U.S. ELECTION ASSISTANCE COMMISSION
OFFICE OF INSPECTOR GENERAL

FINAL AUDIT REPORT:

ADMINISTRATION OF PAYMENTS RECEIVED UNDER THE HELP AMERICA VOTE ACT BY THE TEXAS SECRETARY OF STATE

Report No.
E-HP-TX-06-06
October 2006

U.S. ELECTION ASSISTANCE COMMISSION
OFFICE OF INSPECTOR GENERAL
1225 New York Ave. NW - Suite 1100
Washington, DC 20005

October 18, 2006

Memorandum

To: Thomas Wilkey
Executive Director

From: Curtis Crider *Curtis W. Crider*
Inspector General

Subject: Final Audit Report on the Administration of Payments Received Under the Help America Vote Act by the Texas Secretary of State (Assignment No. E-HP-TX-06-06)

This report presents the results of the subject audit. The objectives of the audit were to determine whether Texas (1) expended Help America Vote Act (HAVA) payments in accordance with the Act and related administrative requirements and (2) complied with the HAVA requirements for replacing punch card or lever voting machines, for appropriating a 5 percent match for requirements payments, for establishing an election fund, and for maintaining state expenditures for elections at a level not less than expended in fiscal year 2000.

The report concluded that Texas generally complied with requirements and identified two areas needing management attention, as follows:

- ✓ Texas financed indirect costs with HAVA funds before the Election Assistance Commission (EAC) approved the State's indirect cost rate. This resulted in the improper use of HAVA funds of $180,609 for indirect costs which we classified as questioned costs.

- ✓ Texas needed to take additional steps to ensure that income from county leasing of HAVA-financed voting equipment is accurately computed, reported and properly used.

In an October 12, 2006 response to the draft report (Appendix 3), Texas stated that it had completed appropriate action to resolve the indirect costs finding and was waiting for EAC approval of its measures. Regarding program income, Texas requested approval from EAC to offset the cost of generating gross program income to determine net program income.

Please provide us with your written response to the recommendations included in this report by December 22, 2006. Your response should contain information on actions taken or planned, including target dates and titles of EAC officials responsible for implementing the recommendations

Section 5(a) of the Inspector General Act (5 U.S.C. § App.1) requires the Office of Inspector General to list this report in its semiannual report to Congress.

If you have any questions regarding this report, please call me at (202) 566-3125.

BACKGROUND

HELP AMERICA VOTE ACT

The Help America Vote Act of 2002 (HAVA or the Act) created the U.S. Election Assistance Commission (EAC or Commission) to assist states and insular areas with the administration of Federal elections and to provide funds to states to help implement these improvements. HAVA authorizes payments to states under Titles I and II, as follows:

- ✓ Title I, Section 101 payments are for activities such as complying with Title III of HAVA for uniform and nondiscriminatory election technology and administration requirements, improving the administration of elections for Federal office, educating voters, training election officials and poll workers, and developing a state plan for requirements payments.

- ✓ Title I, Section 102 payments are available only for the replacement of punchcard and lever action voting systems.

- ✓ Title II, Section 251 requirements payments are for complying with Title III requirements for voting system equipment; and for addressing provisional voting, voting information, statewide voter registration lists, and voters who register by mail.

Title II also requires that states must:

- ✓ Have appropriated funds “equal to 5 percent of the total amount to be spent for such activities [activities for which requirements payments are made].” (Section 253(b)(5)).

- ✓ “Maintain the expenditures of the State for activities funded by the [requirements] payment at a level that is not less than the level of such expenditures maintained by the State for the fiscal year ending prior to November 2000.” (Section 254 (a)(7)).

- ✓ Establish an election fund for amounts appropriated by the state “for carrying out the activities for which the requirements payment is made,” for the Federal requirements payments received, for “such other amounts as may be appropriated under law,” and for “interest earned on deposits of the fund.” (Section 254 (b)(1)).

