the selections.

Completion Date: March 1, 2014

### 6. CERTIFIED PAYROLLS NOT OBTAINED

The Department of Transportation did not ensure contractors and subcontractors of the Rail Division's construction contracts submitted the required weekly certified payrolls. As a result, the Department did not comply with federal Davis-Bacon requirements. In addition, there was an increased risk that wages paid to laborers did not comply with the wage requirements.

We tested wage requirements for five construction contracts and 19 weeks of work. We noted that for two of the five contracts and seven of the 19 work weeks, the contractors and subcontractors did not submit all of the required certified payrolls. The two contracts noted as errors had a total value of \$3.3 million with current year federal expenditures of \$472,230, but it is unknown how much of this cost was related to contractors' and subcontractors' payroll.

The two errors were contracts monitored by the Rail Division. The Division did not follow Department procedures to accurately document the collection of the required

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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certified payrolls. In addition, the Department's standard documentation for identifying which certified payrolls had been received was often completed by a prime contractor and not a Division employee. There was no evidence the Division reviewed the documents prepared by the contractor or the certified payrolls to ensure laborers were paid the prevailing wage rates.

The OMB Circular A-133 Compliance Supplement requires that contractors and subcontractors submit to the state awarding agency a certified payroll for each week in which any contract work is performed. The awarding agency is to review the payrolls to ensure all laborers and mechanics employed by contractors and subcontractors to work on construction contracts in excess of \$2,000 are paid wages not less than those established for the locality of the project (prevailing wage rates) by the Department of Labor.

*Federal Award Information:* This finding affects funds administered under the American Recovery and Reinvestment Act award FR-HSR-0006-10-01 for the award period of May 24, 2010 – September 30, 2017.

*Recommendation:* The Department should ensure all certified payrolls are obtained and reviewed for compliance with federal regulations. In addition, management should ensure staff that oversee or coordinate construction projects are properly trained on how to document and execute the Department's designed procedures.

*Department Response:* The Rail Division will ensure certified payrolls for contractors and sub-contractors will be obtained and that the certified payrolls will be reviewed by a DOT employee.

Completion Date: March 1, 2014

### CFDA 20.509 FORMULA GRANT FOR RURAL AREAS

#### 7. SUBRECIPIENT MONITORING NOT ADEQUATELY PERFORMED

The Department of Transportation did not adequately monitor subrecipients of the Formula Grants for Rural Areas. As a result, the Department did not comply with federal monitoring requirements and there was an increased risk that noncompliance with federal requirements occurred at the subrecipient level and was not detected by the Department.

Our review of the Department's monitoring efforts identified the following deficiencies:

- The Department has not performed site visits to monitor subrecipients' fiscal operations and/or compliance with grant requirements since state fiscal year 2010. Department staff attended quarterly meetings of the subrecipients' Transportation Advisory Board where they conducted safety checks, evaluated the cleanliness of the environment and vehicles used in the program, and reviewed certain subrecipient policies. However, these procedures do not provide

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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reasonable assurance that subrecipients complied with all federal requirements, such as allowable costs, equipment maintenance, procurement requirements (including vehicle purchases and facility construction that comply with Buy-American, the Americans with Disability Act, and disadvantaged business enterprises participation), and accurate performance and financial reporting.

- The Department has not required all subrecipients to provide detailed documentation to support cost reimbursement claims. As a result, it did not consistently monitor subrecipient expenditures for allowable activities, allowable costs, or that the costs were true reimbursements. We identified 28 out of 67 subrecipient cost reimbursements that were approved by the Department without detailed documentation to support the expenditures. Department policy does not require subrecipients subject to an A-133 audit to provide supporting documentation for cost reimbursements. However, an A-133 audit does not assure the Rural Areas grant was subjected to testing by the auditor nor does it replace the federal requirement for the Department to conduct during-the-award monitoring. Submitting such documentation may not be necessary if the Department were to examine it during site visits.

