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Subcommittee on Transportation, Housing and  
Urban Development, and Related Agencies  
United States Senate**

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# **American Recovery and Reinvestment Act: DOT's Implementation Challenges and the OIG's Strategy for Continued Oversight of Funds and Programs**

**Statement of  
The Honorable Calvin L. Scovel III  
Inspector General  
U.S. Department of Transportation**



Chairman Murray and Ranking Member Bond:

Thank you for the opportunity to testify today on the challenges facing the Department of Transportation's (DOT) implementation of the American Recovery and Reinvestment Act (ARRA) of 2009<sup>1</sup> and our office's related audit and investigative initiatives. We appreciate the \$20 million in additional funding that the Committee provided to our office to conduct audits and investigations of DOT projects and activities funded by ARRA. This additional funding will go a long way in ensuring that we have the staff, travel budget, information technology, and other resources that we need to help achieve new, ARRA-related goals, meet our increased workload and protect the Federal investment over the long term. Since the passage of ARRA, we have been working with DOT officials to support and oversee their efforts and have assembled a cross-modal team of auditors, analysts, investigators, and attorneys to review DOT's management of recovery program funds.

ARRA designates an unprecedented \$48 billion for DOT programs, adding new challenges on top of the longstanding ones we have highlighted in past reports to the Secretary of Transportation and Congress. These include overseeing numerous grantees and projects across the country as the recovery funding is infused into the economy. In addition to significantly increasing funding for certain DOT programs, ARRA directs DOT to create several new programs and establishes tight timeframes for distributing and expending funds and reporting results, such as the number of jobs created. The Office of Management and Budget (OMB) also mandated additional requirements, including weekly financial reports, which will test DOT's capacity as it strives to effectively implement these changes.

Both the President and Congress have emphasized the need for accountability, efficiency, and transparency in the allocation and expenditure of ARRA funds and have recognized the role of Inspectors General and the Government Accountability Office (GAO) in accomplishing these objectives. For example, ARRA created the Recovery Accountability and Transparency Board, consisting of our office and nine other Inspectors General, and added substantial funding to help address the increased workload. We want to acknowledge this Committee's strong interest in vigilant oversight of the recovery program, with this hearing as just one of the many indicators of that support.

We realize the enormity of the challenges facing DOT and note the commitment of the Secretary of Transportation and his staff to the success of DOT's recovery initiatives. DOT's leadership has been proactive on several fronts. For example, the Department has established the DOT-wide Transportation Investment Generating Economic Recovery (TIGER) team to coordinate DOT's role in the recovery program, ensure accountability, and develop a risk management and financial

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<sup>1</sup> Pub. L. No. 111-5 (2009).

reporting plan. In addition, DOT officials are working with grantees so they can quickly submit proposals that will meet Federal requirements. DOT is also evaluating how to redeploy current agency employees or use “rehired annuitants” to meet the increased workload and conducting outreach to field staff and grantees through frequently-asked-questions and guidance posted on DOT’s recovery internet sites. Sustained leadership will be a prerequisite for continuing to meet the numerous issues facing DOT.

Our statement today focuses on the specific challenges DOT faces as it implements ARRA and our strategy to promote effective and efficient use of funds. Specifically:

- **DOT must continue to address the significant oversight challenges posed by ARRA.** Last month, we reported on the major challenges facing DOT in ensuring that ARRA funds are spent properly and identified actions DOT should take now to support ARRA requirements (see attachment for the full report).<sup>2</sup> This report was based on a comprehensive review of our prior reports and other relevant work. Based on our analysis, we concluded that DOT must exhibit sustained and effective actions to oversee grantees receiving ARRA funding; implement significant new reporting requirements and programs mandated by ARRA; and prevent fraud, waste, and abuse. Actions needed to address these challenges include acquiring sufficient staff with relevant expertise to oversee grantees; developing comprehensive plans and sound criteria for the more than \$9 billion in new programs created by ARRA; and enhancing understanding among DOT staff, grantees, and their contractors on how to recognize, prevent, and report potential fraud to the appropriate authorities.

In addition to serving as “one-stop shopping” for actions DOT must take now to achieve ARRA-related goals, our report set out a roadmap for our future audit and investigative initiatives. In response to our recommendation to develop a plan to address the issues in our report, DOT committed to providing us with a document by April 30, 2009, that will outline its specific actions taken or planned.

- **Our audit and investigative initiatives must continue to examine areas that present the greatest risks and promptly notify DOT and Congress of actions needed to minimize fraud, waste, and abuse and achieve ARRA goals.** We have begun working aggressively to position our office to handle the increased workload. In anticipation of ARRA’s passage, we initiated a three-phase approach to conducting related work. We completed Phase 1 last month with the issuance of our report on key oversight challenges facing DOT. We also identified several audits that, although started prior to ARRA’s passage, have a direct connection to

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<sup>2</sup> OIG Report Number MH-2009-046, “American Recovery and Reinvestment Act of 2009: Oversight Challenges Facing the Department of Transportation,” March 31, 2009. OIG reports and testimonies are available on our website: [www.oig.dot.gov](http://www.oig.dot.gov).

the programs funded under ARRA and related requirements. We plan to fast-track the most time-sensitive results of our work on these audits to ensure we provide DOT, Congress, and taxpayers with timely and relevant information.

Phase 2 of our strategy is underway and involves a systematic scan, or structured survey, of the DOT agencies that received funding in ARRA, based on 10 focus areas identified in our report. These scans will examine vulnerabilities in program management and planning that could impede DOT's ability to provide effective oversight of ARRA-funded projects and meet new statutory and OMB requirements. We plan to begin reporting the results of Phase 2 this summer through a series of ARRA advisories to the Department. Phase 3 is a long-term initiative in which we will drill down on high-risk areas that emerge as a result of our agency scans.

I will now discuss these issues in further detail.

