



John Keel, CPA
State Auditor

A Report on

**State of Texas Compliance with
Federal Requirements for the
National Guard Military
Construction Projects Program
for the Fiscal Year Ended
August 31, 2012**

February 2013

Report No. 13-024



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Overall Conclusion

The State of Texas complied in all material respects with the federal requirements for the National Guard Military Construction Projects Program in fiscal year 2012.

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 Single Audits. Those audits test compliance with federal requirements in up to 14 areas that may have a material effect on a federal program at those non-federal entities. Examples of the types of compliance areas include allowable costs, cash management, and reporting. The Single Audit for the State of Texas included (1) all high-risk federal programs for which the State expended more than \$75,562,558 in federal funds during fiscal year 2012 and (2) other selected federal programs.

From September 1, 2011, through August 31, 2012, the State of Texas expended \$50.2 billion in federal funds for federal programs and clusters of programs. The State Auditor's Office audited compliance with requirements for the National Guard Military Construction Projects Program at the Adjutant General's Department (Department), which spent \$31,855,987 in federal funds during fiscal year 2012.

National Guard Military Construction Projects Program

The National Guard Military Construction Projects Program provides funding for states through cooperative agreements to provide support to the Army National Guard and Air National Guard for the construction of military facilities, real property improvements, design services, and other projects authorized and directed by Congress or the U. S. Department of Defense.

Key Points

The Department complied in all material respects with the requirements tested for the National Guard Military Construction Projects Program. However, auditors identified certain significant deficiencies and non-compliance described below (see text box for definitions of finding classifications).

The Department did not always minimize the time between its drawdowns of federal funds and its disbursement of those funds. In addition, the Department did not calculate or monitor interest it earned on federal funds for which it did not

Finding Classifications

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

- A significant deficiency indicates control weaknesses, but those weaknesses would not likely result in material non-compliance.
- A material weakness indicates significant control weaknesses 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.

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

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

minimize the time between transfer from the U. S. Treasury and disbursement. It also did not remit the interest it earned on those funds to the federal government, as required.

The Department also did not always report complete and correct information in the financial reports it submitted to the federal government. Specifically, the Department did not report the amount of state matching funds it had provided on its request for advance or reimbursement reports. However, the Department identified state matching funds in the supporting documentation that accompanied those reports.

Auditors followed up on four findings from prior fiscal years for the National Guard Military Operations and Maintenance (O&M) Projects Program.

The Department fully implemented recommendations for one finding from a prior fiscal year and partially implemented recommendations for two findings from a prior fiscal year.

One finding from a prior fiscal year related to the American Recovery and Reinvestment Act (Recovery Act) was no longer valid because the Department had completed its construction projects funded by the Recovery Act prior to fiscal year 2012.

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 National Guard Military Construction Projects Program at the Department. Auditors did not identify significant control weaknesses related to the information technology systems reviewed.

Summary of Objectives, Scope, and Methodology

With respect to the National Guard Military Construction Projects 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 and grants that have a direct and material effect on the National Guard Military Construction Projects Program.

The audit scope covered federal funds that the State spent for the National Guard Military Construction Projects Program from September 1, 2011, through August 31, 2012. The 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 National Guard Military Construction Projects Program. Auditors conducted tests of compliance and of the controls identified for each compliance area and performed analytical procedures where appropriate. Auditors assessed the reliability of data the Department provided and determined that the data was reliable for the purposes of expressing an opinion on compliance with the provisions of laws, regulations, and contracts or grants that have a direct and material effect on the National Guard Military Construction Projects Program.

Contents

<i>Independent Auditor's Report</i>	1
<i>Schedule of Findings and Questioned Costs</i>	6
Section 1: Summary of Auditor's Results	7
Section 2: Financial Statement Findings	8
Section 3: Federal Award Findings and Questioned Costs	9
Adjutant General's Department	9
Summary Schedule of Prior Year Audit Findings	12
Adjutant General's Department	12
<i>Appendix</i>	
Objectives, Scope, and Methodology	18

Independent Auditor's Report

*State of Texas Compliance with
Federal Requirements for the
National Guard Military Construction
Projects Program
for the Fiscal Year Ended
August 31, 2012*

**Report on Compliance with Requirements that Could Have a Direct and Material Effect on
The National Guard Military Construction Projects Program and on
Internal Control Over Compliance in Accordance with
U.S. Office of Management and Budget Circular A-133
Independent Auditor's Report**

Compliance

We have audited the State of Texas's (State) compliance with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on the National Guard Military Construction Projects Program for the year ended August 31, 2012. Compliance with the requirements of laws, regulations, contracts, and grants applicable to the National Guard Military Construction Projects 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 the 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 National Guard Military Construction Projects Program occurred. An audit includes examining, on a test basis, evidence about the State's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the State's compliance with those requirements.