The OMB Circular A-133 Compliance Supplement requires a pass-through entity monitor subrecipients to provide reasonable assurance that the federal awards are administered in compliance with laws, regulations, and the provisions of contract or grant agreement and that performance goals are achieved. The Department's State Management Plan says the Department will conduct on-site reviews of every subrecipient every three years to ensure compliance with federal and state regulations and agreements.

Similar aspects of this finding were reported in 2011.

*Federal Award Information:* This finding affects the Formula Grants for Rural Areas awards NC-18-X026-00 award period July 1, 2006 – December 31, 2007; NC-18-X028-00 award period July 1, 2008 – December 31, 2009; NC-18-X030-00 award period July 1, 2009 – December 31, 2010; NC-18-X030-01 award period July 1, 2010 – December 31, 2011; NC-18-X032-00 award period July 1, 2009 – December 31, 2010; NC-18-X034-00 award period July 1, 2010 – December 31, 2012; NC-18-X034-01 award period July 1, 2011 – December 31, 2012 and NC-18-X034-02 award period November 1, 2011 – June 30, 2013. The finding also affects funds administered under American Recovery and Reinvestment Act awards NC-86-X001-00 for the award period February 1, 2009 – December 31, 2012 and NC-86-X001-01 for the award period of October 9, 2009 – August 30, 2013.

*Recommendation:* The Department should perform monitoring procedures to ensure subrecipients administer federal awards in compliance with laws, regulations, and the provisions of contracts or grant agreements. Management should ensure monitoring procedures comply with the Department's State Management Plan.

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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*Department Response:* Recognizing that issues existed, there has been a change in the leadership position of the area. The Public Transportation Division is creating a plan to conduct on-site compliance reviews. The on-site reviews will include items to assist meeting A-133 audit requirements (including sampling the documentation that supports the invoices). In addition, all subrecipients will be required to attend a webinar to understand their legal responsibilities when receiving federal funds prior to future grant awards.

*Anticipated Completion Date:* Efforts are underway but cannot be fully accomplished in FY14 since it is late in the fiscal year. NCDOT anticipates being complete by December 2014.

### 8. SUBRECIPIENT DATA IN FEDERAL REPORTS NOT REVIEWED

The Department of Transportation did not ensure the subrecipient data in the Formula Grants for Rural Areas' annual financial and operating reports were complete and accurate. As a result, the Department did not comply with federal requirements and there was an increased risk that the federal reports contained errors that were not detected and corrected by the Department. Errors in federal reports reduce the usefulness of the data to the users and may result in noncompliance with federal reporting requirements.

The Department contracted with an external vendor to prepare the annual report using data supplied by subrecipients. The Department did not review the data supplied by the subrecipients for reasonableness and it did not review the vendor-prepared report prior to submitting it to the federal agency. We were able to agree the vendor-prepared report to subrecipient supplied data but were unable to verify the accuracy of the subrecipient data because the underlying support resides at the subrecipient. As noted in another finding, the Department has not performed on-site monitoring to verify the accuracy of subrecipient reports.

The OMB Circular A-133 Compliance Supplement and the federal reporting manual for the Rural Areas grant requires recipients to submit an annual report with financial and operating information. The state agency administering the grant is responsible for collecting data and submitting the report. The compliance supplement also requires recipients of federal awards to ensure federal reports include all activity of the reporting period, are supported by applicable accounting or performance records, and are fairly presented in accordance with program requirements.

*Federal Award Information:* This finding affects the Formula Grants for Rural Areas awards NC-18-X026-00 award period July 1, 2006 – December 31, 2007; NC-18-X028-00 award period July 1, 2008 – December 31, 2009; NC-18-X030-00 award period July 1, 2009 – December 31, 2010; NC-18-X030-01 award period July 1, 2010 – December 31, 2011; NC-18-X032-00 award period July 1, 2009 – December 31, 2010; NC-18-X034-00 award period July 1, 2010 – December 31, 2012; NC-18-X034-01 award period July 1, 2011 – December 31, 2012. The finding also affects funds administered

## AUDIT FINDINGS AND RESPONSES (CONTINUED)

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under American Recovery and Reinvestment Act awards NC-86-X001-00 for the award period February 1, 2009 – December 31, 2012 and NC-86-X001-01 for the award period of October 9, 2009 – August 30, 2013.