## **DOT MUST CONTINUE TO ADDRESS THE SIGNIFICANT OVERSIGHT CHALLENGES POSED BY ARRA**

In anticipation of ARRA's passage, we initiated a comprehensive review of our prior audit and investigative work—as well as the relevant work of other accountability organizations—to identify the major challenges facing DOT as it implements such a large infusion of new funding and program requirements. We reported the results of our review last month: *American Recovery and Reinvestment Act of 2009: Oversight Challenges Facing the Department of Transportation*. Our report linked the challenges identified to 10 specific focus areas where DOT must exhibit sustained and effective actions and oversight; these areas are shown in table 1 on the next page. (The full report is presented as an attachment to this statement.)

Based on our analysis of past findings, we see three major ARRA oversight challenges facing DOT:

- Ensuring that DOT's grantees properly spend ARRA funds;
- Implementing new accountability requirements and programs mandated by ARRA in an effective manner; and
- Combating fraud, waste, and abuse.

To ensure sufficient consideration of the potential risks discussed in this report, we also recommended that the Secretary of Transportation, through the DOT TIGER team, develop an oversight implementation plan that outlines the key actions DOT has underway or will take to address these issues. DOT agreed to provide us with a document by April 30, 2009, outlining actions taken or planned in these areas.

**Table 1. Major ARRA Challenges and Related Focus Areas for DOT**

<p><b>Ensuring that DOT’s grantees properly spend ARRA funds</b></p>	<ol style="list-style-type: none"> <li>1. Acquire sufficient personnel with relevant expertise to oversee grantees.</li> <li>2. Adhere to existing Federal requirements for programs funded under ARRA.</li> <li>3. Evaluate the credibility and completeness of cost and schedule estimates.</li> <li>4. Oversee grantees’ contracting management activities and ensure selection of appropriate contract types.</li> <li>5. Address internal control weaknesses and identify unused funds for use on other eligible projects.</li> </ol>
<p><b>Implementing new accountability requirements and programs mandated by ARRA in an effective manner</b></p>	<ol style="list-style-type: none"> <li>6. Implement new ARRA tracking and reporting requirements that are designed to promote accountability and transparency.</li> <li>7. Develop comprehensive plans and sound criteria for the new discretionary grant and passenger rail programs within statutory deadlines.</li> <li>8. Develop appropriate oversight strategies for the new discretionary grant and passenger rail programs.</li> </ol>
<p><b>Combating fraud, waste, and abuse</b></p>	<ol style="list-style-type: none"> <li>9. Enhance understanding among DOT staff, grantees, and their contractors on how to recognize, prevent, and report potential fraud to the appropriate authorities.</li> <li>10. Take timely and effective action to suspend or debar individuals or firms that have defrauded the Department so they do not receive future Federal contracts.</li> </ol>

Today, I will highlight a few of the key areas where action is needed.

**Ensuring That DOT’s Grantees Properly Spend ARRA Funds**

The large amounts of funding that DOT is responsible for under ARRA and the accelerated timeframes to use those funds will place great demands on DOT’s workforce, oversight processes, and financial management systems. Some of the more significant challenges relate to ensuring that DOT’s Operating Administrations

oversee grantees' contract management activities; addressing internal weaknesses that could lead to ineffective use of ARRA dollars; and having sufficient staff with relevant expertise to monitor grantees' planning and execution of ARRA-funded projects. We are encouraged by Secretary LaHood's statement that DOT is committed to do things "by the book," follow established policies and procedures, and employ sound business practices.

### *Overseeing Grantees' Contracting Management Activities and Ensuring Selection of Appropriate Contract Types*

Oversight of grantees' contracting management practices warrants particular attention as the ARRA program is quickly rolled out. Actions needed are (1) specifying contract requirements early; (2) maximizing competition; (3) using appropriate contract types; and (4) preventing unallowable costs, improper payments, and excessive overhead charges during contract execution. The magnitude and the accelerated pace for spending ARRA dollars could exacerbate contract award problems we previously identified, which include inappropriate contract types, inadequate competition, and failure to ensure contract prices are fair and reasonable.

Our basis for these concerns resides in several examples. Specifically, audits of DOT and state contracts used to respond to the Hurricane Katrina emergency found instances in which DOT money was spent inefficiently. This occurred because grantees used risky contracting methods in spending Federal funds, such as sole-sourced contracts, which resulted in significantly higher costs.<sup>3</sup> For example, we found that a state department of transportation awarded two sole-source contracts without assurance of fair and reasonable prices, which resulted in the state paying about \$1.7 million more than necessary for bridge repairs. Our review of controls over DOT's contract for Hurricane Katrina emergency disaster relief transportation, also found that a Federal Aviation Administration (FAA) contracting officer routinely authorized invoices for payment without any documentation from the contractor showing that the services had actually been provided.<sup>4</sup> In one instance, this lack of controls resulted in a \$33 million overpayment to the contractor for emergency bus transportation and chartered aircraft services; the overpayment was later recovered.

### *Addressing Internal Control Weaknesses and Identifying Unused Funds for Other Eligible Projects*

DOT needs to assess risks and identify and mitigate any internal control<sup>5</sup> weaknesses to ensure that ARRA funding is spent effectively in accordance with Federal

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<sup>3</sup> OIG Report Number MH-2006-065, "Audit of the Mississippi Department of Transportation's Award of Selected Hurricane Katrina Emergency Repair Contracts," September 6, 2006.

<sup>4</sup> OIG Report Number AV-2006-032, "Internal Controls Over the Emergency Disaster Relief Transportation Services Contract," January 20, 2006.

<sup>5</sup> Internal controls provide reasonable assurance of the effectiveness and efficiency of an agency's use of financial resources, the reliability of financial reporting, and compliance with applicable laws and regulations.

regulations and OMB's new requirements. Specifically, OMB is requiring that agencies ensure the prompt award and outlay of ARRA dollars and minimize improper payments. Going forward, DOT must ensure that its risk mitigation plans prevent new and recurrent internal control weaknesses, identify unused funds promptly, ensure timely action to free up unused funds for use on other projects, and detect and prevent improper payments. Our prior and ongoing audit work shows that DOT has experienced problems in these areas.