This audit was conducted as part of the State of Texas Statewide Single Audit for the year ended August 31, 2012. As such, the National Guard Military Construction Projects Program was selected as a major program based on the State of Texas as a whole for the year ended August 31, 2012. The State does not meet the OMB Circular A-133 requirements for a program-specific audit and the presentation of the Schedule of Federal 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.

In our opinion, the State complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on the National Guard Military Construction Projects Program for the year ended August 31, 2012. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as items:

Agency	Program	Compliance Requirement	Finding Number
Adjutant General's Department	CFDA 12.400 - National Guard Military Construction Projects Program	Cash Management	13-101
	CFDA 12.400 - National Guard Military Construction Projects Program	Reporting	13-102

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 National Guard Military Construction Projects Program. In planning and performing our audit, we considered the State's internal control over compliance with the requirements that could have a direct and material effect on the National Guard Military Construction Projects Program in order to determine our auditing procedures for the purposes 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.

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 compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of 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 the State's internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies. *A significant deficiency in internal control over compliance* is a deficiency, or a 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	Program	Compliance Requirement	Finding Number
Adjutant General's Department	CFDA 12.400 - National Guard Military Construction Projects Program	Cash Management	13-101
	CFDA 12.400 - National Guard Military Construction Projects Program	Reporting	13-102

Schedule of Federal Program Expenditures

The accompanying Schedule of Federal Program Expenditures for the National Guard Military Construction Projects Program of the State for the year ended August 31, 2012, 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, 2012*.

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

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

John Keel, CPA
State Auditor

February 21, 2013

**Schedule of Federal Program Expenditures for
 CFDA 12.400 - The National Guard Military Construction Projects Program
 For the State of Texas
 For the Year Ended August 31, 2012**

Schedule of Federal Program Expenditures	
Agency	Federal Direct Expenditures
Adjutant General's Department	\$31,855,987
Total for the National Guard Military Construction Projects Program	\$31,855,987
<p>Note 1: This schedule of federal program expenditures is presented for informational purposes only. For the State's complete Schedule of Expenditures of Federal Awards, see the <i>State of Texas Federal Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2012</i>.</p> <p>Note 2: The National Guard Military Construction Projects Program included only direct expenditures; no funds were passed through to non-state entities.</p>	

Schedule of Findings and Questioned Costs

*State of Texas Compliance with
Federal Requirements for the
National Guard Military Construction
Projects Program
for the Fiscal Year Ended
August 31, 2012*

Summary of Auditor's 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 Year Ended August 31, 2012*.

Federal Awards

Internal Control over major programs:

Material weakness(es) identified? No

Significant deficiency(ies) identified? Yes

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

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:

CFDA Number	Name of Federal Program or Cluster
12.400	National Guard Military Construction Projects Program

Dollar threshold used to distinguish between type A and type B programs: \$75,562,558

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 Year Ended August 31, 2012*.

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).

Adjutant General's Department

Reference No. 13-101

Cash Management

CFDA 12.400 – National Guard Military Construction Projects

Award Year – 2007

Award Numbers – W912L1-07-2-2001 and W912L1-07-2-2003

Type of finding – Significant Deficiency and Non-Compliance

Drawdowns and Disbursements of Federal Funds

A state must minimize the time between the drawdown of funds from the federal government and their disbursement for federal program purposes. The timing and amount of drawdowns must be as close as is administratively feasible to the state's actual cash outlays (Title 31, Code of Federal Regulations, Section 205.33(a)). When it uses an advance funding method, the state agrees to minimize the time elapsing between the drawdowns from the U.S. Treasury and their disbursement by the state. This period may not exceed 45 days (National Guard Regulation 5-1, Section 11-5(a)(5)).

