# MANAGEMENT CONTROLS, FINANCIAL MANAGEMENT SYSTEMS, AND COMPLIANCE WITH LAWS AND REGULATIONS

## FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT

The Federal Managers' Financial Integrity Act (FMFIA) requires agencies to conduct an annual evaluation of its management controls and financial systems and report the results to the President and Congress. The Secretary of Transportation then prepares an annual Statement of Assurance based on these internal evaluations.

The Secretary of Transportation's qualified Statement of Assurance for FY 2005 is included in the Message from the Secretary located at the beginning of this Report. The Department evaluated its management control systems and financial management systems for the fiscal year ending September 30, 2005. This evaluation formed the basis of the Secretary's Statement of Assurance for FY 2005.

### FMFIA ANNUAL ASSURANCE PROCESS

The FMFIA review is an agency self-assessment of the adequacy of financial controls in all areas of the Department's operations—program, administrative, and financial management.

| OBJECTIVES OF CONTROL MECHANISMS |
| --- |
| 1. Financial and other resources are safeguarded from unauthorized use or disposition.<br>2. Transactions are executed in accordance with authorizations.<br>3. Records and reports are reliable.<br>4. Applicable laws, regulations, and policies are observed.<br>5. Resources are efficiently and effectively managed.<br>6. Financial systems conform to government-wide standards. |

Managers within the Department, being in the best position to know and understand the nature of the problems they face, establish appropriate control mechanisms to ensure Departmental resources are sufficiently protected from fraud, waste, and abuse, and to meet the intent and requirements of the FMFIA.

The head of each Operating Administration and Departmental office submits an annual statement of assurance representing the overall adequacy and effectiveness of management controls within the organization to the Department's Office of Financial Management. FMFIA material weakness and material nonconformances are also reported, citing milestones and/or accomplishments. Specific guidance for completing the end of fiscal year assurance statement and reporting on material deficiencies is issued annually by the Department's Office of Financial Management.

## CRITERIA FOR REPORTING MATERIAL WEAKNESSES AND NONCONFORMANCES

A material weakness under FMFIA must fall into one or more of the categories below plus merit the attention of the Executive Office of the President and/or the relevant Congressional oversight committees.

| CRITERIA FOR REPORTING A MATERIAL WEAKNESS |
|---|
| 1. Significant weakness of the safeguards (controls) against waste, loss, unauthorized use or misappropriation of funds, property, or other assets.<br>2. Violates statutory authority, or results in a conflict of interest.<br>3. Deprives the public of significant services, or seriously affects safety or the environment.<br>4. Impairs significantly the fulfillment of the agency's mission.<br>5. Would result in significant adverse effects on the credibility of the agency. |

A material nonconformance under FMFIA must fall into one or more of the categories below plus merit the attention of the Executive Office of the President or the relevant Congressional oversight committees.

| CRITERIA FOR REPORTING A MATERIAL NONCONFORMANCE |
|---|
| 1. Prevent the primary accounting system from centrally controlling financial transactions and resource balances.<br>2. Prevent compliance of the primary accounting system, subsidiary system, or program system under the Office of Management and Budget Circular A-127. |

## SUMMARY OF FY 2005 FMFIA MATERIAL WEAKNESSES

### Status of Internal Controls—FMFIA, Section 2

DOT has three material weaknesses. Two of the material weaknesses—HTF financial reporting and Highway grants management—were carryovers from FY 2004. FAA financial reporting is a new material weakness. The three material weaknesses are:

HTF Agencies' Financial Management and Reporting Activities. Since the audit of the FY 2003 HTF financial statements, we reported that material deficiencies existed in internal controls over financial management and reporting activities in the HTF agencies. While FHWA began making organizational and procedural improvements during FY 2005, many of the improvements were initiated too late in the year and were not in effect for sufficient time to overcome the accounting problems that existed in prior years. In addition, extraordinary efforts were again needed to prepare the HTF financial statements during the year and at September 30, 2005. The remaining deficiencies to be overcome include (1) financial statement preparation and analysis, (2) resolving reconciliation differences during the year, (3) implementing managerial cost accounting, (4) tracking intragovernmental transactions, and (5) linking the FACTS II reporting to the financial statement preparation process.

FINANCIAL OVERSIGHT OF HIGHWAY GRANTS. Last year we reported that FHWA and the FTA needed to establish stronger financial and cost controls to better ensure that grant funds are protected from fraud, waste, and abuse. FHWA and FTA have both implemented improved procedures and controls over grants during FY 2005. For example, FHWA initiated the Financial Integrity Review and Evaluation (FIRE) program in March 2005, and FTA instituted sufficient improvements in its oversight of transit grants to not be included in the material weakness this year. However, FHWA needs to continue to improve its financial oversight of highway grants.

TIMELY PROCESSING OF FAA TRANSACTIONS AND RECONCILIATION OF ACCOUNTS. Last year, FAA faced problems implementing Delphi and a new procurement system. During FY 2005, the problems became more severe and adversely affected FAA's ability to process transactions and reconcile accounting balances in a timely manner. FAA needs to improve processes and controls to ensure that property plant and equipment is consistently and accurately capitalized, obligations are recorded in a timely manner, reconciliations of Fund balances with Treasury and suspense accounts are timely, abnormal balances in budgetary to proprietary account relationships are investigated, and subsidiary systems and supporting documentation are reconciled to general ledger balances. Consequently, FAA's interim financial statements were not reliable and FAA needed to make adjustments totaling $2.1 billion to the draft FY 2005 financial statements in order to make them reliable. FAA is committed to correcting the problems in early FY 2006.

The following table shows the Department's progress during the past five years with correcting and closing material weaknesses.

| DEPARTMENT OF TRANSPORTATION<br>STATISTICAL SUMMARY OF PERFORMANCE<br>SECTION 2, INTERNAL CONTROLS | | | |
|---|---|---|---|
| | NUMBER OF MATERIAL WEAKNESSES | | |
| | NUMBER OF REPORTED<br>FOR THE FIRST TIME IN: | FOR THAT YEAR,NUMBER THAT HAVE<br>BEEN CORRECTED: | FOR THAT YEAR,<br>NUMBER STILL PENDING: |
| 1999 Report | 1<br>FAA Property, Plant and Equipment | 0 | 0 |
| 2000 Report | 0<br>FAA Property, Plant and Equipment (R) | 0 | 0 |
| 2001 Report | 1<br>FAA Property, Plant and Equipment (R)<br>Information Security Program | 0 | 0 |
| 2002 Report | 2<br>Information Security Program (R)<br>FTA Management<br>FAA Contracts | 1<br>FAA Property, Plant and Equipment | 0 |
| 2003 Report | 2<br>Information Security Program (R)<br>FAA Contracts (R)<br>HTF Financial Mgmt.<br>Reconciling Transactions (Eliminations) | 1<br>FTA Management | 1<br>HTF Financial Management |
| 2004 Report | 2<br>HTF Financial Mgmt. (R)<br>Reconciling Transactions (Eliminations) (R)<br>HTF Grants<br>Financial System Controls | 2<br>Information Security Program<br>FAA Contracts | 1<br>HTF Grants |
| 2005 Report | 1<br>HTF Financial Mgmt. (R)<br>HTF Grants (R)<br>FAA Reconciliations | 2<br>Reconciling Transactions<br>Financial System Controls | 1<br>FAA Reconciliations |
| 1999 –2005 Total | 9 | 6 | 3 |

Of the total number corrected, how many were corrected in 2005 __2__; (R) - Repeat

### Status of financial management systems FMFIA, Section 4

One material nonconformance from FY 2004—financial system controls—was downgraded to a reportable condition in FY 2005. DOT reported again this year that the Department was not in substantial compliance with OMB Circular A-127. For FY 2005 this noncompliance consists of three issues: Preparation of financial statements; Use of a Standard General Ledger (credit reform/loans); and Federal Accounting Standards (cost accounting).

| DEPARTMENT OF TRANSPORTATION<br>STATISTICAL SUMMARY OF PERFORMANCE<br>SECTION 4, FINANCIAL MANAGEMENT SYSTEMS | | | |
|---|---|---|---|
| NUMBER OF MATERIAL NONCONFORMANCES | | | |
| | NUMBER OF REPORTED<br>FOR THE FIRST TIME IN: | FOR THAT YEAR,NUMBER THAT HAVE<br>BEEN CORRECTED: | FOR THAT YEAR,<br>NUMBER STILL PENDING: |
| 1999 Report | 0 | 0 | 0 |
| 2000 Report | 1<br>FFMIA Nonconformance<br>1.a. Preparation of Financial Statements<br>1.b. Standard General Ledger<br>1.c. Managerial Cost Accounting | 0 | 1<br>FFMIA Nonconformance<br>1.a. Preparation of Financial Statements<br>1.b. Standard General Ledger<br>1.c. Managerial Cost Accounting |
| 2001 Report | 1<br>Information Security Program<br>FFMIA Nonconformance (R) | 0 | 0 |
| 2002 Report | 0<br>Information Security Program (R)<br>FFMIA Nonconformance (R) | 0 | 0 |
| 2003 Report | 0<br>FFMIA Nonconformance (R) | 1<br>Information Security Program | 0 |
| 2004 Report | 1<br>Financial System Controls<br>FFMIA Nonconformance (R) | 0 | 0 |
| 2005 Report | 0<br>FFMIA Nonconformance (R) | 1<br>Financial System Controls | 0 |
| 1999 –2005 Total | 3 | 2 | 1 |
| Of the total number corrected, how many were corrected in 2005 1 ; (R) - Repeat | | | |

## FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT

The Federal Financial Management Improvement Act of 1996 (FFMIA) requires that agencies' financial management systems provide reliable financial data in accordance with generally accepted accounting principles and standards. Under FFMIA, financial management systems must substantially comply with three requirements: Federal financial management system requirements; applicable Federal accounting standards; and the U.S. Government Standard General Ledger (SGL). In addition, agencies must determine annually whether their systems meet these requirements. This determination is to be made no later than 120 days after the earlier of (a) the date of receipt of the agency-wide audited financial statement, or (b) the last day of the fiscal year following the year covered by such statement.