FUNDING FOR TEXAS

HAVA funds received and expended by Texas are as follows:

TYPE OF PAYMENT	*AMOUNT RECEIVED*	*OUTLAYS*	
		AMOUNT	*AS OF*[1]
101	$17,206,595	$841,251	12/31/05
102	6,269,521	4,219,039	12/31/05
251	160,691,949	24,852,392	09/30/05
Totals	$184,168,065	$29,912,682	

FINANCIAL MANAGEMENT REQUIREMENTS

Within the Office of the Texas Secretary of State, HAVA programs are administered by the Elections Division and the Administrative Services Division. To account for the HAVA payments, the Act requires recipients to maintain records that are consistent with sound accounting principles, that fully disclose the amount and disposition of the payments, that identify project costs financed with the payments and with other sources, and that will facilitate an effective audit.

In addition, the Commission notified states of other management requirements. Specifically, that states must:

- ✓ Comply with the *Uniform Administrative Requirements for Grants and Cooperative Agreements with State and Local Governments* (also known as the "Common Rule").

- ✓ Expend payments in accordance with cost principles for establishing the allowability or unallowability of certain items of cost for federal participation issued by the Office of Management and Budget (OMB) in Circular A-87.

- ✓ Submit annual financial reports on the use of Title I and Title II payments.

OBJECTIVE

The objectives of our audit were to determine whether Texas (1) expended HAVA payments in accordance with the Act and related administrative requirements and (2) complied with the HAVA requirements for replacing punch card or lever voting machines, for establishing an election fund, for appropriating a 5 percent match for requirements payments, and for maintaining state expenditures for elections at a level not less than expended in fiscal year 2000. Specifically, we audited expenditures from May 1, 2003 through

[1] EAC requires states to submit annual reports on the expenditure of HAVA Sections 101, 102, and 251 funds. For Sections 101 and 102, reports are due on February 28 for the activities of the previous calendar year. For Section 251, reports are due by March 30 for the activities of the previous fiscal year ending on September 30.

December 31, 2005, and reviewed controls to assess their adequacy over the expenditure of HAVA funds. We also evaluated compliance with certain HAVA requirements for the following activities:

- ✓ Accumulating financial information reported to EAC on the Financial Status Reports (Standard Forms number 269).
- ✓ Accounting for property.
- ✓ Purchasing goods and services.
- ✓ Accounting for salaries.
- ✓ Charging indirect costs.
- ✓ Spending by counties.

We also determined whether Texas had complied with the requirements in HAVA applicable to Section 251 requirements payments for:

- ✓ Establishing and maintaining the election fund.
- ✓ Appropriating funds equal to five percent of the amount necessary for carrying out activities financed with Section 251 requirements payments.
- ✓ Sustaining the State's level of expenditures for elections.

RESULTS OF AUDIT

SUMMARY

We concluded that Texas (1) generally administered HAVA funds in accordance with requirements and (2) properly established the State election fund, appropriated and deposited into the election fund its matching monies, and sustained the appropriate level of state expenditures for elections. Also, our audit identified two areas regarding the management of HAVA funds that need further attention. First, Texas financed indirect costs with HAVA funds before EAC approved the State's indirect cost rate. This resulted in the improper use of HAVA funds of $180,609 for indirect costs which we classified as questioned costs. Second, we found that the State needs to take additional steps to ensure that income from county leasing of HAVA-financed voting equipment is accurately computed, reported and properly used.

INDIRECT COSTS

Texas reported on the Financial Status Report (SF-269) for HAVA Section 101 funds for the period ending December 31, 2005, the expenditure of $180,609 for indirect costs. The SF-269 indicated that the indirect costs were based on a provisional rate of 49.768 percent applied to a base of $362,901. Although Texas had submitted its indirect cost rate proposal to EAC, EAC had not yet approved the rate. Federal cost principles contained in OMB Circular A-87 require an indirect cost rate to be approved by the cognizant Federal agency (EAC) before the rate is used.[2] As such, we questioned the use of HAVA funds for indirect costs of $180,609.

Notwithstanding the lack of an approved indirect cost rate, we noted that Texas incorrectly calculated indirect costs. Specifically, Texas applied the proposed rate of 49.768 percent to total direct costs less payments to counties resulting in the $180,609 charge for indirect costs. However, the Texas indirect cost proposal specifies that the rate will be applied to only personal services costs, which would result in a lesser charge for indirect costs.

Texas made adjustments to its reported indirect costs after we informed them of our finding. On July 6, 2006, Texas submitted amended SF-269s to EAC in which it reduced its indirect charge from $180,609 to $62,223. Texas based its reduction on the application of its current pending rate of 48.548 percent applicable to personal services of $128,168. This calculation reflects the proper application of the rate. Therefore, if EAC approves an indirect cost rate of 48.548 percent for fiscal years 2004 and 2005, Texas has made the proper adjustments and no further action is necessary regarding this matter.