Questioned Cost: \$ 538

U.S. Department of Defense

For 3 (25 percent) of 12 drawdowns tested that the Adjutant General's Department (Department) received on an advance basis, the Department did not minimize the time between its drawdowns of federal funds and its disbursement of those funds. As a result, the Department did not disburse \$1,514,671 within 45 days of its drawdown of those funds from the U.S. Treasury. The Department disbursed one of those drawdowns 51 days after it received those funds, and it had not disbursed the remaining two drawdowns as of August 31, 2012 (277 days after the Department received those funds). The Department asserted that it had not disbursed those funds because they were associated with final payments on construction projects, and the vendors had not yet completed all outstanding work on those projects. However, the Department does not have controls to monitor disbursements of federal funds to ensure that it makes disbursements within 45 days of receiving those funds.

Not minimizing the time between drawdowns of federal funds and the disbursement of those funds increases the risk that the Department could draw down federal funds from the U.S. Treasury in excess of its needs.

Interest Earned

National Guard Regulation (NGR) 5-1, Section 11-5(c)(1), states that the amount of interest due to the United States on funds advanced to a state or of interest due a state shall be determined and paid in accordance with Title 31, United States Code, Section 6503, Intergovernmental Financing, and regulations issued by the U.S. Department of Treasury and the U.S. Department of Defense. Additionally, the State may be accountable for interest earned on advances when it does not minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement of those funds (NGR 5-1, Section 11-5(c)(3)).

Except for interest earned on advances of funds exempt under the Intergovernmental Cooperation Act (Title 31, United States Code, Section 6501 et seq.) and the Indian Self-Determination Act (Title 23, United States Code, Section 450), grantees and subgrantees shall promptly, but at least quarterly, remit interest earned on advances to the federal agency. The grantee or subgrantee may keep interest amounts up to \$100 per year for administrative expenses (Title 32, Code of Federal Regulations, Section 33.21(i)).

ADJUTANT GENERAL'S DEPARTMENT

For the National Military Construction Projects program, the Department did not calculate or monitor interest it earned on federal funds for which it did not minimize the time between transfer from the U.S. Treasury and disbursement. It also did not remit the interest it earned on those funds. The Department has not established a process to calculate or monitor interest it earns on advanced federal funds when it does not disburse those funds in a timely manner. In fiscal year 2012, the Department earned a total of \$638 in interest on the advanced federal funds that it did not disburse in a timely manner. Specifically, the Department earned \$17 in interest associated with award W912L1-07-2-2001 and \$621 in interest associated with award W912L1-07-2-2003. As discussed above, grantees can retain interest of up to \$100 per year for administrative expenses; therefore, the Department should have remitted \$538 in earned interest to the U.S. Treasury for fiscal year 2012.

Recommendations:

The Department should:

- Establish and implement procedures to ensure that it minimizes the time between its drawdown of federal funds and the disbursement of those funds.
- Establish and implement procedures to calculate interest it earns on advanced federal funds and remit interest exceeding \$100 annually to the U.S. Department of Treasury on at least a quarterly basis.

Management Response and Corrective Action Plan:

Management agrees with the recommendation and will establish and implement procedures to ensure the time between the drawdown and the disbursement of funds is minimized. The department will establish and implement procedures to calculate and remit interest exceeding \$100 annually to the U.S. Department of Treasury.

Implementation Date: July 2013

Responsible Persons: Pamela Darden and Cathy Mann

Reference No. 13-102

Reporting

CFDA 12.400 – National Guard Military Construction Projects

Award year – 2009

Award number – W912L1-09-2-2001

Type of finding – Significant Deficiency and Non-Compliance

The Adjutant General's Department (Department) is required to submit Standard Form 270 "Request for Advance or Reimbursement" each time it requests payments or advances of federal funds from the National Guard Bureau (NGR 5-1, Chapter 11, Section 11-4). As part of its Standard Form 270 reports, the Department is required to report the non-federal share of its cash outlays for the period (Office of Management and Budget, Standard Form 270 and instructions).

Questioned Cost: \$ 0

U.S. Department of Defense

The Department did not report the amount of state matching funds (a form of non-federal cash outlay) on its Standard Form 270 reports during fiscal year 2012. During fiscal year 2012, the Department spent \$269,825 in state matching funds associated with work for the only appendix in the Department's master cooperative agreement for the National Guard Military Construction Projects program that required matching funds during fiscal year 2012. The Department's process for completing Standard Form 270 reports does not include reporting state matching funds. However, the Department identified state matching funds in the supporting documentation that accompanied its Standard Form 270 report.