In particular, we have found that DOT must improve its controls for identifying unused funds in its financial management systems and take appropriate action to release them on completed, cancelled, and reduced-scope projects. For example, in fiscal year (FY) 2008, auditors found idle funds at the Federal Highway Administration (FHWA) estimated at about \$300 million. Similarly, we found that in 2007 FAA allowed numerous Airport Improvement Program grants to remain inactive and obligations to remain on closed grants, both for excessive periods of time.<sup>6</sup> Without sufficient controls going forward, any unused ARRA funds could remain idle for long periods of time. This in turn could prevent other worthy projects from receiving Federal funds and potentially undermine ARRA's ability to stimulate the U.S. economy by quickly spurring construction activity across the country.

Avoiding improper payments also presents a continuing challenge to DOT. For example, our prior work at FHWA identified oversight weaknesses that led to such payments, which DOT must avoid in the ARRA program. Specifically, we examined FHWA's oversight of design and engineering (D&E) firms' indirect costs claimed on Federal-aid grants and found that Federal funds were used to reimburse unallowable costs totaling nearly \$16 million.<sup>7</sup> This occurred in part due to ineffective oversight by FHWA and state transportation departments of the certified public accounting firms hired by the D&E firms. As OMB stipulated in its implementation guidance,<sup>8</sup> it is critical to mitigate the risks of improper payments in the recovery program to ensure that DOT maximizes the return on the Federal investment.

### *Acquiring Sufficient Personnel With Relevant Expertise To Oversee Grantees*

DOT must ensure that it has sufficient personnel with relevant expertise to meet the increased workload, new requirements, and accelerated timeframes associated with recovery spending. A sufficient and trained workforce is critical to hold grantees accountable for contract actions and realistic cost and schedule estimates and to ensure that state or local recipients can effectively manage their projects and the risks associated with the recovery program.

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<sup>6</sup> OIG Report Number AV-2007-073, "FAA's Oversight of Inactive Airport Improvement Program Grant Obligations," September 13, 2007.

<sup>7</sup> OIG Report Number ZA-2009-033, "Oversight of Design and Engineering Firms' Indirect Costs Claimed on Federal-Aid Grants," February 5, 2009.

<sup>8</sup> OMB, "Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009," April 3, 2009.

DOT officials expressed concerns about their ability to provide sufficient oversight with limited time and staff, particularly in regional and division offices, and noted actions under consideration. For instance, some Operating Administrations may detail staff from each of their headquarters to their regional and division offices and rehire retired Federal employees on a temporary basis. These efforts were supported when the Office of Personnel Management granted DOT direct-hire authority and delegated to it dual compensation waiver authority. These hiring flexibilities should help enable DOT to meet critical hiring needs. The key will be to utilize these flexibilities effectively to augment other staffing actions. We plan to evaluate the adequacy of DOT's workforce as part of our future audits on DOT's oversight of ARRA projects.

### **Implementing New Reporting Requirements and Programs Mandated by ARRA in an Effective Manner**

In addition to increasing the funding levels of existing programs, ARRA presents new goals for DOT. First, ARRA mandates several new reporting requirements that are designed to promote accountability and transparency, which OMB enhanced in its recent implementation guidance. Second, ARRA creates two new, large programs that provide \$1.5 billion in supplementary discretionary grants to improve the Nation's transportation infrastructure and \$8 billion in grants for high-speed rail corridors and intercity passenger rail service.<sup>9</sup> These programs are being designed from the ground up and, therefore, pose particular vulnerabilities for DOT.

#### *Implementing New ARRA Tracking and Reporting Requirements Designed To Promote Accountability and Transparency*

To meet ARRA accountability and transparency requirements, DOT must ensure that its financial management systems can track ARRA spending and produce reliable information to report results in a meaningful way. Specifically, DOT must ensure that its financial management systems can clearly and reliably track recovery funds separately from other program funds, as required by OMB. This will be important as OMB's guidance requires agencies to submit regular reports, and the information to generate these reports will come largely from DOT's financial management systems.

For example, OMB's final implementation guidance requires DOT to provide weekly Financial and Activity Reports that provide, by Treasury Account, total obligations and total outlays as recorded in agency financial systems on a cumulative basis. These reports will also provide a bulleted list of the major actions taken or planned. In addition, DOT will need to develop processes for meeting OMB requirements to report on the number of jobs created or preserved. Some ARRA information will be

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<sup>9</sup> ARRA stipulates that the discretionary grant program can be used for a variety of projects, including highway, bridge, public transportation, passenger and freight rail, or port infrastructure projects.

available publicly on the Administration's website, [www.recovery.gov](http://www.recovery.gov),<sup>10</sup> and therefore must meet DOT and OMB data quality requirements. These requirements underscore the need for DOT to adjust its financial management systems so that they provide reliable and complete management reports that DOT staff can use to effectively guide and oversee grantees.

In the past, DOT has experienced challenges in this area. For example, in September 2007 we testified that FHWA was unable to determine how much of the billions of dollars in Highway Bridge Program funding were actually spent on structurally deficient bridges, because its financial management system did not differentiate between spending on structurally deficient bridges and other bridge-related expenditures.<sup>11</sup> In this case, the absence of sufficient management-level information inhibited FHWA's ability to assess the impact of Federal dollars on bridge conditions. We are working on a follow-up audit to assess FHWA's bridge funding and oversight activities in greater detail.

### *Developing Comprehensive Plans and Sound Criteria for the New Discretionary Grant and Passenger Rail Programs Within Statutory Deadlines*

Creating and executing the new programs called for by ARRA presents a huge challenge for DOT. Meeting statutory deadlines will be difficult due to the number of tasks that must be completed in short timeframes, including quickly producing planning documentation and guidance. ARRA directs the Office of the Secretary of Transportation (OST) to publish criteria for its grant program within 90 days of ARRA enactment, accept applications for grants within 180 days after the criteria are published, and announce all projects selected within 1 year of ARRA enactment. Further, ARRA requires the Federal Railroad Administration (FRA) to produce a strategic plan for the passenger rail program within 60 days of ARRA enactment and interim implementation guidance to applicants within 120 days.

