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State Auditor

A Report on

**State of Texas Compliance with
Federal Requirements for
Selected Major Programs at the
Water Development Board for
the Fiscal Year Ended
August 31, 2013**

February 2014
Report No. 14-023



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Overall Conclusion

The State of Texas complied in all material respects with the federal requirements for the Capitalization Grants for Clean Water State Revolving Funds Program (Clean Water Program) and the Capitalization Grants for Drinking Water State Revolving Funds Program (Drinking Water Program) in fiscal year 2013.

As a condition of receiving federal funding, U.S. Office of Management and Budget (OMB) Circular A-133 requires non-federal entities that expend at least \$500,000 in federal awards in a fiscal year to obtain annual Single Audits. Those audits test compliance with federal requirements in 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 monitoring of non-state entities (subrecipients) to which the State passes federal funds. The requirements for 1 of those 14 areas vary by federal program and outline special tests that auditors are required to perform, such as requirements related to environmental reviews and financial commitments that the Water Development Board (Board) is required to make to its subrecipients. The Single Audit for the State of Texas included (1) all high-risk federal programs for which the State expended more than \$73,222,469 in federal funds during fiscal year 2013 and (2) other selected federal programs.

From September 1, 2012, through August 31, 2013, the State of Texas expended \$48.6 billion in federal funds. The State Auditor's Office audited compliance with requirements for the Clean Water Program and the Drinking Water Program at the Board, which spent \$67.8 million in federal Clean Water Program funds and \$44.3 million in federal Drinking Water Program funds during fiscal year 2013.

The Capitalization Grants for Clean Water State Revolving Funds Program

The Capitalization Grants for Clean Water State Revolving Funds Program (Clean Water Program), which is administered by the U.S. Environmental Protection Agency, provides states with a long-term source of financing for construction of wastewater treatment facilities and implementation of other water quality management activities.

The Capitalization Grants for Drinking Water State Revolving Funds Program

The Capitalization Grants for Drinking Water State Revolving Funds Program (Drinking Water Program), which is administered by the U.S. Environmental Protection Agency, provides states with a long-term source of financing to cover the costs of drinking water infrastructure.

Key Points

The Board complied in all material respects with requirements for the Clean Water Program and the Drinking Water Program.

Although auditors identified findings at the Board, it is important to note that no finding was material to the federal programs audited. While that indicates that the State of Texas complied in all material respects with the requirements tested, the Board should correct the following non-compliance and significant deficiencies (see text box for definitions of finding classifications):

- The Board did not maintain adequate user access controls for its Labor Distribution system. That issue affected both the Clean Water Program and the Drinking Water Program.
- For the Clean Water Program, the Board did not always communicate required award information to subrecipients at the time of the award.

In addition, the Board fully implemented recommendations for all five findings from the prior fiscal year related to the Clean Water Program, the Drinking Water Program, and the Severe Repetitive Loss Program.

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.

Summary of Management's Response

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

Summary of Information Technology Review

The audit work included a review of general and application controls for key information technology systems related to the Clean Water Program and the Drinking Water Program. As noted above, auditors identified a weakness related to access controls for the Board's Labor Distribution system.

Summary of Objectives, Scope, and Methodology

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

The audit scope covered federal funds that the State spent for the Clean Water Program and the Drinking Water Program at the Board from September 1, 2012, through August 31, 2013. The audit work included control and compliance tests at the Board.

The audit methodology included developing an understanding of controls over each compliance area that was direct and material to the Clean Water Program and the Drinking Water Program. Auditors' sampling methodology was based on the American Institute of Certified Public Accountants' audit guide entitled *Government Auditing Standards and Circular A-133 Audits* dated February 1, 2013. Auditors conducted tests of compliance and of controls identified for each direct and material compliance area and performed analytical procedures when appropriate. Auditors assessed the reliability of data the Board provided and determined that the data was sufficiently reliable for the purposes of expressing an opinion on compliance with the provisions of laws, regulations, and contracts or grants that have a direct and material effect on the programs identified above.