In response to this finding, Texas stated that it had:

> received the EAC Cognizant Agency Indirect Cost Negotiation Agreement Filing Ref: TX-SFY05-06 dated September 19, 2006 approving the indirect cost rate of 48.548 percent. As noted in the audit report, the SOS has already made the accounting adjustment to reflect the 48.548 percent rate. Accordingly, the SOS requests that the EAC conclude that no further action is necessary.

Recommendation:

1. We recommend that EAC resolve the questioned costs of $180,609.

PROGRAM INCOME

Program income has not been properly computed, reported and (if applicable) used to support HAVA-related activities. According to the *Uniform Administrative Requirements for Grants and Cooperative Agreements with State and Local Governments* (41 CFR 105-71.125), program income is defined as gross income received from a grant-supported activity during the grant period and includes items such as

[2] OMB Circular A-87, Attachment E, Part E.1 requires indirect cost rates to be reviewed, negotiated and approved by the cognizant Federal agency before it will be accepted and used by all Federal agencies.

fees from the use or rental of real or personal property acquired with grant funds. In the case of the HAVA program, the grant-supported activity is the acquisition of voting machines. And, according to a December 28, 2005 EAC letter to the Texas Secretary of State, the grant period started on the date HAVA funds were disbursed to the State (May 1, 2003 for 102 funds and June 15, 2004 for 251 funds) and will end on the date that the State and/or a political subdivision of the State expends all the funds received (which has yet to occur).

The Uniform Administrative Requirements also stipulate, in part, that the costs incident to the generation of program income may be deducted from gross income to determine program income, if authorized by Federal regulations or the grant agreement.

Computation: Three of the four counties we visited during our audit collected revenue that included program income. For example, Texas granted Harris County about $21 million as reimbursement for the purchase of HAVA-compliant voting equipment. Harris County has subsequently entered into lease agreements with local governments, such as the City of Houston and county school districts, to support elections. The lease agreements included fees for election judges, supervisors, clerks, training booklets, postage, technical support, polling places, printing and supplies, rental of voting equipment, and several similar items. Harris County lease revenues beginning in fiscal year 2004 are as follows:

Fiscal Year	Amount
2003 - 2004	$4,423,593
2004 - 2005	3,924,776
2005 - 2006	2,538,523
2006 - 2007	178,095
Total	$11,064,987

To compute program income, an analysis must be performed that:

- ✓ Determines the specific grant periods for 102- and 251-funded voting equipment included in the leases. (The periods will differ because the funds were received by Texas on different dates.)
- ✓ Determines gross revenues applicable to only the use of HAVA-funded equipment from total lease revenue.
- ✓ Identifies the costs of generating the gross program income

applicable to the HAVA-funded activities.

- ✓ Reduces, subject to EAC approval, gross program income by the applicable costs.

Reporting: Both the federal Standard Form 269 and the Texas online grant application, approval, and payment system provide for reporting program income. However, none of the counties we visited reported any program income. Texas should ensure that its counties accurately report program income for subsequent reporting to EAC.

Use: In its December 28, 2005 letter to Texas, EAC said that counties which generate program income should dedicate the income to uses permitted under HAVA, Section 251. In this regard, we noted that Harris County deposited the revenue from its support of local elections into its general fund. Therefore, counties with program income should establish a separate fund that reserves the income for uses only as authorized under HAVA, Section 251.

Although Texas incorported into its grant agreements the Uniform Administrative Requirements and also had a separate section in the agreements on program income, its guidance was prepared before EAC defined the grant period. Thus, state guidance did not identify the parameters for determining program income.