We have reviewed the strategic plan FRA released on April 16. We are cognizant that FRA had a limited timeframe in which to prepare the plan and believe the plan provides a meaningful, broad vision for the program and recognizes many of the risks inherent in implementing this program. However, the plan lacks detailed strategies for achieving its goals and performance measures to evaluate progress towards those goals. The interim performance guidance will provide an additional near-term opportunity for FRA to address these issues.

To meet deadlines for the discretionary grant program, the Secretary established a working group within OST to develop criteria and determine the best administrative

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<sup>10</sup> The Administration created this website to provide information to the public on the planning and implementation of ARRA.

<sup>11</sup> OIG Testimony Number CC-2007-095, "Federal Highway Administration's Oversight of Structurally Deficient Bridges," September 5, 2007.

structure. OST also has an advisory task force comprised of staff from the Operating Administrations. According to DOT officials, a central issue for the task force is determining the most appropriate place to administer the grants—within OST or the Operating Administration that would normally be responsible for a particular type of project. For example, if OST delegates administrative responsibility for a bridge replacement project to FHWA, it would need to monitor how this delegation of authority is effectively achieving the established goals and requirements of ARRA.

FRA also faces daunting challenges because it has not previously implemented a program like the large-scale, high-speed passenger rail program called for in ARRA. FRA has begun establishing specific plans for this program. These include determining how to allocate the funds among the eligible purposes<sup>12</sup> and developing program guidance within the statutory timeframes. Because FRA is a small agency that had few grant programs before ARRA was passed, it is critical for FRA staff to leverage the in-house expertise throughout DOT and determine what additional resources it may need. To design and implement this program, FRA must, for example, establish sufficient controls to ensure that Federal investments do not simply supplant investments the freight railroads already planned to undertake on their rail lines.

### **Combating Fraud, Waste, and Abuse**

DOT needs to tailor its counter-fraud efforts to adapt to the increase in capital funding associated with the recovery program and the expected surge in construction activity throughout the country. OMB's guidance for ARRA implementation directs Federal agencies to be aggressive in preventing fraud, waste, and abuse. This requires sustained action in two key areas, discussed below.

#### *Enhancing Understanding Among DOT Staff, Grantees, and Their Contractors on How To Recognize, Prevent, and Report Potential Fraud*

DOT must target its outreach efforts at deterring fraud schemes that we have seen with past DOT projects and must be avoided with projects receiving funding under ARRA. These include false claims for materials and labor, bribes related to contracts for materials or labor, and product substitution.<sup>13</sup> An important way to deter fraud is for DOT staff and grantees to be aware of certain “red flag” indicators typically associated with fraud schemes. For example, a contractor regularly taking or labeling quality control samples away from inspector oversight or insisting on transporting these samples from the construction site to a lab might indicate quality control testing fraud.

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<sup>12</sup> According to FRA, the \$8 billion can be used for three programs: (1) high-speed corridor program, (2) intercity passenger rail service grants, and (3) congestion grants.

<sup>13</sup> Our March 2009 report, which is attached to this statement, contains a list of common fraud schemes and fraud indicators.

One significant case we were involved with illustrates this type of fraud. In this case, an Indiana contractor agreed to pay more than \$8.2 million to settle Federal and state claims alleging that a contractor fraudulently swapped samples of asphalt to inflate the amount paid on road projects by FHWA, the Commonwealth of Kentucky, and the State of Indiana. This joint investigation, conducted with FHWA and the U.S. Attorney's Office for the Western District of Kentucky, revealed that the contractor's employees fraudulently swapped "good" cores for "bad" cores (i.e., cores with failing density).

The best way to make individuals aware of fraud schemes and their indicators is to conduct systematic fraud prevention education. DOT and the Operating Administrations receiving ARRA funds will need to enhance their outreach efforts to ensure recipients of Federal grants and contracts—and their contractors—have meaningful ethics programs and sound internal controls to recognize, prevent, and report fraud.

### *Taking Timely and Effective Action To Suspend or Debar Individuals and Firms That Have Defrauded the Department*

DOT will need to ensure timely and effective action is taken on suspension and debarment cases against those individuals or firms that have defrauded the Department. Federal regulations prohibit firms and individuals without satisfactory records of integrity and business ethics from receiving Federal contracts. Our work has shown that the Operating Administrations do not consistently take suspension and debarment actions in a timely manner, even though the DOT Order requires that such decisions be made within 45 days.<sup>14</sup> Taking action to address these deficiencies is critical as DOT implements ARRA. We plan to issue the results of our ongoing audit in the near future as part of our effort to fast-track the release of information that is pertinent to the effective implementation of ARRA.

## **THE OFFICE OF INSPECTOR GENERAL WILL CONTINUE TO EXAMINE AREAS THAT PRESENT THE GREATEST RISKS AND PROMPTLY NOTIFY DOT AND CONGRESS OF ACTIONS NEEDED TO MINIMIZE FRAUD, WASTE, AND ABUSE AND ACHIEVE ARRA GOALS**

Our office supports DOT in its oversight initiatives, and we have developed a risk-based strategy in response to the new challenges presented by ARRA that will target the highest risk areas and emphasize timely reporting of results. To that end, we will evaluate DOT's management of the ARRA programs and its oversight of grantees and contractors receiving recovery funding. Our work is being coordinated with the

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<sup>14</sup> DOT Order 4200.5D, "Governmentwide Debarment, Suspension, and Ineligibility," June 7, 2005.

Government Accountability Office to avoid duplication of effort and maximize accountability coverage. In addition, we have a number of ongoing audits—undertaken before passage of ARRA—that directly relate to the DOT programs that received additional funding in ARRA. We have also begun several actions to enhance our capacity to assist DOT in ensuring accountability; these include hiring new staff to handle our increased audit and investigations workload.