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Independent Auditor's Report

*State of Texas Compliance with
Federal Requirements for
Selected Major Programs at the
Water Development Board
for the Fiscal Year Ended
August 31, 2013*

Report on Compliance for the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program, and Report on Internal Control Over Compliance Required by OMB Circular A-133

Independent Auditor's Report

The Honorable Rick Perry, Governor
The Honorable David Dewhurst, Lieutenant Governor
The Honorable Joe Straus, Speaker of the House of Representatives
and
Members of the Legislature, State of Texas

Report on Compliance for the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program

We have audited the State of Texas's (State) compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program for the year ended August 31, 2013. The State's major federal programs at the Water Development Board are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

Our responsibility is to express an opinion on the State's compliance for the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program based on our audit of the types of compliance requirements referred to above. Except as discussed in the following paragraph, we conducted our audit of compliance in accordance with auditing standards generally accepted in the United State of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program occurred. An audit includes examining, on a test basis, evidence about the State's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

This audit was conducted as part of the State of Texas Statewide Single Audit for the year ended August 31, 2013. As such, the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program were selected as major programs based on the State of Texas as a whole for the year ended August 31, 2013. 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.

We believe that our audit provides a reasonable basis for our opinion on compliance for the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program. However, our audit does not provide a legal determination of the State's compliance.

Opinion on the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program

In our opinion, the State complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program for the year ended August 31, 2013.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance, 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
Water Development Board	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds	Subrecipient Monitoring	2013-196

Our opinion on the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program is not modified with respect to these matters.

The State's response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The State's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Report on Internal Control Over Compliance

Management of the State 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 the State's internal control over compliance with the types of requirements that could have a direct and material effect on the

Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds 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 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 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 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. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we consider the following deficiencies in internal control over compliance, as described in the accompanying schedule of findings and questioned costs, to be significant deficiencies:

Agency	Program	Compliance Requirement	Finding Number
Water Development Board	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds	Allowable Costs/Cost Principles	2013-195
	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds - ARRA		
	CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds		
	CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds - ARRA		
	CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds	Subrecipient Monitoring	2013-196

The State's response to the internal control over compliance findings identified in our audit is described in the accompanying schedule of findings and questioned costs. The State's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

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 report is not suitable for any other purposes.

Schedule of Federal Program Expenditures

The accompanying Schedule of Federal Program Expenditures for the Capitalization Grants for Clean Water State Revolving Funds Program and the Capitalization Grants for Drinking Water State Revolving Funds Program of the State for the year ended August 31, 2013, 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, 2013*.

John Keel, CPA
State Auditor

February 21, 2014

**Schedule of Federal Program Expenditures for
The Capitalization Grants for Clean Water State Revolving Funds Program and
The Capitalization Grants for Drinking Water State Revolving Funds Program
For the State of Texas
For the Year Ended August 31, 2013**

Schedule of Federal Program Expenditures CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds Program			
Agency	Federal Pass-through to Non-state Entity	Federal Direct Expenditures	Totals
Water Development Board			
Other than American Recovery and Reinvestment Act	\$24,221,099	\$37,742,621	\$61,963,720
American Recovery and Reinvestment Act	4,111,047	1,746,185	5,857,232
Totals for Capitalization Grants for Clean Water State Revolving Funds Program	\$28,332,146	\$39,488,806	\$67,820,952
<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, 2013</i>.</p>			

Schedule of Federal Program Expenditures CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds Program			
Agency	Federal Pass-through to Non-state Entity	Federal Direct Expenditures	Totals
Water Development Board			
Other than American Recovery and Reinvestment Act	\$35,362,044	\$3,067,478	\$38,429,522
American Recovery and Reinvestment Act	5,537,138	304,178	5,841,316
Totals for Capitalization Grants for Drinking Water State Revolving Funds Program	\$40,899,182	\$3,371,656	\$44,270,838
<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, 2013</i>.</p> <p>Note 2: Federal expenditures for the Capitalization Grants for Drinking Water State Revolving Funds Program at state entities not included in the scope of this audit totaled \$7,640,479 for the year ended August 31, 2013.</p>			

Schedule of Findings and Questioned Costs

*State of Texas Compliance with
Federal Requirements for
Selected Major Programs at the
Water Development Board
for the Fiscal Year Ended
August 31, 2013*

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, 2013*.

Federal Awards

Internal Control over major programs:

Material weakness(es) identified? No

Significant deficiency(ies) identified? Yes

Major programs with Significant Deficiencies:

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

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

Unmodified:

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

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
66.458	Capitalization Grants for Clean Water State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds

Dollar threshold used to distinguish between type A
and type B programs: \$73,222,469

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, 2013*.