*Recommendation:* The Department should ensure the accuracy and completeness of the annual financial and operating reports. The subrecipient data supplied for the report should be monitored for accuracy and, prior to submission, the report should be reviewed for compliance with federal requirements.

*Department Response:* The results from a report from the Institute for Transportation Research and Education (ITRE) contained information that could not be reconciled to the DOT financials system and the local auditing process. Public Transportation will reinstitute a review process to ensure accurate data reporting inclusive of the operating data for federal compliance. The Deputy Director will approve the final financial data prior to submittal.

Anticipated Completion Date: Changes will be fully implemented by September 30, 2014.

### 9. REVIEW OF SUBRECIPIENT APPLICATIONS NOT ALWAYS DOCUMENTED

The Department of Transportation did not consistently document its review of subrecipient grant applications for allowable activities and subrecipient eligibility. As a result, there was an increased risk of awarding a grant for unallowable activities or to an ineligible subrecipient.

We identified five out of 18 subrecipients, a 28% error rate, for which the Department was unable to provide a completed application review checklist. Department policy is to complete a standard checklist to document the review of subrecipient applications to ensure allowable activities are approved and eligible recipients are awarded federal funds. Although completed checklists were not provided, our review of the applications found the five subrecipients were eligible and the applications proposed allowable activities.

*Federal Award Information:* This finding affects the Formula Grants for Rural Areas award NC-18-X034-02 for the award period of November 1, 2011 – June 30, 2013.

*Recommendation:* The Department should ensure subrecipient application reviews are consistently documented and maintained.

*Department Response:* In order to provide better electronic retention capability for future Application Checklists, they will be attached to the Partner Connect System. Once a grant application is reviewed and approved by the respective program managers, it will be attached to the grant award record.

The Program Manager will review that all information is complete in the process. Assistant Directors have also been charged with properly training the Mobility



## AUDIT FINDINGS AND RESPONSES (CONCLUDED)

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Development Specialists (MDS) and ensuring that all documentation can be found in Partner Connect and placed in the appropriate files.

Anticipated Completion Date: April 1, 2014

### 10. SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS NOT ACCURATE

The Department of Transportation did not accurately report the amount provided to subrecipients of the Formula Grants for Rural Areas on its Schedule of Expenditures of Federal Awards (SEFA). Errors in federal reports reduce the usefulness of the data to the users and may result in noncompliance with federal reporting requirements.

The subrecipient expenditures for the Formula Grants for Rural Areas funded by the American Recovery and Reinvestment Act were understated by \$3.6 million. The Department purchased security equipment for the benefit of and use by program subrecipients but did not include the costs in the SEFA as amounts provided to subrecipients.

OMB Circular A-133 requires a pass-through entity to identify in its SEFA the total amount provided to subrecipients (both cash and non-cash) from each federal award.

*Federal Award Information:* The finding affects funds administered under American Recovery and Reinvestment Act awards NC-86-X001-00 for the award period February 1, 2009 – December 31, 2012 and NC-86-X001-01 for the award period of October 9, 2009 – August 30, 2013.

*Recommendation:* The Department should ensure the SEFA is presented in accordance with federal guidelines.

*Department Response:* Cameras and security equipment were purchased by NCDOT purchase orders during the fiscal year for each subrecipient. This was an unusual situation but deemed a quicker solution in order to collectively purchase the items rather than each subrecipient procuring the items. The expense was not identified or communicated as subrecipient related cost. An adjusting entry has been made to correct the reporting of this purchase and new general ledger codes have been established for this type of activity.

Completion Date: March 1, 2014

## ORDERING INFORMATION

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Copies of this report may be obtained by contacting the:

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For additional information contact:

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