To assess conformance with FFMIA, the Department uses OMB Circular A-127 survey results, FFMIA implementation guidance issued by OMB, results of OIG and GAO audit reports, annual financial statement audits, the Department's annual Federal Information Security Management Act (FISMA) Report, and other relevant information. The Department's assessment also relies a great deal upon evaluations and assurances under the FMFIA, with particular importance attached to any reported material weaknesses and material nonconformances.

## FFMIA OF 1996 NONCOMPLIANCE ISSUES

In FY 2005, DOT reported that the Department was not in compliance with FFMIA. For FY 2005, this noncompliance consists of three issues: preparation of financial statements, use of Standard General Ledger, and Federal Accounting Standards (cost accounting).

PREPARATION OF FINANCIAL STATEMENTS. The process used by FHWA and FAA, including utilization of the Delphi accounting system, was not adequate to prepare reliable and timely financial statements during the year or at September 30, 2005. Several adjustments were made to correct system processing errors, record activities not recorded at the transaction level, and correct discrepancies with the data reflected in subsidiary systems. FAA system conversion issues contributed to problems in recording all Delphi transactions, which interfered with FAA's ability to produce accurate and complete financial and budgetary reports.

FFMIA requires agencies to produce auditable financial statements based on data from it financial systems on a timely basis.

USE OF STANDARD GENERAL LEDGER. HTF Agencies have not consistently used Delphi for routine accounting events at the transaction level to meet OMB and Treasury reporting requirements.

FEDERAL ACCOUNTING STANDARDS. HTF Agencies were not in full compliance with the SFFAS No. 4 Managerial Cost Accounting Concepts and Standards for the Federal Government and the related provisions of the Government Performance and Results Act (GPRA). The FY 2005 financial statements did not properly reflect full costs or measure the effectiveness of the Agencies' programs.

## FEDERAL INFORMATION SECURITY MANAGEMENT ACT

FISMA requires Federal agencies to identify and provide security protections commensurate with the risk and magnitude of harm resulting from the loss of, misuse of, unauthorized access to, or modification of information collected or maintained by or on behalf of the agency. DOT maintains one of the largest portfolios of information technology (IT) systems among Federal civilian agencies; it is therefore essential that the Department protect these systems, along with their sensitive data. In FY 2005, DOT's IT budget totaled about $2.7 billion.

For FISMA, the Inspector General's office tested a representative subset of DOT systems, including contractor-operated or -maintained systems that had undergone systems security certification reviews in order to determine whether DOT had complied with Government standards for (1) assessing system risks, (2) identifying security requirements, (3) testing security controls, and (4) accrediting systems as able to support business operations.

The IG identified that DOT needs to better manage corrections of system security deficiencies and that FAA needs to take aggressive actions to enhance the air traffic control systems security. In FY 2005, the Government Accountability Office (GAO) identified the need to enhance computer security protection in air traffic control systems and physical security protection at air traffic control facilities. In April 2005, FAA started to initiate aggressive actions to correct previously identified air traffic control security deficiencies.

## SAS-70 REVIEW ON DOT'S FINANCIAL MANAGEMENT SYSTEM

An annual external review was conducted for cross-servicing functions within the Department as required by the Office of Management and Budget (OMB) guidance. The OMB requires Centers of Excellence to provide Federal agencies with an independent audit report in accordance with the American Institute of Certified Public Accountants' (AICPA) Statement of Auditing Standards (SAS) 70.

The Department's report summarizes the results of a review of system security controls over the DOT Enterprise Service Center's (service center) Delphi Financial Management System. The Delphi Financial Management System performs accounting and financial management functions for DOT and other Federal agencies. It is maintained by Federal Aviation Administration employees at the Mike Monroney Aeronautical Center in Oklahoma City, Oklahoma, under the direction of the departmental Chief Financial Officer.

The service center is one of four Centers of Excellence designated by the OMB to provide financial management information system services to other Federal agencies. To date, the service center supports one other Federal agency, the National Endowment for the Arts.

Clifton Gunderson, LLP, an independent auditor, of Calverton, Maryland, completed the review. The OIG performed a quality control review of Gunderson's audit work to ensure that it complied with applicable auditing standards Generally Accepted Government Auditing Standards and the AICPA's SAS-70.

The Gunderson audit report concluded that management's description of controls for the Delphi Financial Management System presents fairly, in all material respects, the controls that had been placed in operation as of June 30, 2005. In addition, Gunderson concluded that controls, as described, are suitably designed to provide reasonable assurance that 8 of the 10 specified control objectives would be achieved, if these controls were complied satisfactorily. Gunderson's testing found that controls were operating effectively to provide reasonable assurance that 7 of the 10 control objectives were achieved during the period from October 1, 2004 to May 31, 2005.

Since September 2003, DOT management implemented more disciplined security administration and oversight of Delphi operations, strengthened controls over access to the General Ledger module to ensure the integrity of financial statement compilation in Delphi, and installed an enclosed area in the computer center to better protect Delphi servers. In addition, management enhanced controls over changes to Delphi production programs and tested the contingency plan to ensure continuity of Delphi operations in case of emergency.

## IMPROPER PAYMENTS PROGRAM FOR FY 2005 AND PLANS FOR FUTURE YEARS

In FY 2005, the Department engaged AOC Solutions, Inc. to conduct an improper payments review of FY 2004 payments in ten programs for compliance with the Improper Payments Information Act of 2002 (IPIA). The objectives of this review were to (1) assess the amount and causes of improper payments, (2) identify programs with significant improper payments, and (3) identify action plans for reducing improper payments in programs identified as high risk.

The following programs were reviewed by AOC Solutions, Inc.

- Department of Transportation Payroll
- Office of the Secretary of Transportation—Working Capital Fund
- Federal Railroad Administration—Grant Program
- Federal Highway Administration—Federal Aid Grant Program*
- FHWA—Federal Lands
- Federal Transit Administration—Formula Grant Program*
- FTA—Capital Investment Grant Program*
- Federal Aviation Administration—Airport Improvement Program*
- FAA—Operations (excluding Payroll)
- FAA—Facilities and Equipment

* Identified in Section 57 of OMB A-11

During the review, AOC Solutions, Inc. found no significant improper payments which would result in a program exceeding 2.5% and $10 million of the total expenditures for the fiscal year. In total, eight improper payments were found, resulting in a projected amount of improper payment to be $8,125.

Additionally, the Department was able to improve its processes over last year. In the previous PAR it was reported that FAA was not able to provide sufficient data or answers to many outstanding questions. During the review this year, FAA was able to provide sufficient information for all questions, and had no questionable payments.

As noted in last year's PAR, another constraint was the limited amount grant data available. During our review this year, test procedures applied covered payments made by DOT to grantee entities. However, test procedures did not address subsequent flow down payments made by grantees to vendors. States and other non-Federal entities administer these grant programs and, accordingly, much of the activity subject to testing for improper payments is accounted for at these entities.

To address the limitation, DOT devised an innovative research and development (R&D) strategy that was implemented at the Federal Highway Administration's Highway and Construction grant program. The R&D project strategy; was to develop and test a methodology for implementing the IPIA requirements at the grantee level.

The development phase of this study involved meeting with State transportation and audit officials to document the processes used in administering the Federal Highway Planning and Construction Program. This resulted in a comprehensive document that described the planning and construction phases of projects and a methodology for determining whether goods and services received were in accordance with contractual terms and conditions, including Federal requirements. Payments for goods and services that did not comply with contractual terms and conditions represented an improper payment.

For testing, two project sites were selected to test the methodology. The tests involved a sample value of $21,269,706 from a population value of $26,056,918 for the first project and a sample value of $6,741,482 from a population value of $8,450,999 for the second project.

The tests disclosed three underpayments, one of which (from project one) was statistically insignificant and an extrapolation of the other two to the population of payments for the project (project two) in which they occurred resulted in an improper payment estimate of $111,671.