Section 3:

Federal Award Findings and Questioned Costs

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

Water Development Board

Reference No. 2013-195

Allowable Costs/Cost Principles

CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds

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

Award years - October 1, 2008 to August 31, 2014; June 6, 2011 to August 31, 2015; and September 5, 2012 to August 31, 2016

Award numbers - 2W-96692401 (ARRA), CS-48000211, and CS-48000212

CFDA 66.468 - Capitalization Grants for Drinking Water State Revolving Funds

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

Award years - February 1, 2009 to August 31, 2014; January 1, 2008 to December 31, 2014; September 1, 2008 to August 31, 2014; September 1, 2010 to August 31, 2015; September 1, 2011 to August 31, 2016; and September 1, 2012 to August 31, 2016

Award numbers - 2F-96692301 (ARRA), FS-99679511, FS-99679512, FS-99679514, FS-99679515, and FS-99679516

Type of finding - Significant Deficiency

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

Questioned Cost: \$ 0
U.S. Environmental Protection Agency

The Water Development Board (Board) did not maintain adequate user access controls over its Labor Distribution system. Specifically, one employee had access rights as a high-level system administrator and as a system programmer, and that employee also had the ability to move programming changes into the production environment of the Labor Distribution system. A lack of segregation of duties in system access and allowing programmers to migrate code to the production environment increases the risk of inappropriate changes to systems.

Recommendation:

The Board should segregate the responsibilities for administrative tasks from programming tasks, and segregate the responsibilities for programming code from migrating code to the production environment.

Management Response and Corrective Action Plan:

Management concurs and has, beginning November 1, 2013, segregated the above referenced duties between three different individuals, as follows:

- *The programmer programs the code;*
- *The database administrator moves the code to production; and,*
- *The systems analyst performs system administrative duties.*

WATER DEVELOPMENT BOARD

Implementation Date: *November 1, 2013*

Responsible Person: *Wendy Brown*

Reference No. 2013-196

Subrecipient Monitoring

CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds

Award year - September 5, 2012 to August 31, 2016

Award number - CS-48000212

Type of finding - Significant Deficiency and Non-Compliance

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

Questioned Cost: \$ 0

U.S. Environmental Protection Agency

For 1 (13 percent) of 8 subrecipients tested, the Board communicated an incorrect CFDA title and number to the subrecipient at the time of the subaward commitment. The Board provided documentation that it correctly identified the project in its internal documentation, but it could not provide evidence that it communicated the correct CFDA title and number to the subrecipient. Inadequate identification of federal awards could lead to improper reporting of federal funding on a subrecipient's schedule of expenditures of federal awards.

Recommendation:

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

Management Response and Corrective Action Plan:

The Board agrees with the need to accurately communicate the subrecipient's CFDA title and number. Management believes the incorrect CFDA title and number referenced above to be an isolated incident which was mainly caused by staff not using the appropriate agency template. As a corrective action plan, management has enhanced its quality control procedures by re-emphasizing (to staff) the need to utilize the appropriate template when issuing an award letter. In addition, management has stressed the need to take additional care in ensuring the accuracy of the CFDA title and number.

Implementation Date: *January 22, 2014*

Responsible Person: *Carleton Wilkes*

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 2012 Schedule of Findings and Questioned Costs.
- Each finding in the 2012 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, 2013) has been prepared to address these responsibilities.

Water Development Board

Reference No. 13-180

Allowable Costs/Cost Principles

CFDA 66.458 – Capitalization Grants for Clean Water State Revolving Funds

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

Award years - October 1, 2009 to August 31, 2014; June 6, 2011 to August 31, 2015; and October 1, 2008 to August 31, 2014

Award numbers - CS-48000210, CS-48000211, and 2W-96692401

CFDA 66.468 – Capitalization Grants for Drinking Water State Revolving Funds

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

Award years – September 20, 2006 to September 15, 2013; January 1, 2008 to December 31, 2014; September 1, 2009 to August 31, 2014; September 1, 2010 to August 31, 2015; September 1, 2011 to August 31, 2016; and February 1, 2009 to August 31, 2014

Award numbers – FS-99679510, FS-99679511, FS-99679513, FS-99679514, FS-99679515, and 2F-96692301

Type of finding – Significant Deficiency

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

The Water Development Board (Board) has not implemented adequate logical access controls for its automated timekeeping system, the electronic Time Sheet Solution (eTSS). This increases the risk of unauthorized system access and could result in the compromise of data.