ADJUTANT GENERAL'S DEPARTMENT

Recommendation:

The Department should report state matching funds on its Standard Form 270 reports.

Management Response and Corrective Action Plan:

Management agrees with the recommendation and will establish and implement procedures to report state matching funds on the Standard Form 270 reports.

Implementation Date: July 2013

Responsible Persons: Pamela Darden and Cathy Mann

Summary Schedule of Prior Year Audit Findings

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

- Each finding in the 2011 Schedule of Findings and Questioned Costs.
- Each finding in the 2011 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, 2012) has been prepared to address these responsibilities.

Adjutant General's Department

Reference No. 12-101

Cash Management

(Prior Audit Issue 10-01)

CFDA 12.401 - National Guard Military Operations and Maintenance Projects

Award year – October 1, 2010 to September 30, 2015

Award numbers – W912L1-11-2-1001 and W912L1-11-2-1007

Type of finding – Significant Deficiency and Non-Compliance

To the extent available, recipients shall disburse funds available from repayments to and interest earned on a revolving fund, program income, rebates, refunds, contract settlements, audit recoveries and interest earned on such funds before requesting additional cash payments (Title 2, Code of Federal Regulations, Section 215.22).

Initial Year Written: 2009
Status: Partially Implemented

U.S. Department of Defense

In addition, National Guard Regulation (NGR) 5-1, Chapter 11, Section 11-6, states that the amount the grantee requests for reimbursement will be reduced by the amount of program income received.

The Adjutant General's Department (Department) did not disburse program income prior to requesting advance funding or submitting reimbursement requests. The Department has established a process to separately account for and collect program income. However, program managers determine when to disburse program income; as a result, program income is often not disbursed until a purchase can be made entirely with available program income. This leads to the Department processing advance and reimbursement requests while program income is still available. Based on data the Department provided, the Department earned a total of \$28,950 in program income in fiscal year 2011. Department management also asserted that the Department had \$13,809 in available program income as of August 31, 2011.

Not disbursing program income prior to requesting federal funds results in the Department requesting more federal funds than it needs.

Recommendation:

The Department should disburse program income prior to requesting advance funding or submitting reimbursement requests.

ADJUTANT GENERAL'S DEPARTMENT

Management Response and Corrective Action Plan 2011:

Management agrees with the recommendation and, to the extent possible, the department will disburse program income prior to requesting advance funding or submitting reimbursement requests. The department is developing written policies and procedure to address the reporting and disbursement of program income.

Management Response and Corrective Action Plan 2012:

Management agrees with the recommendation and, to the extent possible, the department will disburse program income prior to requesting advance funding or submitting reimbursement requests. The department has coordinated with the United States Property & Fiscal Officer (USPFO) to develop a written policy and procedure to address the reporting and disbursement of program income. The procedures are effective for Federal Fiscal Year 2013.

The intent is that the Program Manager (PM) will assign expenditures to the Program Income fund and vendor payments will be made directly from the fund. The result will be reported on the SF270 monthly.

Implementation Date: October 2012

Responsible Person: Cathy Mann

Reference No. 12-102

Davis-Bacon Act

CFDA 12.401 - National Guard Military Operations and Maintenance Projects - ARRA
Award year – July 24, 2009 to September 30, 2010
Award number – W912L1-09-2-9036 (ARRA)
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). All projects funded in whole or in part by the American Recovery and Reinvestment Act of 2009 (Recovery Act) are required to comply with Davis-Bacon Act requirements (Title 2, Code of Federal Regulations (CFR), Section 176, Subpart C).

Initial Year Written: 2011 Status: No Longer Valid U.S. Department of Defense

Non-federal entities shall include in their construction contracts 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's regulations (Title 29, 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).

For one construction project funded by the Recovery Act in fiscal year 2011, the Adjutant General's Department (Department) did not require either of its two contractors to submit certified weekly payrolls. This construction project was the Department's only Recovery Act-funded construction project during fiscal year 2011, and it was completed in June 2011. The standard contract language the Department uses requires the contractor to make the records available for Department review, but the contract does not specifically require contractors and subcontractors to submit weekly certified payrolls to the Department. Additionally, the Department did not request to review any certified payrolls from the two contractors during fiscal year 2011. Department payments in this program for contracts subject to the Davis-Bacon Act totaled \$2,794,912 for fiscal year 2011. In

the absence of certified weekly payrolls, the Department was unable to ensure that its contractors paid laborers and mechanics wages established by the DOL.