DOT completed the project successfully in the summer of 2005 and is in the process of extending the methodology nationwide.

In 2006 and 2007 the Department has several goals for the improper payments program. First, the Department will continue its recovery audit work, which has been conducted since 2002. While there have been no significant findings, the Department has found it to be very beneficial.

Secondly, DOT will continue to expand the methodology from the R&D project. Work has begun to develop a similar methodology in the Department's remaining OMB A-11, Section 57 grant programs. To help facilitate the expansion of this methodology the Department has put together the following plans.

In 2006, the Department will begin testing the four Section 57 grant programs for improper payments in a concentrated area. DOT has spent millions of dollars on relief efforts to repair damage from Hurricanes Katrina and Rita. Depending on supplemental appropriations, DOT expects to spend billions of dollars to rebuild the transportation infrastructure in Alabama, Louisiana, Texas, and Mississippi.

By testing for improper payments in this region, DOT will be able to focus on inherently high risk projects, based on the dollar amount and the speed at which money is being spent. This will allow for further refining of our improper payment methodology and contribute to the oversight of these regions. As a result of the testing, DOT will be able to test and establish new controls for emergency projects.

Concurrently, DOT will work with the FAA, FTA, and FHWA grant programs to implement the methodology into their normal grant processes. By having the improper payment methodology worked into the normal grant procedures, the Department will have nationwide testing beginning in FY 2007.

## SCORECARD ON THE PRESIDENT'S MANAGEMENT AGENDA

### HUMAN CAPITAL INITIATIVE

Develop a Department-wide human capital workforce strategy to address future workforce gaps, eliminate skill gaps in critical occupations, develop performance-based incentives for the workforce, ensure citizen-centered, delayered, and mission-focused organizations; strengthen leadership skills, and ensure a robust leadership pipeline; improve the measurement and evaluation of human capital strategies; and integrate E-Government and Competitive Sourcing strategies.

**FY 2005 STATUS** ● GREEN

**PROGRESS** ● GREEN

HOW DOT IS MEETING PMA CHALLENGES. DOT's Human Capital Plan is aligned with the President's Management Agenda and the OPM/OMB Standards for Success. During this fiscal year, the Department:

- Completed FAA's Air Traffic Controller staffing plan to ensure that there will be adequate prepared controllers to accommodate a retirement surge and increasing workloads;
- Steadily improved annual workforce planning and analysis, integrating competitive sourcing, and acquiring a new forecasting tool;
- Achieved provisional certification of the SES performance management system, developed SES pay for performance policies, and instituted a centralized executive coaching program for new SES hires;
- Acquired, automated, and piloted a model for measurement and management of leadership competencies, and developed a GS-15 Executive Pipeline forum series;
- Began systematic measurement and target-setting for mission-critical competencies;
- Instituted a Career Residents program to hire and develop promising graduates into mission critical occupations;
- Eliminated pass-fail performance management systems, replacing them with systems that link to strategic goals and make performance distinctions, and set new requirements for the training and evaluation of leaders;
- Developed new policies to improve the strategic use of probationary periods for new supervisors and managers and for employees;
- Conducted gap analysis for IT competencies and set targets for closing gaps;
- Decreased the time-to-fill for SES and GS positions, and
- Assessed Department-level accountability system, and began documentation and review of accountability measures and practices at the OA level in all areas of human capital management.

## COMPETITIVE SOURCING INITIATIVE

Improved consistency for defining commercial and inherently governmental inventories across the Department. Identified commercial competable activities, provided strategic direction for competitive sourcing and human capital initiatives, and developed and shared high-quality intellectual capital with staffs at OPM and OMB.

**FY 2005 STATUS** ● GREEN

**PROGRESS** ● GREEN

HOW DOT IS MEETING PMA CHALLENGES. In FY 2005, DOT maintained its green status on the President's Management Agenda scorecard for competitive sourcing.

During 2005, DOT completed one standard and six streamlined competitions including the largest and most complex competition conducted to date under OMB Circular A-76 for FAA's automated flight service stations. To date, DOT has completed 20 competitions for over 2,889 full time equivalent positions with anticipated savings of over $2.0 billion over the performance periods.

DOT initiated an Executive Steering Committee for competitive sourcing which evaluates the opportunity for cross organizational competitions throughout the Department and brings more consistency to DOT's competitive sourcing efforts.

DOT requires OAs develop their competitive sourcing plans in conjunction with their workforce planning efforts to ensure human capital solution strategies include public-private competition.

## E-GOVERNMENT INITIATIVE

Better justify and track costs and performance of information technology projects, as well as participate in government-wide initiatives that automate and simplify how the public deals with the government and reduce redundancies and increase efficiencies government-wide.

**FY 2005 STATUS** ● GREEN

**PROGRESS** ● GREEN

HOW DOT IS MEETING PMA CHALLENGES: Capital Planning. Participation in capital planning process expanded across all Operating Administrations. DOT Departmental Investment Review Board (IRB) reviewed and approved the FY 2007 IT portfolio in support of the budget and Department mission and goals. IRB conducted quarterly reviews of high risk major projects. Updated Capital Planning and Investment Control and Enterprise Architecture (EA) policy and governance structure to ensure alignment between the two areas. Achieved 100% acceptable business cases for the FY 2006 budget.

IT Security. DOT has certified and accredited 85% of all IT systems. DOT continues to conduct weekly vulnerability scanning of all public facing and e-Government Web servers. Expanded the vulnerability scanning to internal servers as well as part of a quarterly compliance review process.

Enterprise Architecture (EA). Released an updated iteration of DOT’s Modernization Blueprint including As-Is and To-Be architecture for the DOT common IT infrastructure. The EA Framework and Reference Models are aligned with the OMB Federal Enterprise Architecture Program Management Office Framework. OAs continue to make progress maturing their EAs for their unique business/mission areas.

Government-wide Initiatives. DOT participates in 24 e-Government initiatives that span all four categories. The e-Government project managers work closely with Managing Partners in the implementation of these initiatives. The Office of the Chief Information Officer monitors initiative progress against milestones in the OMB approved e-Gov Implementation Plan. Major schedule and performance issues are brought to the IRB for review and action. DOT completed the migration to a new payroll provider except for FAA who will migrate in October 2005. DOT completed the implementation of a Department-wide Learning Management System except for OIG who will migrate in the first quarter of FY 2006. DOT will complete the implementation of e-Authentication for the SAFER system in October 2005.

## BUDGET AND PERFORMANCE INTEGRATION INITIATIVE

Better integrate budget and performance functions by integrating respective staff work; developing plans and budget with outcome goals, output targets, and resources requested in the context of past results; charging full budgetary costs of programs; and documenting program effectiveness.

**FY 2005 STATUS** ● GREEN

**PROGRESS** ● GREEN

HOW DOT IS MEETING PMA CHALLENGES. In FY 2005, DOT achieved its goals in this area and earned a green score on the scorecard by completing the following:

- DOT identified efficiency measures for all programs that have been scored by the Program Assessment Rating Tool (PART).
- All DOT modes provided marginal cost of performance information in their budget submissions for at least one of their performance goals.
- Recognized as a leader in marginal cost within the Federal government, DOT presented its marginal cost of performance approach to other Federal agencies at an OMB sponsored seminar on improving marginal cost methods and practices.

DOT Performance Plan and Reports. DOT's Performance and Accountability Report has consistently garnered a high standing from George Mason University's Mercatus Center, scoring within the top three across government for the fifth year in a row.

## IMPROVED FINANCIAL MANAGEMENT INITIATIVE

Develop financial management systems capable of producing more timely and accurate information, and maintain a record of unqualified opinions on our financial statements.

**FY 2005 STATUS** ● RED

**PROGRESS** ● GREEN

HOW DOT IS MEETING PMA CHALLENGES

- DOT received its fifth consecutive unqualified audit opinion.
- DOT produced its FY 2005 financial statements on target and met the November 15, 2005 deadline for audit completion and submission of this year's Performance and Accountability Report.
- DOT put into production a DASHboard. The DASHboard provides up-to-date financial and performance information to program managers. DOT is developing a plan to expand the use of the DASHboard to incorporate additional program performance information and financial data.
- Financial data from Delphi is available on demand to 3,500 users and is being used throughout the Department to help manage programs on a daily basis.
- DOT was named a Center of Excellence for Financial Systems and Services. DOT has one external customer, the National Endowment for the Arts, in production since October 2004. In addition, DOT has signed two new customers: the Commodity Futures Trading Commission and the Institute for Museum and Library Services, which will be implemented on DOT's Delphi financial management

system in FY 2006 and will also be using accounting services from DOT's Center of Excellence. DOT has competitively selected a private sector business partner to help market to implement new customers on our Delphi Financial Management System (Oracle Federal Financials).

### RESEARCH AND DEVELOPMENT INITIATIVE

Apply the Research and Development (R&D) Investment Criteria of relevance, quality, and performance and continuously improve management of research programs.