Initial Year Written: 2012
Status: Implemented

U.S. Environmental Protection
Agency

Corrective Action:

Corrective action was taken.

Reference No. 13-181

Reporting

CFDA 66.458 - Capitalization Grants for Clean Water State Revolving Funds

Award year – June 6, 2011 to August 31, 2015

Award number – CS-48000211

Type of finding – Significant Deficiency and Non-Compliance

Transparency Act Reporting

The Federal Funding Accountability and Transparency Act (FFATA) requires prime recipients of federal awards made on or after October 1, 2010, to capture and report subaward and executive compensation data regarding first-tier subawards that exceed \$25,000. A subaward is defined as a legal instrument to provide support for the performance of any portion of the substantive project or program for which a recipient received a grant or cooperative agreement award and that is awarded to an eligible subrecipient (Title 2, Code of Federal Regulations (CFR), Chapter 170).

Initial Year Written: 2012 Status: Implemented

U.S. Environmental Protection Agency

Additionally, recipients must report all required elements established in the Office of Management and Budget's *Open Government Directive- Federal Spending Transparency and Subaward and Compensation Data Reporting* (August 27, 2010), Appendix C, including the subaward date, subawardee Dun and Bradstreet Data Universal Numbering System (DUNS) number, amount of subaward, subaward obligation or action date, date of report submission, and subaward number.

For 1 (14 percent) of 7 subaward projects tested for which the Water Development Board (Board) was required to submit FFATA reports, the Board did not accurately report the subaward number. That occurred because of a data input error that occurred when the Board entered the information into the FFATA Subaward Reporting System (FSRS).

The Board did not have a control, such as a review prior to submission, to ensure that all information it reported in FSRS was accurate.

Additionally, the Board performs a reconciliation to ensure that all subawards that require reports are identified; however, it did not perform that reconciliation on a monthly basis, as required by its procedures. Performing those reconciliations on a monthly basis could help to ensure compliance with the requirement to report subaward information through FSRS by the end of the month following the month in which the subaward was signed. Although auditors did not identify compliance issues regarding the timeliness of reports during testing, not reconciling subaward information increases the risk that the Board may not submit all required reports in a timely manner.

Reporting inaccurate information to FSRS decreases the reliability of information provided to the awarding agency and other intended users of that information.

Corrective Action:

Corrective action was taken.

Reference No. 13-182

Procurement and Suspension and Debarment

Subrecipient Monitoring

(Prior Audit Issue 12-191)

CFDA 66.468 – Capitalization Grants for Drinking Water State Revolving Funds

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

Award years – September 20, 2006 to September 15, 2013; January 1, 2008 to December 31, 2014; September 1, 2009 to August 31, 2014; September 1, 2010 to August 31, 2015; September 1, 2011 to August 31, 2016; and February 1, 2009 to August 31, 2014

Award numbers – FS-99679510, FS-96679511, FS-99679513, FS-99679514, FS-99679515, and 2F-96692301

Type of finding – Significant Deficiency and Non-Compliance

Subrecipient Suspension and Debarment

Federal rules require that, when a non-federal entity enters into a covered transaction with an entity at a lower tier, the non-federal entity must verify that the entity is not suspended or debarred or otherwise excluded from federal contracts. This verification may be accomplished by checking the Excluded Parties List System (EPLS), collecting a certification from the entity, or adding a clause or condition to the covered transaction with that entity (Title 2, Code of Federal Regulations (CFR), Section 180.300).

Covered transactions include procurement contracts for goods and services awarded under a nonprocurement transaction that are expected to equal or exceed \$25,000 (Title 2, CFR, Section 180.220) and all nonprocurement transactions (i.e., subawards to subrecipients) irrespective of award amount (Title 2, CFR, Section 180.210).

Initial Year Written: 2011
Status: Implemented

U.S. Environmental Protection Agency

For 1 (8 percent) of 13 subrecipients tested, the Water Development Board (Board) could not provide evidence that the subrecipient had certified that it was not suspended or debarred. The Board asserted that, although it received the certification form from the subrecipient, it did not retain the form due to a manual error. Auditors determined that the subrecipient was not currently suspended or debarred by checking the EPLS.

When the Board does not maintain evidence of its verification that subrecipients are not suspended or debarred, this increases the risk that it could enter into an agreement with a subrecipient that is not eligible to receive federal funding.