### **The Office of Inspector General Is Using a Three-Phase Approach To Emphasize High-Risk Areas and Promptly Report Results**

In anticipation of ARRA's passage, we initiated Phase 1 of our planned audit and investigative strategy. This phase involved a comprehensive review of prior reports and testimonies to identify major challenges facing DOT as it implements ARRA. We analyzed this work and reported our results last month. As part of this effort, we identified a number of ongoing audits and investigative activities that directly relate to the challenges facing DOT under ARRA. For the most part, ARRA provided an infusion of new money to existing DOT programs, such as FHWA's Surface Transportation Program, the Federal Transit Administration's (FTA) Urbanized Area Formula Grant and New Starts programs, and FAA's Airport Improvement Program. We were already conducting work on issues related to many of these programs before the passage of ARRA. Any actions that DOT takes to improve these programs based on our findings and recommendations may increase the likelihood that ARRA dollars will be spent efficiently and effectively.

For example, our ongoing, follow-up audit of structurally deficient bridges indicates that while FHWA could account for the overall amount of Highway Bridge Program funding (in billions of dollars) apportioned to states for deficient bridges, its project-based accounting system lacks sufficiently detailed data. Therefore, the system could not evaluate whether the money was used to effectively improve the conditions of deficient bridges, as required by statute and FHWA policy. As a result, FHWA could not determine whether Highway Bridge Program funding improved the conditions of deficient bridges nationwide.

We will place priority on issuing ARRA-related reports as quickly as we can within compliance of generally accepted government auditing standards to provide timely information to DOT and Congress. To bolster this effort, we will also issue interim ARRA advisories to highlight key results of these audits that may warrant immediate attention by DOT agencies.

#### ***Phase 2: Conducting Agency Scans To Identify Vulnerabilities in ARRA Implementation***

Currently, we are in Phase 2 of our strategy, which involves conducting structured surveys, or scans, of each DOT agency's implementation of ARRA. Our objective in these agency scans is to evaluate vulnerabilities that could impede DOT's ability to

(1) provide effective oversight to ARRA-funded projects and (2) meet new requirements mandated by ARRA and OMB, including financial and job creation reporting.

We will conduct a scan at each DOT office or Operating Administration that received funding in ARRA: FHWA, FRA, FTA, OST, FAA, and the Maritime Administration (MARAD). Table 2 below shows the agencies that received ARRA funds and the amount allotted to each agency. In addition, once DOT provides us with its plan for addressing the key challenges it faces under ARRA—in response to our March 2009 recommendation—we will assess the actions taken or planned as part of our agency scans.

Each scan will be conducted using a standardized methodology, including questions that probe what actions DOT has taken or planned to address the 10 focus areas we reported. As with our ongoing, ARRA-related audits, we plan to expedite our reporting to ensure that DOT, Congress, and taxpayers have real-time information related to these scans. That is, if we identify any issues during the scans that warrant immediate attention, we will issue a series of ARRA advisories to highlight those issues. Earlier this week, we issued an announcement letter to formally initiate our Phase 2 work.

**Table 2. Distribution of ARRA Funds Within DOT**

<b>DOT Component</b>	<b>ARRA Funds (millions)</b>	<b>Percent of Total*</b>
FHWA	\$27,500	57.15%
FRA	\$9,300	19.33%
FTA	\$8,400	17.46%
OST	\$1,500	3.12%
FAA	\$1,300	2.70%
MARAD	\$100	0.21%
OIG	\$20	0.04%
<b>Total</b>	<b>\$48,120</b>	<b>100.00%</b>

Source: ARRA.

\*Percentages do not add up exactly due to rounding.

### *Phase 3: Examining High-Risk Areas*

Phase 3 of our strategy involves using the results of our agency scans to identify areas that warrant additional work and reporting based on potential risks. We will use this information to develop a long-term plan outlining our ARRA audit and investigative initiatives. In addition to our near-term phased approach, we remain committed to protecting the Federal investment over the long term.

### *Other Investigative Initiatives*

Our investigators have been proactive in their fraud deterrence efforts, recognizing that risks of fraud will increase as the recovery funds are poured into the economy in the coming months. To help mitigate these risks, we are:

- conducting fraud awareness and prevention activities to alert DOT staff and grantees, including contractors, at all levels of government so they know how to recognize, prevent, and report suspected fraud. They must also know that fraudulent misrepresentation for personal or corporate gain is unacceptable under any circumstance. As part of this effort, our special agents facilitated fraud, waste, and abuse workshops for oversight officials within DOT's Operating Administrations and state and local agencies receiving ARRA funds, and we will continue these efforts. In addition, the Secretary of Transportation and I hosted a webcast last month for DOT staff that focused on how to prevent fraud, waste, and abuse involving common fraud schemes.<sup>15</sup>
- distributing materials such as hotline posters and "red flag" fraud indicator cards to Federal, state, and local agencies to support their oversight efforts.

Our strategy also involves investigating allegations of fraud on DOT-funded projects. We will be vigilant in presenting cases to the Department of Justice (DOJ) for prosecution and participating in resulting prosecutions. We will also focus on ensuring that DOT's Operating Administrations and states take appropriate suspension and debarment actions. For example, we have already met with various DOJ personnel, including senior members of the National Procurement Fraud Task Force and the Antitrust Division in Washington, D.C. We also met with Federal Bureau of Investigation fraud and public corruption agents to discuss how we can best leverage scarce investigative resources. Further, we are reaching out to our investigative counterparts at the state and local levels.

### **The Office of Inspector General Is Taking Action To Best Position Itself To Meet the Increased Workload Under ARRA**

ARRA also presented our office with resource challenges. Even before ARRA's passage, we were already a small Inspector General office in relation to DOT's large budget. Accordingly, we intend to make the most of the \$20 million in additional funding that ARRA provided to our office. This additional funding will go a long way in ensuring that we have the staff, travel budget, information technology, and other resources that we need to help achieve new, ARRA-related goals.

I can assure you that we are maximizing the new funding and program flexibilities we received in recent months. For instance, we are working aggressively to hire new

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<sup>15</sup> This webcast can be viewed at: [www.oig.dot.gov/recovery/](http://www.oig.dot.gov/recovery/).

auditors and investigators. Our FY 2009 appropriation supports a base of approximately 414 full-time equivalents (FTE), and we employed 397 FTEs as of April 7, 2009. By this summer, we plan to have a new group of ARRA-focused auditors and investigators on board to supplement our existing staff. We plan to hire approximately 17 FTEs to reach our base and 37 new FTEs to perform recovery work.