Corrective Action:

The Department has completed its American Recovery and Reinvestment Act-funded construction projects. Therefore, this finding is no longer valid.

Reference No. 12-103

Reporting

CFDA 12.401 - National Guard Military Operations and Maintenance Projects
CFDA 12.401 - National Guard Military Operations and Maintenance Projects - ARRA
Award years – see below
Award numbers – see below
Type of finding – Significant Deficiency and Non-Compliance

The Adjutant General's Department (Department) is required to submit Standard Form 270 (SF 270) "Request for Advance or Reimbursement" each time it requests payments or advances of federal funds from the National Guard Bureau (NGR 5-1, Chapter 11, Section 11-4). Program income is reported upon reimbursement or liquidation of advance payment vouchers as soon as such income is considered "received" pursuant to state accounting procedures (NGR 5-1, Chapter 11, Section 11-6).

Initial Year Written: 2011
Status: Partially Implemented
U.S. Department of Defense

The Department did not report program income on its SF 270 reports during fiscal year 2011. The Department's process for completing SF 270 reports does not include reporting program income. Only two appendices in the Department's master cooperative agreement describe earning program income: appendix 1 and appendix 7. The Department earned a total of \$28,950 in program income in fiscal year 2011. As a result of not reporting program income on its SF 270 reports, Department expenditures were not reviewed for allowability by the U.S. property and fiscal officer.

The Department also did not report the amount of state matching funds on its SF 270 reports during fiscal year 2011. The Department's process for completing SF 270 reports does not include reporting state matching funds. However, state matching funds are clearly identified in the reports that accompany the SF 270 reports. As a result of the Department's not reporting state matching amounts on the SF 270 reports, those reports were not complete.

Additionally, the Department reported amounts on its SF 270 reports that were not supported by information from its accounting system, the Uniform Statewide Accounting System (USAS), and its subledger system (the Integrated Engineering Management System or IEMS). While the Department used expenditure data from IEMS to determine the "federal share now requested" and attached that support to the SF 270 reports it submitted, it did not use accounting data to complete other lines on its SF 270 reports. Instead, the Department entered other information on the reports based on prior reports or calculations. Specifically, the Department determined its "federal payments previously requested" by recording the total program outlays from the prior month's SF-270 report, and it determined its "total program outlays to date" by adding its current expenditures to the "federal payments previously requested" line of the SF 270 report.

Reporting amounts that are not supported by financial records increases the risk that those amounts could be incorrect.

ADJUTANT GENERAL'S DEPARTMENT

The issues discussed above affected the following awards:

<u>Award Numbers</u>	<u>Award Years</u>
W912L1-11-2-1000 (MCA)	October 1, 2010 to September 30, 2015
W912L1-11-2-1001 (Appendix 1)	October 1, 2010 to September 30, 2015
W912L1-11-2-1002 (Appendix 2)	October 1, 2010 to September 30, 2015
W912L1-11-2-1003 (Appendix 3)	October 1, 2010 to September 30, 2015
W912L1-11-2-1004 (Appendix 4)	October 1, 2010 to September 30, 2015
W912L1-11-2-1005 (Appendix 5)	October 1, 2010 to September 30, 2015
W912L1-11-2-1007 (Appendix 7)	October 1, 2010 to September 30, 2015
W912L1-11-2-1010 (Appendix 10)	October 1, 2010 to September 30, 2015
W912L1-11-2-1014 (Appendix 14)	October 1, 2010 to September 30, 2015
W912L1-11-2-1021 (Appendix 21)	October 1, 2010 to September 30, 2015
W912L1-11-2-1022 (Appendix 22)	October 1, 2010 to September 30, 2015
W912L1-11-2-1023 (Appendix 23)	October 1, 2010 to September 30, 2015
W912L1-11-2-1024 (Appendix 24)	October 1, 2010 to September 30, 2015
W912L1-11-2-1040 (Appendix 40)	October 1, 2010 to September 30, 2015
W912L1-10-2-3053 (RSMS)	October 1, 2009 to September 30, 2015
W912L1-07-2-3061 (ALERRT)	September 25, 2007 to September 30, 2011
W912L1-09-2-9036 (ARRA)	July 24, 2009 to September 30, 2010

Recommendations:

The Department should:

- Report program income on advance funding or reimbursement requests.
- Report state matching funds on advance funding or reimbursement requests.
- Ensure amounts it reports on the SF 270 reports agree to accounting records that support its financial statements and Schedule of Expenditures of Federal Awards, and include this supporting documentation for each part of the SF 270 report in the packet it submits to the U. S. property and fiscal officer to enhance the review and approval process.