Award Identification

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

The Board was unable to provide evidence that it communicated the CFDA number and other required information to 1 (8 percent) of 13 subrecipients tested. Although the Board sent an award letter to the subrecipient at the time of commitment, that letter did not contain the CFDA title and number or the award name and number. The Board asserted it changed the award letter template in fiscal year 2011 to include the CFDA title and number and the award name and number and that it sent an award letter to that subrecipient prior to making those changes. Auditors did not identify similar errors for awards tested after the beginning of fiscal year 2011.

Inadequate identification of federal awards could lead to improper reporting of federal funding on a subrecipient's schedule of expenditures of federal awards.

During-the-award Monitoring

As a pass-through entity, the Board is required by OMB Circular A-133, Subpart D, Section 400(d), to monitor the activities of subrecipients to ensure that federal awards are used in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.

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

The Board conducts monthly onsite inspections of subrecipients to monitor compliance with requirements related to projects in the construction phase. Based on the Board's policy, individuals in its Inspection and Field Support Division conduct those inspections, and a team lead in that division reviews the inspection reports.

For 3 (23 percent) of 13 subrecipients tested, the Board was unable to provide evidence that a team lead reviewed inspection reports. The Board asserted that, due to limitations in its Inspection and Field Support Services database, the Board did not consistently require review of inspection reports when the inspection was conducted by a field office manager or team lead. Although this lack of review increases the risk that the Board may not detect subrecipient non-compliance with federal requirements, auditors identified no compliance issues regarding the Board's inspection activities for the subrecipients tested.

Corrective Action:

Corrective action was taken.

Reference No. 13-183

Reporting

CFDA 97.110 – Severe Repetitive Loss Program

Award years – September 12, 2011 to February 28, 2015 and June 25, 2012 to June 24, 2015

Award numbers – EMT-2011-SR-0002 and EMT-2012-SR-0001

Type of finding – Significant Deficiency and Non-Compliance

Transparency Act Reporting

The Federal Funding Accountability and Transparency Act (FFATA) requires prime recipients of federal awards made on or after October 1, 2010, to capture and report subaward and executive compensation data regarding first-tier subawards that exceed \$25,000. A subaward is defined as a legal instrument to provide support for the performance of any portion of the substantive project or program for which a recipient received a grant or cooperative agreement award and that is awarded to an eligible subrecipient (Title 2, Code of Federal Regulations, Chapter 170).

Initial Year Written: 2012 Status: Implemented U.S. Department of Homeland Security

Additionally, recipients must report all required elements established in the Office of Management and Budget's *Open Government Directive- Federal Spending Transparency and Subaward and Compensation Data Reporting* (August 27, 2010), Appendix C, including the subaward date, subawardee Dun and Bradstreet Data Universal Numbering System (DUNS) number, amount of subaward, subaward obligation or action date, date of report submission, and subaward number.

The Water Development Board (Board) did not always submit reports to the FFATA Subaward Reporting System (FSRS) in a complete and timely manner as required. Specifically:

- For 1 (14 percent) of 7 subaward projects tested for which the Board was required to submit reports, the Board did not submit the required report to FSRS. Although the Board correctly identified that a FFATA report was required for that project, it did not have a control to ensure that it submitted the required report.
- For all 6 subaward projects tested for which the Board did submit FFATA reports to FSRS, the Board did not submit the reports within the required time frame. Specifically, the Board submitted those reports between 8

and 99 days late. Those errors occurred because the Board did not have a control to ensure that it submitted reports within the required time frame.

In addition, while auditors identified no compliance issues regarding the accuracy of required reports during testing, the Board did not have a formal, documented control to ensure that all information it reported in FSRS was accurate.

Not submitting all required reports to FSRS in a complete and timely manner decreases the reliability and availability of information provided to the awarding agency and other users of that information.

Corrective Action:

Corrective action was taken.