**FY 2005 STATUS** ● GREEN

**PROGRESS** ● GREEN

HOW DOT IS MEETING PMA CHALLENGES. In FY 2005, DOT achieved its goals in this area and earned a green score on the scorecard by completing the following:

- DOT established the Research and Innovative Technology Administration (RITA) to guide the coordination and management of R&D activities across the Department. The creation of RITA instituted an integrated planning process to ensure that RD&T investments are effective and aligned with Departmental goals. The process has three elements: multiyear strategic planning, annual program planning, and budget and performance planning.

- DOT also established two executive-level bodies: the RD&T Planning Council composed of Operating Administrators and Assistant Secretaries, and the RD&T Planning Team, which includes modal RD&T program managers at the Associate Administrator level. These bodies ensure the collaboration and coordination of RD&T both within DOT and with external entities.

- In 2005, the RD&T Planning Council and Planning Team led DOT in the setting of agency-wide priorities for the FY 2007 RD&T budget. They also provided guidance for annual program reviews, at which the Operating Administrations presented their RD&T programs' mission and goals, research focus, and use of the R&D investment criteria.

- DOT also issued the annual *RD&T Plan* and the RITA Report to Congress on the Department's research priorities. Both reports were developed through extensive cross-modal planning and coordination.

### REAL PROPERTY ASSET MANAGEMENT INITIATIVE

Uses sound real property management of real property resources for diverse transportation missions, maintaining the quality of real property assets managed, and disposing of no longer required assets.

**FY 2005 STATUS** ● RED

**PROGRESS** ● GREEN

**How DOT is Meeting PMA Challenges.** DOT continues to make progress under this initiative. The 2005 status of the PMA initiative is RED due to the amount of work required to create an accurate inventory of all real property assets throughout the Department. However, OMB rated the Department GREEN in progress in recognition of the significant advances made in the fourth quarter of FY 2005 in accomplishing the goals set forth in this PMA initiative.

The Federal Aviation Administration owns approximately 69,500 of the roughly 70,000 assets in the Department and has continued to lead in managing the inventory databases and applications.

DOT is aggressively pursuing a status upgrade to yellow in the first quarter of FY 2006:

- DOT will complete the Asset Management Plan (AMP) for OMB approval
- DOT will implement the AMP
- DOT will capture Federal Real Property Council established performance measure data for successful inventory reporting December 15th to GSA

DOT's two chartered committees will establish decision making guidelines for acquisition, disposition, capital funding, and a three year timeline of initiatives.

## IMPROPER PAYMENTS INITIATIVE

Develop financial management systems capable of producing more timely and accurate information, and maintain a record of unqualified opinions on our financial statements.

**FY 2005 STATUS** ● RED

**PROGRESS** ● GREEN

**How DOT is Meeting PMA Challenges.** In FY 2005, the Department took several steps towards eliminating improper payments.

- Tested the Department's Top Ten Program for improper payments and found little to no erroneous payments.
- Conducted Recovery Audits in all Operating Administrations finding a very small number of overpayments.
- Developed and tested an innovative solution for determining the level of improper payments in grantees and sub-grantees.

# POSSIBLE FUTURE EFFECTS OF EXISTING EVENTS AND CONDITIONS

## HURRICANE RECOVERY EFFORTS

In support of the Federal response to hurricane relief efforts, DOT is requiring all of its Operating Administrations to report their obligations and expenditures hurricane-related costs. DOT is coordinating all parties involved in the transportation related response and relief efforts. Federal, State, and local governments are working side-by-side to deliver relief to the areas physically damaged by Hurricane Katrina and to communities across the South that have been affected by the storm. Efforts and resources are focused on proving transport and logistics to support long-term recovery. The Department has made available the latest information from its agencies on the operational status of airports, roads and highways, rail lines, transit systems, ports and pipelines in the tri-state area affected by Hurricane Katrina.

## COORDINATION WITH DEPARTMENT OF HOMELAND SECURITY (DHS)

DOT is coordinating with the Department of Homeland Security (DHS) on transportation security related matters. This year, DOT is working with DHS' emergency response staff on the hurricane relief efforts. Numerous DOT offices have ongoing projects related to the Patriot Act compliance for HAZMAT endorsement background checks, and HAZMAT tracking projects. DOT and DHS have an advanced traveler systems work for helping mobility and the flow of traffic during rush hours. FTA has a transit security training project with DHS. The lessons learned from recent National disasters such as Hurricane Katrina and Hurricane Rita are guiding the Department's responses to future natural and man-made disasters.

# OTHER MANAGEMENT INFORMATION, INITIATIVES, AND ISSUES

## FIVE-YEAR FINANCIAL MANAGEMENT PLAN: PROGRESS REPORT TO MEET DOT'S FINANCIAL MANAGEMENT GOALS

### GOALS OF FINANCIAL MANAGEMENT PLAN:

#### Produce accurate and timely financial information.
#### Management's use of the information to drive decisions and results.

DOT continually seeks to expand the use of financial and performance information to ensure that DOT program managers have all the information they need to drive results in their organizations. Through enhanced decision making, the Department can more effectively and efficiently manage tax payers' dollars.

At the forefront of our efforts is the Federal Aviation Administration's Air Traffic Organization (ATO), which has developed key cost metrics for each of its major functions. With accurate financial information, tied with ATO performance information, ATO is increasingly able to make better informed decisions on how to improve the ATO Line of Business. Several other OAs are making similar progress for their program managers.

DOT is expanding our support for providing information to managers through our Delphi DASHboard project. On May 16, 2005, DOT moved its first Delphi DASHboard pilot into production. Using Oracle's Web Portal and Balanced Scorecard tools, DOT managers are using the Delphi DASHboard to track their progress on OMB's Financial Performance Metrics and the DOT's own CFO Internal Scorecard, as well as to check the status of the funds under their control.

#### Implement a plan to expand the scope of routine data use to inform management.

Piloting the Delphi DASHboard has been a valuable learning experience for the Department. Through this effort, DOT is identifying more and more of the Department's data needs and is also identifying the Department's data strengths, i.e., data sources that are already available. The OAs have a wealth of financial and program data for many of their programs and projects. Our DASHboard pilot proved that a Web-enabled dashboard is the best way to present and continue to expand the use of data to make management decisions.

Additionally, DOT will continue working to improve internal controls and overall financial management of the Department's programs and operations, including the centralization of accounting functions at the DOT Financial Management Center of Excellence in Oklahoma City. DOT will also work to improve on the CFO Council's Performance Metrics.

With all this data readily available, the DOT will be reviewing the most efficient and cost effective way to combine and clearly present financial and performance information. For the Fall of FY 2006, DOT has committed to re-examine its methods and tools for meeting its DASHboard and business intelligence needs. Oracle's Balanced Scorecard has proved to be a useful tool, but some of the OAs see value in other solutions. Using input and expertise from the OAs and from our Financial Management Center of Excellence, DOT will determine the most efficient and cost effective Web-enabled solution for flexibly presenting financial and performance data to DOT managers.

### Receive an unqualified audit opinion.

Since early in 2005, DOT has been working hard to receive an unqualified audit opinion on its FY 2005 financial statements. DOT earned an unqualified audit opinion for each of the previous four years.

### Meet financial statement reporting deadlines.

In 2004 the Department met the accelerated November 15 reporting deadline by working closely with each of DOT's financial statement auditors. With upgrades to DOT's Delphi financial system, we are now delivering monthly and year-end financial statements for each OA overnight. This new capability will save us precious time, especially at year-end; previously preparing statements took several days.

### Systems are in compliance with the Federal Financial Management Improvement Act (FFMIA).

With the conversion of the FAA to Delphi on November 10, 2003, DOT completed converting all its OAs to a state-of-the-art, COTS-based, JFMIP-certified, Standard General Ledger (SGL) compliant financial management system. DOT is the first cabinet-level agency to complete this conversion and have all its operating elements in production on a cost-effective single instance of the *Oracle Federal Financials* application software. To take advantage of all new system capabilities as they become available, we upgraded Delphi to release 11.5.9 in May 2004 and to the 9i Oracle database technology in August 2004. The next upgrade is scheduled for the Winter of FY 2006. DOT is continuing centralization of accounting operations at the DOT Financial Management Center of Excellence in Oklahoma City.

### Has no material:
- **auditor-reported internal control weaknesses;**
- **noncompliance with laws or regulations; or**
- **weaknesses or nonconformances reported under Sections 2 & 4 of FMFIA**

DOT has been working diligently with our OAs to resolve all material internal control weaknesses reported by our auditors in previous years or at least sufficiently addressed for them to be downgraded to a reportable condition. DOT has made significant progress in this area and will continue to be vigilant in FY 2006 to ensure that we have no material auditor-reported internal control weaknesses.

DOT has alos been working closely with our Operating Administrations to ensure that we have no material noncompliance with laws or regulations and will continue these efforts in FY 2006.