Management Response and Corrective Action Plan 2011:

Management agrees with the recommendations and will start reporting available information on the SF270 related to program income and state match. The department is currently in the process of developing written policies and procedures related to the utilization of program income received, the information that will be included on the SF270, and the support and reconciliation documentation needed to fully support all entries on each SF270 submitted for advances and/or reimbursements.

The department will coordinate a process with the U.S. Property and Fiscal Office to enhance the review and approval process of requests.

Management Response and Corrective Action Plan 2012:

Management agrees with the recommendation and, to the extent possible, the department will disburse program income prior to requesting advance funding or submitting reimbursement requests. The department has coordinated with the United States Property & Fiscal Officer (USPFO) to develop a written policy and procedure to address the reporting and disbursement of program income. The procedures are effective for Federal Fiscal Year 2013.

The intent is that the Program Manager (PM) will assign expenditures to the Program Income fund and vendor payments will be made directly from the fund. The result will be reported on the SF270 monthly.

Implementation Date: October 2012

Responsible Person: Cathy Mann

Reference No. 10-03

**Procurement and Suspension and Debarment
Allowable Costs/Cost Principles**

CFDA 12.401 - National Guard Military Operations and Maintenance Projects

Award years - see below

Award numbers - see below

Type of finding - Significant Deficiency and Non-Compliance

Procurement and Suspension and Debarment

National Guard Regulation (NGR) 5-1, Section 3-10, states that acquisition of goods and services in performance of the cooperative agreement shall be according to state contracting procedures per Title 32, Code of Federal Regulations (CFR), Section 33.36, which states the following:

Initial Year Written: 2009
Status: Implemented

U.S. Department of Defense

- When procuring property and services under a grant, a state will follow the same policies and procedures it uses for procurements from its non-federal funds.
- Grantees will maintain records sufficient to detail the significant history of a procurement. These records will include, but are not limited to, rationale for the method of procurement, selection of contract type, contractor selection or rejection, and the basis for the contract price.

State procurement guidelines include the following:

- Texas Government Code, Section 2155.132 (e), requires competitive bidding, whether formal or informal, for a purchase by a state agency if the purchase exceeds \$5,000 and is made under a written contract.
- The Texas Comptroller of Public Accounts' *The State of Texas Procurement Manual*, Section 2-28, states that, for procurements that are not subject to alternate procurement methods and are for estimated purchases of \$5,000 to \$25,000, agencies must obtain at least three informal bids, two of which must be from vendors certified as historically underutilized business (HUB) by the State.
- The Department's *Purchasing Guide* requires that purchases between \$5,000 and \$25,000 must obtain three informal verbal bids. Agencies must use the Centralized Master Bidders List (CMBL) to locate vendors who service the specific highway district for the specified class and item number. Two (2) bids must be solicited from certified HUB program. If it will enhance competition, the agency may add non-CMBL vendors to the final bid list, but written approval from the head of the agency is required to supplement non-CMBL vendors.

ADJUTANT GENERAL'S DEPARTMENT

The Department did not consistently follow requirements for competitive bidding and retain justification for purchases when there were fewer than three bidders. Auditors identified the following during testing:

- Three closely related purchases that were individually under \$5,000 should have been combined for a total purchase of \$5,930 and, therefore, should have been subject to competitive bidding. Although the purchases were submitted on the same day and for the same service, they were assigned consecutive purchase order numbers, and the Department's purchasers did not require that the purchases be combined and competitively bid.
- For one \$14,948.28 purchase, purchasers did not ensure that the requester obtained at least three bids from the CMBL and HUB vendors, and they did not include documentation to explain the procurement method.
- For one \$127,178 purchase, purchasers did not retain adequate documentation in the procurement file, including documentation for a comparison of vendors' qualifications or for use of the CMBL.