Reference No. 13-184

Subrecipient Monitoring

CFDA 97.110 – Severe Repetitive Loss Program

Award years – September 11, 2008 to September 10, 2013; September 8, 2009 to May 13, 2013; and September 12, 2011 to February 28, 2015

Award numbers – EMT-2008-SR-0001, EMT-2009-SR-0002, and EMT-2011-SR-0002

Type of finding – Significant Deficiency and Non-Compliance

Subrecipient Audits

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

Initial Year Written: 2012 Status: Implemented U.S. Department of Homeland Security

The Board did not effectively monitor or enforce subrecipient compliance with the requirement to obtain Single Audits. Prior to August 2012, the Board did not have a process to determine whether subrecipients for the Severe Repetitive Loss Program were subject to Single Audit requirements; therefore, it did not review those subrecipients' Single Audit reports. After auditors inquired about the Board's process for reviewing those subrecipients' Single Audits reports, the Board began monitoring those subrecipients' compliance with the requirement to obtain a Single Audit.

For 5 (63 percent) of 8 subrecipients tested, the Board completed its review of the subrecipients' Single Audit reports between August 28, 2012, and August 29, 2012. For all five of those subrecipients, the Single Audit reports (or the subrecipients' certification that no audit was required) were provided to the Board more than nine months after the end of the subrecipients' fiscal years. The Board had previously reviewed the Single Audit reports for the remaining three subrecipients tested because those subrecipients received federal funds for other programs the Board administers.

Not ensuring that subrecipients obtain Single Audits and not following up on deficiencies noted in subrecipients' Single Audit reports increases the risk that deficiencies could go unaddressed.

During-the-award Monitoring

OMB Circular A-133, Subpart D, Section 400(d), requires the Board to monitor the activities of subrecipients 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. Pass-through entities must ensure that subrecipients conform substantially to the same standards of timing and amount that apply to cash advances by federal agencies (Title 44, Code of Federal Regulations (CFR), Section 13.37 (a)(4)). Additionally, grantees and subgrantees must 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 44, CFR, Section 13.21(i)).

For all three subrecipients tested that received advances of federal funds, the Board did not monitor the interest the subrecipients earned. The Board has not established a process to monitor subrecipients that may be required to return interest or to ensure that subrecipients remit interest in a timely manner. As a result, the Board drew funds on an advance basis for subrecipients, but it did not determine whether interest associated with those advances was due.

When the Board does not monitor interest earned on advances of federal funds to subrecipients, that increases the risk that subrecipients may not remit interest as required.

Corrective Action:

Corrective action was taken.

Appendix

Objectives, Scope, and Methodology

Objectives

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

Scope

The audit scope covered federal funds that the State spent for the Clean Water Program and the Drinking Water Program at the Water Development Board (Board) from September 1, 2012, through August 31, 2013. The audit work included control and compliance tests at the Board.

Methodology

The audit methodology included developing an understanding of controls over each compliance area that was direct and material to the Clean Water Program and the Drinking Water Program.

Auditors selected non-statistical samples for tests of compliance and controls for each direct and material compliance area based on the American Institute of Certified Public Accountants' audit guide entitled *Government Auditing Standards and Circular A-133 Audits* dated February 1, 2013. In determining 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 used professional judgment to select additional items for compliance testing. Those sample items generally are not representative of the population and, therefore, it would be inappropriate to extrapolate those results to the population.

Auditors conducted tests of compliance and of controls identified for each direct and material compliance area and performed analytical procedures when appropriate.

Auditors assessed the reliability of data the Board provided and determined that the data was sufficiently reliable for the purposes of expressing an opinion on compliance with the provisions of laws, regulations, and contracts or grants that have a direct and material effect on the Clean Water Program and Drinking Water Program.

Information collected and reviewed included the following:

- Board data for expenditures, procurement, reporting, cash revenue, required matching funds, program income, and subrecipients.
- Federal notices of award and award proposals.
- Transactional support related to expenditures, procurement, and revenues.
- Board-generated reports and data used to support reports, revenues, and other compliance areas.
- Information system support for Board assertions related to general controls over information systems that support the control structure related to federal compliance.

Procedures and tests conducted included the following:

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

Criteria used included the following:

- The Code of Federal Regulations.
- United States Code.
- U.S. Office of Management and Budget Circulars A-87, A-102, and A-133.
- The American Recovery and Reinvestment Act.
- The Federal Funding Accountability and Transparency Act.
- Federal notices of award and award proposals.

- Federal agency circulars, handbooks, and guidance.
- Board policies and procedures.

Project Information

Audit fieldwork was conducted from August 2013 through December 2013. Except as discussed above in the Independent Auditor's Report, we conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations.

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

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The Honorable Harvey Hilderbran, House Ways and Means Committee

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Water Development Board

Members of the Water Development Board

Mr. Carlos Rubinstein, Chairman

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