DOT has been working closely with each Operating Administration to correct all material weaknesses and nonconformances reported under Section 2 and Section 4 of the Federal Managers' Financial Integrity Act that impact the agency's internal control over financial reporting or financial systems. We will continue these efforts throughout FY 2006.

## IMPLEMENTING A-123

### APPENDIX A

During FY 2005, DOT moved aggressively to address the requirements of Appendix A, beginning with the establishment of an distinct organizational structure to oversee the implementation of this initiative. An Internal Controls Senior Advisory Team (ICSAT), headed by the CFO, was established with senior-level representation from each of DOT's Operating Administrations. The ICSAT meets on a monthly basis to review progress and to actively engage in all decisions relating to approach and the prioritization of issues. A working group consisting of representatives was also established to complement the ICSAT and to carry out the decisions at the working level across the Department. DOT has also engaged the services of a contractor to participate in both the planning and testing phases of this initiative.

DOT's plan for approaching Appendix A was submitted to OMB in August and received favorable feedback. Since then, considerable progress has been made in implementing this plan, including the identification and documentation of key business processes and controls, determination of materiality, and the establishment of a testing approach. The DOT ICSAT recognizes that the implementation of all aspects of Appendix A will require a multi-year approach. During FY 2006, initial testing will be based upon assessment of risk and availability of resources. A similar approach will be applied to addressing follow-on work in FY 2007 and 2008.

### APPENDIX B

In anticipation of the issuance of Appendix B, DOT proactively worked these new requirements into the re-competition of our task orders with our bank providers. As a result, DOT is well-positioned to implement these requirements in FY 2006 with minimal cost and disruption of resources.

On the travel card side, for example, DOT arranged for the creditworthiness requirement to be managed by the vendor **at no cost to the Government**. We have also established a salary offset program in the FAA which covers the vast majority of DOT credit card holders. Preliminary technical work has also been initiated to implement split disbursement for the reimbursement of travel expenses. We have been coordinating the introduction of split pay with our e-Travel provider and will work with them to introduce this enhancement to our travelers in FY 2006.

## MANAGERIAL COST ACCOUNTING

Managerial cost accounting identifies, tracks, and analyzes the total cost attributable to a particular task, job, or program. The purpose of managerial cost accounting is to provide program managers the cost information required to accurately report program efficiency and development of a program's future budget. DOT policy requires that OAs accumulate, distribute, monitor, and evaluate cost information during each accounting period.

All DOT OAs have implemented the Department's financial management system, Delphi, but it will be several years before cost-accounting data systems are fully mature and include historical data that will allow DOT managers to integrate performance and accounting data. In the meantime, DOT must be able to tie resources to results.

DOT, therefore, has decided to focus during the FY 2007 budget cycle on the linkage between funding and agency level outcomes and outputs and draw a comparison between the marginal benefits and the marginal cost associated with additional funds or reduced funding as recommended in section 51.2 of OMB Circular A-11. To accomplish this, the DOT OAs will be requested to provide the following in their FY 2007 budgets for at least one performance measure.

- Current services funding;
- Requested increase or decrease to funding;
- Associated agency-level performance measure for the activity in question;
- Baseline performance targets associated with the current services funding;
- New targets associated with changes in funding; and
- Discussion of how agency level results contribute to DOT level strategic outcomes.

This will be an interim step in tying resources to results until cost accounting data is more widely available throughout the Department. This approach does the following:

- Introduces a new conceptual framework for budget-building;
- Builds a more visible logic model showing the tie between agency funding and Departmental outcomes;
- Requires more rigorous target-setting methods from the OAs; and
- Helps the OAs articulate more clearly the impact of funding changes.

## INSPECTOR GENERAL'S TOP MANAGEMENT CHALLENGES REPORTED FROM FY 2002–FY 2005

The Department recognizes that Management Challenges are not issues that are easily solved. In many cases they require investments or upgrades to technology or substantial changes in long-standing procedures or program activities. As a result, to completely address a Management Challenge may take more than one fiscal year. In an effort to provide some context to the Management Challenges, we have listed information on the year that the challenge was first reported. DOT hopes to begin to collect information to that will supply perspective overtime on the Department's progress towards resolving the challenges.

### 1. CHALLENGE: AVIATION SAFETY

The U.S. aviation industry continues to be the safest in the world. However, FAA must adjust its safety oversight to emerging trends in the aviation industry and changing economic conditions. While air carriers have turned increasingly to outside, contracted repair stations, FAA continues to focus its inspection resources on air carriers' in-house maintenance work. The IG recommended that FAA strengthen its oversight procedures of foreign aviation authorities conducting inspections on its behalf. Since the OIG's Report was released, there was real progress on runway incursions (potential collisions on the ground), but operational errors (when air traffic controllers allow planes to come too close together in the air) continue to increase. Corrective actions are imperative to address this ongoing safety problem.

**Reported:** FY 2002

**Resolved:** This item is has not been resolved.

### FAA Actions Taken to Resolve Challenge:

#### Adjust safety oversight to address increased maintenance outsourcing.

To address challenges at air carrier repair stations, FAA formed a Risk Assessment work group, which is developing a repair station prototype program. This program will bring together a team representing all the areas of expertise to oversee aviation certificate holders of large repair stations or companies that own multiple repair stations and satellite repair stations.

The work group is developing guidance materials for inspectors and information databases to improve FAA oversight of repair stations. The work group has also developed a comprehensive surveillance program, which requires repair stations to use elements of a system-safety approach such as risk assessment and risk management tools. FAA has revised its guidance and anticipates training for the inspector workforce to begin in November 2005.

Additionally, FAA is revising its Flight Standards Handbook Bulletin for Airworthiness (14 CFR Part 43.17) to incorporate the pending Bilateral Aviation Safety Agreement with associated Maintenance Implementation Procedures (BASA/MIP) with Canada to ensure the standardization of maintenance on U.S. certified aircraft repaired in Canada. There are no FAA certificated repair stations in Canada. In lieu of FAA certificated repair stations, the Handbook states that the United States accepts the work and return to service of U.S.-registered aircraft and components that are located in Canada by a properly Transport Canada Civil Aviation (TCCA) certificated entity.

Finally, FAA is negotiating a BASA/MIP with the European Union that will be used to continuously verify European member states conducting surveillance/certification activities on behalf of the FAA. FAA hopes to finish negotiations and implement the agreement by 2008.

#### Reduce operational errors and runway incursions as traffic rebounds.

Reducing operational errors and runway incursions as traffic continues to increase is a shared responsibility among pilots, air traffic controllers, and vehicle drivers. To address this challenge, the FAA focused on outreach, awareness, improved procedures and infrastructure, and technology.

Progress was made in reducing the severity, number and rate of pilot deviations—the most common type of runway incursion. To enhance pilot situational awareness, the FAA released a new pilot guide and DVD that highlighted communication procedures for safe surface operations. In collaboration with industry, the FAA also created an online course that educates general aviation pilots on runway safety.

To enhance air traffic supervisor and controller discussion of serious events during team briefings, the FAA developed a safety awareness campaign designed to help controllers visualize an event that actually happened and aid the development of strategies based on intuitive and experiential expertise for use in similar situations. Additionally, the agency has developed an operational error database to support identification of trends from which error reduction initiatives will be developed.

### Improve operational error reporting from Tower and Terminal Radar Approach Control (TRACON) facilities.

In July 2005, the FAA issued a general notice (GENOT) instructing all air traffic control facilities to establish a facility audit process by September 1, 2005. This audit process allows for random reviews of Air Traffic Services using playback tools to identify operational errors and operational deviations, and provides greater assurance that operational errors and operational deviations are being reported.

In addition to the facility audit process conducted each month, the agency identified select facilities based on trends, analysis, intelligence, complaints and statistics, and required them to review data. The FAA reviewed the same data from these select facilities and addressed the issue by training or decertifying controllers, as appropriate. The agency's findings and supporting data are retained at the headquarters' level for two and one half years.

## 2. CHALLENGE: MOTOR VEHICLE SAFETY

In its 2005 update on DOT's management challenges, the IG made four findings related to motor vehicle safety: (1) Overcoming obstacles to increasing safety belt usage; (2) Addressing SUV rollover issues; (3) Pursuing laws to discourage alcohol-impaired driving; and (4) Spotting vehicle defects.

**Reported:** FY 2002

**Resolved:** FY 2004.

**Re-Reported in FY 2005**

**Actions Taken to Resolve Challenge:**

To improve defect investigations, the routine submission of additional manufacturer data, pursuant to the requirements of the Transportation Recall Enhancement, Accountability and Documentation (TREAD) Act, allows NHTSA access to a substantially increased amount of early-warning data that can be analyzed to determine whether a potential safety-related problem exists, giving the agency the ability to report any defects to the public in a more-timely manner.