We have issued numerous vacancy announcements at all levels and have begun selecting qualified applicants. Further, the Office of Personnel Management gave us authority to utilize “rehired annuitants” to supplement our staff. The ability to expeditiously hire high-caliber staff is critical so we can deploy them to track the influx of ARRA funds and deal with the increased workload of hotline complaints that are likely to occur as ARRA projects begin construction.

We are also conducting systematic outreach with congressional and other stakeholders, including staff of our authorization and appropriations committees in the House and Senate and major transportation associations. For example, earlier this month we met with various congressional staff directors and industry representatives to listen to their concerns about ARRA’s implementation.

Moreover, in response to the new challenges presented by ARRA, our office is updating its comprehensive strategic plan so that our ARRA audits and investigations are tied to an overarching strategy. This strategy will recognize the connection of ARRA to other key transportation issues and reflect the cross-cutting nature of DOT’s strategic goals, such as reducing congestion and improving safety. To expedite this planning effort and target resources more effectively going forward, we convened a daylong session earlier this month with our Senior Executive Service staff and audit Program Directors.

Finally, we are developing new reporting formats that will allow us to expeditiously issue the results of our work when we determine that action can be taken in a timely manner. We are also focused on presenting our ARRA work in a user-friendly, understandable manner to maximize the impact of our findings and recommendations.

## **CONCLUSION**

DOT will need sustained efforts to ensure that accountability, efficiency, and effectiveness are maintained in its portion of the recovery program. To that end, we acknowledge the TIGER team-led efforts that DOT has underway to successfully implement the ARRA program. We are focused on assisting DOT officials in their efforts by identifying vulnerabilities and making recommendations for program improvements. Further, we recognize the importance of collaboration across the accountability community, which is necessary to best protect taxpayer interests and promote achievement of ARRA’s goals.

It is important that we ensure accountability to help restore Americans' trust in Government and to maximize the return on the \$48 billion in transportation investments provided by the recovery program. ARRA presents a unique opportunity for DOT to make needed or neglected investments in the repair, rehabilitation, and modernization of the Nation's aging transportation infrastructure; to fund projects to reduce congestion; and to improve the overall safety of the transportation system. It is critical that we do everything possible to maximize this opportunity. We are committed to doing just that.

That concludes my statement, Madam Chairman. Once again, I would like to thank the Committee for its tremendous support of our oversight efforts related to ARRA. I will be happy to answer any questions you or other Members of the Committee may have.

**AMERICAN RECOVERY AND  
REINVESTMENT ACT OF 2009:  
OVERSIGHT CHALLENGES  
FACING THE DEPARTMENT OF  
TRANSPORTATION**

*Department of Transportation*

*Report Number: MH-2009-046*

*Date Issued: March 31, 2009*

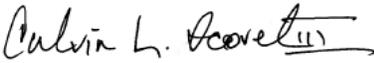


# Memorandum

U.S. Department of  
Transportation  
Office of the Secretary  
of Transportation  
Office of Inspector General

Subject: **ACTION:** American Recovery and Reinvestment Act of 2009: Oversight Challenges Facing the Department of Transportation  
Report Number MH-2009-046

Date: March 31, 2009

From: Calvin L. Scovel III   
Inspector General

Reply to  
Attn. of: J-1

To: All Secretarial Officers  
Heads of All Operating Administrations

On February 17, 2009, the President signed into law the American Recovery and Reinvestment Act (ARRA), which designated over \$48 billion to the Department of Transportation (DOT).<sup>1</sup> This audit report represents the second product in the Office of Inspector General's (OIG) review of DOT's implementation of ARRA.<sup>2</sup> The objective of this audit was to highlight key DOT oversight challenges—based on prior OIG reports and other agencies' relevant audit work—and identify actions DOT should take now in support of ARRA requirements.

According to the Secretary of Transportation, ARRA represents “the largest investment in America’s roads, bridges, transit lines, and rail systems since the creation of the interstate highway system.” Key provisions of ARRA are preserving and creating jobs, promoting economic recovery, and investing in transportation infrastructure that will provide long-term economic benefits. In addition to providing funding for a number of existing DOT programs, ARRA directs DOT to create several new programs and establishes tight time frames for distributing and expending funds and for reporting results (for example, the number of jobs created).

The vast majority of ARRA funding goes to the Federal Highway Administration (FHWA), the Federal Railroad Administration (FRA), and the Federal Transit Administration (FTA) for the construction and/or maintenance of highway, road,

<sup>1</sup> Public Law 111-5, February 17, 2009.

<sup>2</sup> OIG Testimony CC-2009-045, “Top Management Challenges Facing the Department of Transportation,” March 10, 2009. OIG reports and testimonies are available on our website: [www.oig.dot.gov](http://www.oig.dot.gov).

bridge, transit, and rail projects. The remaining ARRA funds are distributed among the Office of the Secretary of Transportation (OST), the Federal Aviation Administration (FAA), the Maritime Administration (MARAD), and OIG. Table 1 shows the distribution of ARRA funding within DOT.

**Table 1. Distribution of ARRA Funds Within DOT**

<b>DOT Component</b>	<b>Stimulus Funds (millions)</b>	<b>Percent of Total*</b>
FHWA	\$27,500	57.15%
FRA	\$9,300	19.33%
FTA	\$8,400	17.46%
OST	\$1,500	3.12%
FAA	\$1,300	2.70%
MARAD	\$100	0.21%
OIG	\$20	0.04%
<b>Total</b>	<b>\$48,120</b>	<b>100.00%</b>

Source: ARRA.

\* Percents do not add up due to rounding.