Recommendations:

We recommend that EAC ensure that the Texas Office of the Secretary of State:

2. Provides guidance to counties on computing, reporting, and using program income.

3. Ensures that counties follow the guidance for program income.

SCOPE AND METHODOLOGY

To accomplish our objective, we reviewed:

- ✓ The prior single audit report and other reviews related to the Secretary of State's financial management systems and the HAVA program for the last 2 years.
- ✓ Policies, procedures and regulations for the Texas Secretary of State's management and accounting systems as they relate to the administration of HAVA programs.
- ✓ Inventory lists of equipment purchased with HAVA funds.
- ✓ Major purchases.
- ✓ Supporting documents maintained in the accounting system for payments made with HAVA funds.
- ✓ Support for reimbursements to counties.
- ✓ Certain Texas laws that impacted the election fund.
- ✓ Appropriations and expenditure reports for State funds used to maintain the level of expenses for elections at least equal to the amount expended in fiscal year 2000 and to meet the five percent matching requirement for section 251 requirements payments.
- ✓ Information regarding source/supporting documents kept for maintenance of effort and matching contributions.

We also interviewed appropriate Division employees about the organization and operation of the HAVA program.

We conducted our review in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. As such, we included tests and procedures as considered necessary under the circumstances to evaluate the Division's controls over the administration of HAVA payments. Because of inherent limitations, a study and evaluation made for the limited purposes of our review would not necessarily disclose all weaknesses in administering HAVA payments.

MONETARY IMPACT

Description	*Questioned Costs*
Indirect Costs	$180,609

The State of Texas

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October 12, 2006

Mr. Roger La Rouche
US Election Assistance Commission Acting Inspector General
1225 New York Ave. NW – Suite 1100
Washington, DC 20005

RE: HELP AMERICA VOTE ACT "HAVA" REPORT NO. E-HP-TX-06-06

Dear Mr. La Rouche:

Enclosed for your review are the written comments to the findings issued in the draft report entitled "Administration of Payments Received Under the Help America Vote Act by the Texas Secretary of State" Assignment No. E-HP-TX-06-06.

Thank you for your visit to Texas and the assistance you provided to my staff. If you have any additional questions, please do not hesitate to contact my office.

Sincerely,

Roger Williams
Texas Secretary of State

Cc: Paul DeGregorio, Chairman US Election Assistance Commission
Tom Wilkey, Executive Director US Election Assistance Commission

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Texas Secretary of State

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Tom Wilkey, Executive Director US Election Assistance Commission

TEXAS SECRETARY OF STATE COMMENTS
DRAFT AUDIT REPORT
ADMINISTRATION OF PAYMENTS RECEIVED UNDER
THE HELP AMERICA VOTE ACT BY THE TEXAS SECRETARY OF STATE
ASSIGNMENT NO. E-HP-TX-06-06

INDIRECT COSTS – AUDIT RESULT

The EAC Office of Inspector General reported the following:

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> ***Recommendation:***
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SOS Management Response:

The SOS received the EAC Cognizant Agency Indirect Cost Negotiation Agreement Filing Ref: TX-SFY05-06 dated September 19, 2006 approving the indirect cost rate of 48.548 percent. As noted in the audit result, the SOS has already made the accounting adjustment to reflect the 48.548 percent rate. Accordingly, the SOS requests that the EAC conclude that no further action is necessary.

PROGRAM INCOME – AUDIT RESULT

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Computation: Three of the four counties we visited during our audit collected revenue that included program income. For example, Texas granted Harris County about $21 million as reimbursement for the purchase of HAVA-compliant voting equipment. Harris County has subsequently entered into lease agreements with local governments, such as the City of Houston and county school districts, to support elections. The lease agreements included fess for election judges, supervisors, clerks, training booklets, postage, technical support, polling places, printing and supplies, rental of voting equipment, and several similar items. Harris County lease revenues beginning in fiscal year 2004 are as follows:

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Recommendation:

We recommend that the EAC ensure that the Texas Office of the Secretary of State:

1. Provides guidance to counties on computing, reporting, and using program income.

2. Ensures that counties follow the guidance for program income.

SOS Management Response:

Pursuant to the Uniform Administrative Requirements, gross program income must be reduced, subject to EAC approval, by the costs to generate the gross program income. In other words, the costs to maintain the HAVA-compliant voting equipment should reduce the program income generated by leasing the equipment.

The SOS submitted a letter dated August 1, 2006 to the EAC requesting that Texas be allowed to deduct costs incurred as a result of earning program income. Furthermore, it is our estimation that the expenses incurred by counties as a result of supporting and maintaining the new HAVA-mandated equipment exceed earned program income. Pending the response to that inquiry, the SOS will instruct the counties on how to compute, report, and use program income. In addition, the SOS reviews compliance with program income guidelines as part of its current monitoring program.

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