Safety Belt Use—Safety belt use in 2005 increased to 82%, an all-time high. NHTSA is continuing to implement strategies from its 2003 integrated project team (IPT) report on increasing safety belt usage, to include an added emphasis on high-risk groups such as minorities, younger drivers, rural populations, pick-up truck occupants, 8–15 year-old passengers, part-time safety belt users, and motor vehicle occupants in States with secondary safety belt use laws. In addition to an occupant protection IPT, NHTSA also had an IPT on vehicle rollover. The agency is continuing to implement strategies and activities from the report to include necessary safety standard requirements to reduce rollover events and minimize injuries when such events occur.

Drug-Impaired Driving—To reduce alcohol-impaired driving, NHTSA made available more than $29.9 million in alcohol-impaired driving countermeasure incentive grants to 34 States having alcohol-impaired driving laws such as open container and repeat offender laws.

## 3. CHALLENGE: THE FUTURE OF INTERCITY PASSENGER RAIL

DOT should continue to work with the Congress to break the cycle of appropriations without authorization for Amtrak and to realign the size, operations, and governance of the intercity passenger rail system to match the levels of funding available from all sources.

**Reported:** FY 2002

**Resolved:** This item has not been resolved.

**Actions Taken to Resolve Challenge:**

FRA, together with the Office of the Secretary, has been heavily engaged in promoting a reauthorization of Amtrak that would address many issues surrounding intercity passenger rail. These issues include but are not limited to size, operations and governance of the Nation's passenger rail systems. Through the annual grants to Amtrak, in particular the capital grant, and the Department's presence on the Amtrak Board of Directors, FRA has been able to assure that capital investments address the company's highest priorities, and are consistent with the funding available. FRA recognizes that the need for work in this area is ongoing, particularly in addressing Amtrak's operating accounts and the services it provides such as food and beverage and first class services.

## 4. CHALLENGE: INFORMATION TECHNOLOGY MANAGEMENT

DOT has one of the largest IT investment portfolios among the civilian agencies. DOT IT systems support air traffic control and distribute billions of dollars in Federal grants for transportation improvements. Security breaches against these systems could have far-reaching effects on the Nation's transportation system and economy.

DOT enhanced its defense against Internet intrusions and developed a more reliable inventory of systems. DOT, however, must further protect critical IT systems (especially air traffic control systems) against attack and enhance contingency planning to ensure business continuity in an emergency.

**Reported:** FY 2002

**Resolved:** This item has not been resolved.

**Actions Taken to Resolve Challenge:**

In FY 2005, DOT revised its Departmental Information Resources Management Manual (DIRMM), and updated policies and practices specific to Information Technology Capital Planning, IT Security, and Enterprise Architecture. This will ensure that:

- DOT is in compliance with legal and OMB requirements;
- Operating Administrations manage their portfolios of investments in a like manner; there is a consistent approach in security and the development of a "Federated" Enterprise Architecture; and,
- As a result of a consistent approach for enterprise architecture, DOT reduces redundant systems, promotes data sharing, component re-use, and collaborative efforts within DOT and with external partners.

DOT revised its Capital Planning and Investment Control Guide clearly defining, through detailed criteria, how DOT will identify high-risk agency IT projects for review. The revised guidance also includes process changes specific to earned value management, which DOT will use to identify high risk projects that exceed established variance levels.

DOT issued new, specific guidance on reporting project cost, schedule and performance variance. Project reports are provided to the CIO on a quarterly basis, but include monthly data.

### FAA Securing Critical Computer Systems:

Because FAA's IT portfolio constitutes a significant portion of the entire DOT portfolio, it was critical to the Departmental effort that FAA also takes specific steps to strengthen its oversight of IT investment. Accordingly, in FY 2005, FAA:

- Built on an already-strong Exhibit 300 training, development, and approval process, resulting in significant improvement to its initial passback scores over the previous year.
- Implemented a process to evaluate adherence to cost and schedule projections on all major projects, regularly monitor cost, schedule, and performance variances, and institutionalized the use of Corrective Action Plans for investments with variances greater than negative 10 percent.
- Achieved one of the highest scores of any agency on the GAO IT Investment Management Model (ITIM) scorecard, and adopted GAO's recommendations to move the agency to level 3 compliance with GAO's model. In FY 2005, FAA implemented 79% of ITIM stage two practices.
- Improved processes and capabilities for acquiring software intensive systems.
- Instituted changes to the overall acquisition management system, including the use of Exhibit 300s as the core investment decision document.

The Department's Transportation Cyber Incident Response Center (TCIRC) serves as the focal point for monitoring and protecting the Department's critical IT assets. Using a wide variety of tools, the TCIRC continuously monitors and scans the Department's IT infrastructure and looks for vulnerabilities. The Office of the CIO has also established a robust continuity of operations plan that provides for the quick reconstitution of critical IT services in the event of a prolonged disruption.

The FAA made significant progress toward improving information systems security for all FAA systems in FY 2005 and increased monitoring of its information systems through additional intrusion detection systems. The FAA Computer Security Incident Response Center also monitors the DOT system after normal working hours and on weekends and holidays thus providing DOT continual coverage.

Investments: In FY 2005, DOT continued to expand and enhance the role of the Departmental Investment Review Board (IRB). The IRB, which is chaired by the Deputy Secretary, and consists of the CIO, Chief Financial Officer, General Counsel, Under Secretary for Policy, Assistant Secretary for Administration, and four Operating Administrators, has the authority to approve, modify, or terminate major IT investments. To ensure that the IRB can improve the cost-effectiveness of DOT's $2.6 billion annual IT investment, it needs to:

- play a more proactive role in identifying high-risk modal administration IT projects for review;
- ensure that OAs conduct effective and detailed reviews of their portfolios;

- require the modal administrations to share more timely information on proposed IT projects; and
- perform more in-depth reviews of the data.

## 5. CHALLENGE: HOLDING THE LINE ON PROGRAMS CONDUCIVE TO FRAUD

For the Department of Transportation, fraud has the serious potential for diverting critical funds from infrastructure programs, subverting the efforts of safety regulators and undermining the integrity of important public policy. The Office of Inspector General (OIG) has identified three areas where fraud has a particularly damaging effect on the Department's mission: (1) Federal Highway Administration (FHWA) and Federal Transit Administration (FTA) programs involving highway and transit infrastructure, (2) Federal Motor Carrier Safety Administration's (FMCSA) program related to commercial driver's licenses, and (3) DOT's Disadvantaged Business Enterprise Program.

**REPORTED:** FY 2002

**RESOLVED:** This item has not been resolved.

### ACTIONS TAKEN TO RESOLVE CHALLENGE:

HIGHWAY AND TRANSIT INFRASTRUCTURE PROJECTS. FHWA continues to stress the use of fraud indicators and reporting procedures and is working with the transportation and highway industry to include the DOT OIG as a resource for reporting allegations of fraud, waste, and abuse on Federal-aid infrastructure construction projects. The FHWA and the Internal Revenue Service have jointly developed an enforcement strategy to strengthen tax evasion enforcement. FHWA identified opportunities to fortify deterrence strategies by increasing both, failure to register penalties and failure to report penalties from $50 to $10,000 per occurrence. In July 2005, FHWA changed the requirement that heavy vehicle use tax (HVUT) be paid quarterly to an annual payment to match the vehicle registration payment cycle. Finally, they developed temporary regulations for the tamper-proof dye injectors, which became effective October 2005.

Going forward FHWA and the Internal Revenue Service (IRS) will implement the provisions from Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU) and the American Jobs Creation Act of 2004. As each of the new provisions is applied over the next few years, the enforcement program will become more comprehensive. The IRS will be able to identify where evasion is occurring and target resources in those areas. For instance, enforcement efforts will be focused through a National fuel tax territory. The territory will work as one unit focusing on specific areas where evasion problems have been identified.

FTA initiated a risk management program which consists of planning, assessment activities, mitigation strategies for risk, and monitoring. This program creates a level of confidence in the project budget and schedule and enables FTA and the grantee to proactively manage the project.

MONITORING COMMERCIAL DRIVER'S LICENSES. To combat fraud in licensing for commercial motor vehicles, FMCSA:

- Distributed more than $28 million in grants to States for Commercial Driver's License (CDL) fraud prevention, covert monitoring of the CDL process, and support of CDL improvement projects;

- Developed a fraud emergency warning system to notify States of acts of fraud and theft of documents, identification production equipment etc;
- Developed the Commercial Skills Test Information Management System, a Web-based system to assist States in administering and providing oversight of third-party skill testers; and
- Conducted 13 CDL Compliance Reviews to check State implementation of the CDL program.

#### Disadvantaged Business Enterprise (DBE) Program

FAA took a number of actions in FY 2005 to strengthen oversight of the DBE program. The agency conducted limited reviews of basic DBE compliance activities at airports and developed a standard methodology for conducting DBE self-assessments and compliance reviews. FAA developed a Web-based system for airports to report their DBE accomplishments. This system will enable the agency to conduct trend analyses of the data received. The agency issued a revised regulation for airport concessions, which contains items to assist in the prevention of DBE fraud, such as a personal net worth cap, required eligibility reviews, and increased emphasis on monitoring and compliance by airports.