Both the President and Congress have emphasized the need for accountability, efficiency, and transparency in the allocation and expenditure of ARRA funds. Accordingly, the Office of Management and Budget (OMB) has called on Federal agencies to: (1) award and distribute funds in a prompt, fair, and reasonable manner; (2) ensure the recipients and uses of the funds are transparent to the public, and the resulting benefits are reported clearly, accurately, and promptly; (3) ensure funds are used for authorized purposes and to mitigate instances of fraud, waste, and abuse; (4) avoid unnecessary project delays and cost overruns; and (5) achieve specific program outcomes and improve results on economic indicators.<sup>3</sup>

To achieve these goals, DOT's leadership has been proactive on several fronts, including the establishment of the DOT-wide Transportation Investment Generating Economic Recovery (TIGER) team to coordinate the Department's role and ensure accountability. DOT's Operating Administrations are also working with senior Department officials in developing methods for tracking and reporting expenditures, job creation, and results; working with potential grantees to quickly identify and process proposals; and considering strategies for strengthening their existing oversight processes. OIG supports DOT in its oversight initiatives and has developed an audit strategy in response to the new challenges presented by ARRA.

Exhibit A presents our scope and methodology. We discussed our work and recommendations with DOT representatives, including the TIGER team, and appreciate their courtesies and cooperation during this audit. Exhibit B is a list of the relevant reports and testimonies issued by OIG. Exhibit C provides additional information on the specific DOT programs that received funding in ARRA and the statutory deadlines for spending the money.

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<sup>3</sup> OMB "Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009," February 18, 2009.

## RESULTS: OVERSIGHT CHALLENGES FACING DOT

Based on our analysis of ongoing and prior audit work and observations of DOT's efforts to implement ARRA, we see three major oversight challenges facing DOT:

1. Ensuring that DOT's grantees properly spend ARRA funds;
2. Implementing new accountability requirements and programs mandated by ARRA; and
3. Combating fraud, waste, and abuse.

The challenges and 10 focus areas associated with them are shown in table 2.

**Table 2. Major ARRA Challenges and Related Focus Areas for DOT**

Challenges	Focus Areas
<b>1. Ensuring that DOT's grantees properly spend ARRA funds</b>	<ul style="list-style-type: none"> <li>- Acquire sufficient personnel with relevant expertise to oversee grantees.</li> <li>- Adhere to existing Federal requirements for programs funded under ARRA.</li> <li>- Evaluate the credibility and completeness of cost and schedule estimates.</li> <li>- Oversee grantees' contracting management activities and ensure selection of appropriate contract types.</li> <li>- Address internal control weaknesses and identify unused funds for use elsewhere.</li> </ul>
<b>2. Implementing new accountability requirements and programs mandated by ARRA</b>	<ul style="list-style-type: none"> <li>- Implement new ARRA tracking and reporting requirements that are designed to promote accountability and transparency.</li> <li>- Develop comprehensive plans and sound criteria for the new discretionary grant and passenger rail programs within statutory deadlines.</li> <li>- Develop appropriate oversight strategies for the new discretionary grant and passenger rail programs.</li> </ul>
<b>3. Combating fraud, waste, and abuse</b>	<ul style="list-style-type: none"> <li>- Enhance understanding among DOT staff, grantees, and their contractors on how to recognize, prevent, and report potential fraud to the appropriate authorities.</li> <li>- Take timely and effective action to suspend and/or debar individuals or firms that have defrauded the Department so they do not receive Federal contracts in the future.</li> </ul>

## **ENSURING THAT DOT'S GRANTEES PROPERLY SPEND ARRA FUNDS**

The large amounts of funding that DOT is responsible for under ARRA and the accelerated time frames to use those funds will place great demands on DOT's workforce, oversight processes, business practices, and financial management systems. Accordingly, to meet these demands and provide effective oversight, DOT will need to:

- acquire sufficient personnel with relevant expertise to oversee grantees,
- adhere to existing Federal requirements for programs funded under ARRA,
- evaluate the credibility and completeness of cost and schedule estimates,
- oversee grantees' contracting management activities and ensure selection of appropriate contract types, and
- address internal control weaknesses and identify unused funds for use on other eligible projects.

### **Acquire Sufficient Staff With Relevant Expertise**

DOT must ensure that it has sufficient personnel with relevant expertise to meet the increased workload, new requirements, and accelerated time frames associated with recovery spending. A sufficient and trained workforce is key to holding grantees accountable for contract actions and realistic cost and schedule estimates, and ensuring that state or local recipients can effectively manage their projects and the risks associated with the recovery program.

DOT officials expressed concerns about their ability to provide sufficient oversight with limited time and staff, particularly in regional and division offices, and noted actions under consideration. Some Operating Administrations are considering detailing staff from each of their Headquarters to their regional and division offices and rehiring retired Federal employees (often referred to as "rehired annuitants") on a temporary basis. DOT officials informed us that, earlier this month, the Office of Personnel Management granted DOT direct-hire authority and delegated to it dual compensation waiver authority. These hiring flexibilities should help enable DOT meet critical hiring needs. The key will be to utilize these flexibilities effectively to augment other staffing actions.

These temporary efforts are laudable; but the difficult tasks will be to implement them promptly, evaluate their workability, and make any course corrections, as needed. Additional options may also merit consideration in addressing the

increased workload. One is to use private consultants to supplement—but not substitute for—DOT staff, such as FTA’s use of project management oversight contractors (PMOCs).<sup>4</sup> As we previously reported, the PMOC approach can provide early warnings of cost, schedule, and quality problems, but does not preclude them. Follow-through by DOT staff is critical to the success of this approach. For example, on FTA’s Lower Manhattan Recovery Projects (totaling \$4.55 billion), the PMOCs identified key risks early on that were not sufficiently addressed, such as the insufficient management and technical capabilities exhibited by some grantees.<sup>5</sup> These issues contributed to significant cost increases and schedule delays and an inability to stay within an overall Federal funding cap. In the past year, FTA has enhanced its oversight of these projects and is working with grantees to address issues the PMOCs identified.

However, a key requirement for evaluating staffing shortfalls for ARRA work and other DOT demands is good information on DOT’s workforce, including up-to-date plans. Our work has shown that more needs to be done in certain key areas. For example, DOT continues to face challenges in developing a comprehensive strategic plan for its entire acquisition workforce that oversees the direct award and administration of DOT contracts. DOT officials said they are having difficulty determining the total number of key acquisition workforce positions, such as contracting officer technical representatives and program managers. This is a result of the lack of critical information on these positions, including workforce size, knowledge and skills requirements, and attrition and retirement rates. Without such data, DOT is unable to identify employment trends and assess the current condition of the acquisition workforce, which are needed to determine the ideal composition, skill mix, and talent for its future.