These issues occurred because of a lack of oversight by the Department's purchasing staff and lack of a structured system for monitoring procurement and contracting documents. The issues affected the following awards:

<u>Award Numbers</u>	<u>Award Years</u>
DAHA41-04-2-1000 (MCA)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1001 (Appendix 1)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1002 (Appendix 2)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1003 (Appendix 3)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1004 (Appendix 4)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1005 (Appendix 5)	October 1, 2003 -September 30, 2009
DAHA41-04-2-1007 (Appendix 7)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1014 (Appendix 14)	October 1, 2003 -September 30, 2009
DAHA41-04-2-1021 (Appendix 21)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1022 (Appendix 22)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1023 (Appendix 23)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1024 (Appendix 24)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1028 (Appendix 28)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1040 (Appendix 40)	October 1, 2003 - September 30, 2009
DAHA41-04-2-1010 (Appendix 10)	October 1, 2005 - September 30, 2009
W912L1-04-2-3034 (RSMS)	February 25, 2005 - September 30, 2009
W912L1-05-2-3055 (Geospatial)	September 15, 2005 - September 30, 2009
W912L1-06-2-3059 (Peace Prairie)	March 9, 2007 - June 30, 2009
W912L1-07-2-3061 (ALERT)	September 25, 2007 - March 31, 2010
W912L1-08-2-3070 (JBOT)	October 1, 2008 - March 31, 2010

Corrective Action:

Corrective action was taken.

Appendix

Objectives, Scope, and Methodology

Objectives

With respect to the National Guard Military Construction Projects 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 and grants that have a direct and material effect on the National Guard Military Construction Projects Program.

Scope

The audit scope covered federal funds that the State spent for the National Guard Military Construction Projects Program from September 1, 2011, through August 31, 2012. The audit work included control and compliance work at the Adjutant General's Department (Department).

Methodology

The audit methodology included developing an understanding of controls over each compliance area that was material to the National Guard Military Construction Projects Program. Auditors selected non-statistical samples for tests of compliance and controls for each compliance area identified based on the American Institute of Certified Public Accountants' audit guide entitled *Government Auditing Standards and Circular A-133 Audits* dated February 1, 2012. In determining the sample sizes for control and compliance test work, auditors assessed risk levels for inherent risk of noncompliance, control risk of noncompliance, risk of material noncompliance, detection risk, and audit risk of noncompliance by compliance requirement. Auditors selected samples primarily through random selection designed to be representative of the population. In those cases, results may be extrapolated to the population but the accuracy of the extrapolation cannot be measured. In some cases, auditors may use professional judgment to select additional items for compliance testing. Those sample items generally are not representative of the population and, therefore, it would not be appropriate to extrapolate those results to the population. Auditors conducted tests of compliance and of the controls identified for each compliance area and performed analytical procedures where appropriate. Auditors assessed the reliability of data the Department provided and determined that the data was reliable for the purposes of expressing an opinion on compliance with the provisions of laws, regulations, and contracts or grants that have a direct and material effect on the National Guard Military Construction Projects Program.

Information collected and reviewed included the following:

- Department data on expenditures, procurement, reporting, cash revenue, and required matching funds.
- 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 performed on expenditure data to identify instances of non-compliance.
- Compliance testing for samples of transactions for each direct and material compliance area.
- Tests of design and effectiveness of key controls and tests of design of other 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.
- U. S. Office of Management and Budget Circulars A-87, A-102, and A-133.
- National Guard regulations.
- Federal notices of award and award proposals.
- Department policies and procedures.

Project Information

Audit fieldwork was conducted from June 2012 through December 2012. 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:

- Audrey O'Neill, CIA, CGAP (Project Manager)
- Jennifer Brantley, MS, CPA (Assistant Project Manager)
- Michael F. Boehme, CIA, PHR
- Cheryl Durkop
- Rebecca Franklin, CFE, CGAP, CISA, CICA
- Joseph Mungai, CIA, CISA
- Namita Pai, CPA
- Kristin Alexander, CIA, CFE, MBA (Quality Control Reviewer)
- James Timberlake, CIA (Audit Manager)

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The Honorable Joe Straus III, Speaker of the House, Joint Chair

The Honorable Thomas “Tommy” Williams, Senate Finance Committee

The Honorable Jim Pitts, House Appropriations Committee

The Honorable Harvey Hilderbran, House Ways and Means Committee

Office of the Governor

The Honorable Rick Perry, Governor

Adjutant General’s Department

Major General John F. Nichols, Adjutant General



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