### 6. Challenge: Improved Fiscal Disciplines at FAA

As FAA increasingly turns to the General Fund to make up for revenue shortfalls in the Aviation Trust Fund, the agency will be competing with other critical Federal programs for funds during a period of fixed budgets.

Compounding the budget challenges it faces, FAA estimates that nearly half the controller workforce will leave the FAA between FY 2005 and FY 2012. To hire and train that many controllers within a severely constrained operating budget, FAA must identify ways to make every stage of its process for hiring, placing, and training new controllers more efficient and cost effective.

FAA also faces significant challenges with respect to its major acquisition programs. The Agency will need to gain control of existing projects, determine what the Agency's priorities are, and improve the overall management of its major acquisitions in a constrained budget environment.

**Reported:** FY 2002

**Resolved:** This item has not been resolved.

#### FAA Actions Taken to Resolve Challenge:

In June 2005, an FAA/DOT team drafted an alternative financing options report on the aviation trust fund as part of a broader effort that will take place on developing a reauthorization proposal for FAA programs. This options report will continue to be updated through the end of FY 2005 and into FY 2006 to reflect the final recommendations from FAA and DOT officials and will provide the basis for reauthorization legislation.

On December 21, 2004, the FAA announced its 10-year Air Traffic Controller Staffing Plan. Over the next 10 years, the agency will hire and train 12,500 controllers to backfill projected total retirement and non-retirement controller losses. The Air Traffic Controller Staffing Plan is currently being updated, with the second version to be released in December 2005.

FAA is making significant strides in improving its capital investment acquisition and procurement oversight:

- By the end of FY 2005, there were 105 certified program managers for projects greater than $50 million;
- Large and complex investments were segmented into phases to improve oversight and control;
- In developing the capital budget, the agency prioritized programs and allocated resources using criteria such as strategic relevance, cost reduction and productivity increases, benefits and risk; and
- The newly formed Capital Investment Team, which provides an independent and objective review of costs and benefits of investments, reviewed 79 programs, recommending the re-structuring of 15 and termination of two.

## 7. CHALLENGE: IMPROVING AVIATION SYSTEM CAPACITY

After a few years of relative reprieve from aviation congestion, traffic and delays are once again returning. The Department of Transportation's challenge is determining how and where traffic is likely to grow over the next decade and planning for adequate investment in facilities, technology and operational improvements to address both long-range and short-term needs.

**REPORTED:** FY 2002

**RESOLVED:** This item has not been resolved.

### ACTIONS TAKEN TO RESOLVE CHALLENGE:

DETERMINE HOW AND WHERE TRAFFIC IS LIKELY TO GROW OVER THE NEXT DECADE. In FY 2004, FAA completed a study analyzing system capacity, taking into account the socioeconomic and demographic trends expected to occur in the United States through 2020. This study expanded the focus of the 35 major airports and evaluated nearly 300 commercial service airports nationwide. The study identified the airports that need additional capacity and the constraints to enhancing capacity. In FY 2005, FAA began a second phase of this study that will take a more detailed look at airports other than those in major metropolitan areas and will begin to identify possible solutions to increase long-term capacity.

In the meantime, FAA is increasing short-term capacity by working with airports and local communities to build new runways. While there are no new runways opening in FY 2005, six runways are under construction with four of the runways opening in FY 2006. This will provide the potential to accommodate an additional 665,000 annual operations. Two additional projects, a runway extension and a runway/taxiway relocation, are expected to begin construction in FY 2006. In addition, there are 9 projects, including 3 new airports, in the planning or environmental assessment stages that could provide significant capacity benefits through FY 2015.

NEW RUNWAYS AND AIRSPACE REDESIGN INITIATIVES. Improving the efficiency of existing airport capacity by redesigning airspace is critical for taking full advantage of new runways and enhancing the flow of air travel around existing runways and airports.

The New York/New Jersey/Philadelphia Airspace Redesign project is on schedule to publish a draft Environmental Impact Statement in Fall 2005. This is a critical step in moving to a final decision, after which airspace redesign may begin.

Chicago's O'Hare airport is one of the busiest in the Nation; capacity problems at this airport can quickly cascade throughout the NAS. To address this critical hub in the aviation system, FAA is engaged in two separate, but related activities: the Chicago O'Hare Modernization Project and the Midwest Airspace Enhancement project. These projects will add and modify sectors and routes to increase traffic flow efficiencies in the Midwest by FY 2007.

Along the west coast, a series of advanced navigation routes was implemented in FY 2005 to reduce the miles flown between Seattle and San Francisco or Los Angeles. The routes utilize the navigational capabilities of advances avionics aboard the aircraft, permitting operations along the shortest path between the airports rather than flying over ground-based navigation aids.

POTENTIAL MARKET-BASED INITIATIVES TO MORE EFFICIENTLY ALLOCATE EXISTING CAPACITY. FAA has conducted detailed simulation exercises in the last year to examine the effects of market-based alternatives like congestion pricing and slot auctions (of arrivals and departures) on airlines and airport operations. These simulations have provided stakeholders an opportunity to comment on these potential tools for managing congestion. FAA is committed to continue working toward a market-based solution for congested airports and is investigating these options for potential use at New York's LaGuardia Airport.

## 8. CHALLENGE: GETTING THE MOST VALUE FROM INVESTMENTS IN HIGHWAY AND TRANSIT INFRASTRUCTURE PROJECTS

With fewer resources to fund transportation projects, it is important to ensure that infrastructure improvements are delivered on time and within budgets. In addition, the Department needs to ensure that taxpayer investments yield the greatest benefits for the given costs.

**REPORTED:** FY 2003

**RESOLVED:** This item has not been resolved.

**ACTIONS TAKEN TO RESOLVE CHALLENGE:**

In a 2003 Report to Congress, the FHWA outlined its efforts to develop a more multi-disciplinary approach towards project management and oversight activities. During the past two years, the Agency has addressed four key areas outlined in the Report:

- Optimizing the use of internal staffing;
- Effective recruitment of project managers;
- Increased training for existing and new staff; and
- Implementing specific stewardship and oversight initiatives, including the development of Project Management Plans and an Agency-wide risk management approach.

In FY 2005, the FHWA continued a program to transition Agency employees from the traditional role of reviewing and approving highway engineering project level actions to a new role of ensuring the effectiveness of state department of transportation processes in areas that are major project drivers, such as financing, controlling project level costs, schedule performance, transportation planning, maintaining funds accountability, and providing greater oversight of higher level management and financial issues. The majority of the positions filled in the Agency's Professional Development Program were by individuals from disciplines other than civil engineering, which is the traditional background. A series of multidisciplinary workshops were held for headquarters and field supervisors and managers. The FHWA implemented training that focused on the development of project oversight and financial management, delivered over 30 sessions of a workshop that focuses on process review procedures, and delivered Web conference seminars in the financial management area.

The responsibility for oversight includes monitoring and tracking the cost and schedule elements of a project, as defined in the environmental process, from the design phase to construction completion. The FHWA began monitoring project cost and schedules on projects exceeding $1 billion in costs, called Major projects, in 2000. FHWA is presently monitoring 12 projects that have reached the Initial Financial Plan milestone. As of June 2005, 9 of the projects were within the established budget variance, ranging from 8.24 percent above the base cost estimate to 16.2 percent below. All 10 of the projects are expected to be finished within the variance range of the estimated completion date.

Beginning in 2002, the FHWA began monitoring total cost growth on all large projects, exceeding $10 million in size. Data has been accumulated on projects authorized from FY 2000 through FY 2004. The data indicates that construction projects are generally awarded at a level below the Engineer's Estimate and show a relatively small increase as the projects move to completion. It is not anticipated that the total growth for all projects in this category will increase much beyond 5 percent. The projects authorized in FY 2000 have been underway for 4 to 5 construction seasons; most costs are known by this point. In fact, the growth for projects initiated between FY 2000 and FY 2002 has only risen about 2 percent.

Early in 2005, both the Government Accountability Office (GAO) and the Office of the Inspector General (OIG) raised additional concerns about the Federal Highway Administration (FHWA) oversight of cost and schedule issues on projects funded with Federal-aid resources.[1] While FHWA did agree, in part, with some of the recommendations, the Agency did not agree with the recommendation to convert its Fiscal Management Information System (FMIS) into a Project Management Tracking System. The FMIS is used to track obligations and expenditures on projects or project phases when a State Transportation Agency (STA) elects to use Federal funds as part of the funding package.

To address some of these continuing concerns and take advantage of existing STA project systems, FHWA initiated an effort in June 2005 to develop a more formal, documented approach to Project Delivery Oversight. Each Division Office was directed to survey their respective data systems that contain the

[1] See GAO Report, *Federal-Aid Highways: FHWA Needs a Comprehensive Approach to Improving Project Oversight*, GAO-05-173, January 2005; and the OIG Report, *FHWA Needs to Capture Basic Aggregate Cost and Schedule Data to Improve Its Oversight of Federal-Aid Funds*, No. MH-2005-0046, February 2005.

project cost and schedule management elements. In particular, the Division Offices will assess whether the STA have the needed information for the Agency to perform periodic projects reviews and evaluations on these areas. The results will give FHWA the assurance that future program reviews can access the appropriate project information to effectively monitor project elements using Federal funds.

The FHWA's stewardship and oversight role is strengthened in SAFETEA-LU. The Transportation Secretary is required to establish an oversight program to monitor the effective and efficient use of Federal aid funds. The legislation requires the FHWA conduct an annual review of the State department of transportation financial management systems and project delivery systems, develop minimum standards for estimating project costs and periodically evaluate State practices in these areas. It also places requirements for a Project Management Plan and Financial Plan on all Major projects of $500 million or more, and requires each State to provide a value engineering analysis on each Federal aid project with a total cost of $25 million or more, a bridge project of $20 million or more, and other designated projects.

## 9. CHALLENGE: OVERSIGHT OF THE MARAD TITLE XI LOAN GUARANTEE PROGRAM

The Maritime Administration (MARAD) needs to continue work on implementing the recommendations made on how to best minimize potential financial loss to the $3.8 billion Title XI Loan Guarantee Program.

**REPORTED:** FY 2003

**RESOLVED:** This item resolved in FY 2005.

### MARAD ACTIONS TAKEN TO RESOLVE CHALLENGE:

MARAD and IG staffs have worked closely together to address the issues raised in the audit. These activities have included the development of procedures to monitor the financial condition of borrowers and the assets they finance under the Title XI program. For example, MARAD has developed a Credit Watch Report to more closely monitor and report on the financial condition of Title XI companies that may experience financial difficulties. MARAD has also obligated $2 million for the development of a computer based portfolio monitoring system. Due to these and other efforts undertaken by MARAD, the IG staff has indicated that the recommendations in their audit have been resolved.

## 10. CHALLENGE: STRENGTHENING FINANCIAL MANAGEMENT AND ACCOUNTABILITY

While a lot of work has been accomplished to strengthen financial management, there are still several key areas that the Department needs to continue to improve. Particularly: freeing up dollars in idle funds to be used more productively on active projects, exercising greater stewardship over the $35 billion awarded annually on highway and transit projects, consolidating or replacing fragmented financial systems, and implementing cost accounting systems to help improve operations.

FAA has pledged to have a fully operational cost accounting system and labor distribution system in place by the end of Calendar Year 2005. The agency, however, faces several challenges in reaching that goal: it must revamp the system to account for recent significant organizational changes; deploy the system to new business units; begin associating actual labor costs and other unassigned service costs to specific facilities and activities; and implement financial and performance measures for activities, which are critical to achieving performance efficiencies and cost savings.

**REPORTED:** FY 2003

**RESOLVED:** This item has not been resolved.

### ACTIONS TAKEN TO RESOLVE CHALLENGE:

The fiscal year 2004 audit of the Highway Trust Fund (HTF) identified grants financial management oversight as a material weakness. It had previously been reported as a reportable condition in the FY 2003 audit. FHWA's current Financial Management Improvement Program requires division offices to identify areas needing improvement and then work with the States to make the improvements. The HTF audit stated that the required financial management risk assessment and associated reviews of grantees were not performed in 41 of 45 projects sampled.

In response to the FY 2004 audit findings, the FHWA introduced the Financial Integrity Review and Evaluation (FIRE) Program in April. This program consolidates current financial oversight responsibilities of the Federal-aid division offices into a single directive. It incorporates current requirements to perform a financial management process review, review inactive projects, follow up on audit findings, assure compliance with the Single Audit Act (see below), and assess the accounting and internal controls relating to administrative funds. It also includes new requirements to review a sample of Federal-aid billing transactions and administrative transactions. As a result, Division offices performed the required reviews and analyses, identify areas needing improvements, implement the improvements, report the results annually to the Administrator, and maintain sufficient documentation to support the division office's conclusions and actions taken. Based on the results of the FIRE requirements, the Division Administrator will certify the results of these activities as part of the annual, year-end Section 2 and 4 certification required by the Federal Managers' Financial Integrity Act. Division Offices also completed a risk assessment on the identified financial payment processes but will not be required to perform a grant financial management process review. However, the full requirements of the Order will be in effect during FY 2006.

In compliance with the Single Audit Act, States are required to conduct annual audits of sample grant amounts in excess of $300 thousand dollars to ensure that appropriate controls are in place to identify any payment that should not have been made or that was made for an incorrect amount under statutory, contractual, administrative, or other legally applicable requirements, or to an ineligible recipient. The Single Audit Act requirements, and supporting OMB regulations that States comply with, are insufficient to address and identify improper payments. As a result, the DOT and OMB agreed to better define the criteria that State auditors use to evaluate improper payments and engage State DOT auditors to test the criteria. The results of this research project will be a refinement of OMB's expectations/regulations under the Single Audit Act for use by all State DOT auditors, including possibly the expansion of the definition of an improper payment to include "quality" issues such as "did the design achieve intended results," "did the specifications result in a road condition that will last for X years."

A consulting firm was engaged to conduct this study and the Tennessee DOT is the test State. During March 2005, representatives from OST, FHWA, and the State DOT identified the different phases of a highway project and developed the test criteria specifically for each phase, with emphasis on the construction phase. A Special Advisory Group was established to oversee this research project, which includes the includes DOT Deputy Chief Financial Officer, FHWA Chief Financial Officer, OMB representatives, and the Inspector Generals from the Departments of Labor and Education.

### FAA Actions for Implementing Cost Accounting Systems:

In January 2006, FAA will complete the work to revamp the Cost Accounting System to account for a recent significant organizational change. The system will replace labor assignment business rules with actual labor costs from the Labor Distribution System. This improvement will provide more accurate labor costs using actual time spent to maintain the National Airspace System equipment instead of using current allocation rules based on staffing standards.

FAA plans to implement cost accounting for the Airports and Aviation Safety business units by the end of June 2006. This will complete the implementation of cost accounting for the entire FAA organization.

As part of its cost accounting efforts, FAA will implement financial and performance measures to achieve performance efficiencies and cost savings.

## OTHER REPORTS AND EMERGING ISSUES

### Emerging Issue — Strategic Human Capital Planning

Emerging Issue: GAO has stated that the entire Federal Government faces an impending wave of retirements of long-service, highly competent Federal employees. National demographic projections show the retirement wave will coincide with a reduced labor pool. These circumstances create a large-scale strategic human resource planning challenge. While the exodus of talent will not happen overnight, DOT is planning and acting now to ensure a highly competent, diverse, well-led, and productive workforce at all levels, now and into the future.

While the Inspector General did not cite human capital as a FY 2005 management challenge, he did identify “Meeting Human Resource Needs” as an “emerging issue,” citing specific challenges facing FAA’s controller workforce, and the need for the Federal Highway Administration to balance its changing skill mix.

### GAO Report — Improved Program Management Needed to Address Timely Disposal of Obsolete Ships

GAO: The Maritime Administration has more than 100 obsolete and deteriorating ships awaiting disposal that pose potentially costly environmental threats to the waterways near where they are stored. Congress, in 2000, mandated that MARAD dispose of them by September 30, 2006. While MARAD has various disposal options available, each option is complicated by legal, financial and regulatory factors.

GAO Report 05-264 had three recommendations for executive action to improve MARAD’s ship disposal program:

1) Develop a comprehensive approach to manage MARAD’s ship disposal program that would:

- identify a strategy and an implementation plan to dispose of all existing obsolete ships and future transfers in a timely manner; maximizing the use of all available disposal methods;
- determine the needed resources, the associated funding plan, and specific milestones for this disposal;

- establish a framework for decision making that would delineate roles and responsibilities and establish guidance and procedures;
- identify external factors that could impede program success and develop plans to mitigate them; and
- evaluate annually results and implement corrective actions

2) Regularly communicate MARAD's plan, required resources, and any impediments that require congressional assistance in the mandated reports to Congress.

3) MARAD should change its contracting approach for acquiring ship scrapping services from the use of Program Research and Development Announcements (PRDAs) to an appropriate method.

### MARAD Actions:

MARAD has already taken action on all three recommendations. A Ship Disposal Comprehensive Management Plan (CMP) that addresses the items in the first recommendation is in the final stages of development and will be finalized in first quarter of FY 2006. Upon approval of this CMP, MARAD will be able to proceed further with the second recommendation. MARAD continues to communicate its disposal plan and impediments to the Congress most recently in the mandated reports dated April 2005 and October 2005. Also, if the CMP becomes a mandated requirement through enactment of the House National Defense Authorization Act for FY 2006, the CMP will serve as additional regular communication with the Congress. Finally, MARAD has ceased using PRDAs as a method for acquiring ship scrapping services. Since January 2005, MARAD has been using the Federal Acquisition Regulation (FAR) Test Program for Certain Commercial Items "Standing Quotations." The use of Standing Quotations is a simplified acquisition procedure for the competitive procurement of commercial services.


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