In February 2009, DOT officials compiled a succession plan for the acquisition workforce. It includes a competency assessment for the entire acquisition workforce, some retirement information, hiring plans, and training strategies for contracting positions. As the Operating Administrations design strategies to address weaknesses identified in the plan, they will need to consider the impact of ARRA on the acquisition workforce. We plan to evaluate the adequacy of DOT’s workforce as part of our future audit work evaluating the effectiveness of the Department’s oversight of ARRA projects.

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<sup>4</sup> A project management oversight contractor is retained by FTA to evaluate a grantee’s technical capacity to build, operate, and maintain a project and to monitor the grantee’s implementation of a project. This is done in accordance with FTA guidance.

<sup>5</sup> OIG Report Number MH-2008-086, “Baseline Report on the Lower Manhattan Recovery Projects,” September 26, 2008.

## **Adhere to Existing Federal Requirements for Programs Funded Under ARRA**

DOT must avoid waiving or expediting existing requirements for the programs funded in ARRA and make sure that any required programmatic, financial, or engineering reviews are conducted in a rigorous and systematic manner. We have learned that when DOT's processes and procedures are short cut or bypassed, the potential for inefficient spending increases. Accordingly, DOT needs to carefully follow requirements in these areas by: (1) ensuring that planning requirements are met, including proper accounting for projects in a Statewide Transportation Improvement Program (STIP) and (2) following policies and procedures for the grant programs that received ARRA funding. These requirements exist to increase the likelihood that funds will be effectively planned and spent. As Secretary LaHood stated, DOT has committed to do things "by the book" by following established policies and procedures.

### *Follow Project Planning Requirements*

The Federal Government has a number of key planning requirements, including reviews related to environmental, financial, and project management issues, which must be met before projects can receive Federal funding. DOT will need to ensure that any ARRA projects meet them, even though the Department will be under great pressure to get shovels in the ground. Particular attention must be focused on reviews of required STIPs for highway and transit projects, as well as Airport Improvement Program (AIP) grant applications for aviation projects.

**Review of STIPs for highway and transit projects.** STIPs lay out how states intend to use taxpayers' money to meet their transportation needs, and they are to identify which projects will be funded and the cost and funding sources for those projects. DOT requires that STIPs be fiscally realistic and present truthful and credible information. Having a realistic STIP is critical for transportation and budget planning purposes.

DOT must make sure that FHWA and FTA ARRA-funded projects are included in a STIP; and that they review each state's STIP for fiscal constraint and compliance with statutory requirements, particularly in light of the deteriorating budget situation that state and local governments are experiencing. Further, states must also ensure that the STIPs they submit to DOT have all the required assurances and certifications at the state level. Going forward, we will be assessing states' compliance with the STIP process as part of our planned audit work.

**AIP grant planning.** FAA must ensure that all ARRA-funded aviation construction projects go through its AIP planning and programming processes. By doing so, FAA and its airport sponsors will be assured that only shovel-ready,

high-priority construction projects are approved for ARRA funding. FAA's processes include developing airport layout plans, assessing environmental impacts, completing preliminary designs, and determining project costs based on bids. Because these processes normally take several years to complete, FAA plans to fund only those projects that have already been through its grant review process and are ready to move to the construction phase. FAA must follow through on these plans and not circumvent any established AIP procedures as it evaluates AIP grant applications.

### *Follow Grant Policies and Procedures*

Once projects are approved, DOT's Operating Administrations must ensure adherence to existing oversight requirements related to the grant programs receiving ARRA funds, including FHWA's Surface Transportation Program, FTA's Urbanized Area Formula Program, and FAA's AIP. Failure to follow existing Federal requirements could result in inefficient expenditure of scarce tax payer dollars.

FAA's experience in awarding airport grants in the aftermath of Hurricanes Katrina and Rita is an example of what can happen when speed trumps sound business practices. FAA expedited the award of 10 airport grants totaling \$40.5 million under AIP, without completing steps in its grant award process. After bypassing controls to prevent duplicate payments and basing grant awards on bids rather than estimates, FAA issued grants for work that was later determined to be unneeded. Ultimately, FAA withdrew 7 of the 10 grants until oversight was improved and bids for hurricane-related projects were obtained.<sup>6</sup> Having learned important lessons through these hurricane relief efforts, FAA officials told us they intend to follow all AIP grant policies and procedures during implementation of ARRA. Additionally, FAA issued new ARRA grant guidance this month. In our discussions with FHWA and FTA, they also assured us they will not undermine any established policies and procedures in the rush to approve ARRA-funded projects.

### **Evaluate the Credibility and Completeness of Cost and Schedule Estimates**

DOT must target its oversight efforts at ensuring that cost and schedule estimates are examined and deemed credible and complete, particularly the risks posed by larger and more complicated projects. Cost estimates that are too high could lead to excess and idle funds, while estimates that are too low could force grantees to

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<sup>6</sup> OIG Report Number AV-2007-014, "Oversight of Airport Improvement Program Hurricane Grants," December 13, 2006.

find other sources of funding to cover overruns. Having realistic estimates and staying on-time and on-budget are even more critical now, considering the tight fiscal environment in which state and local governments are operating.

Our prior audit work points to the need for an early and more rigorous evaluation of cost and schedule estimates for ARRA projects. We have seen projects where earlier and more rigorous evaluation of estimates would have been beneficial. For example, in 2008, after assessing cost estimates for the Dulles Corridor Metrorail Project,<sup>7</sup> two independent consultants for FTA determined that the project sponsor underestimated the impact of schedule delays. These delays, in turn, increased the overall cost estimate for this project to almost \$3 billion—doubling an earlier estimate. Earlier scrutiny of the impact of schedule delays on cost estimates might have helped FTA avoid this situation and provide decisionmakers with more realistic information up front.

### **Oversee Grantees' Contracting Management Activities**

To manage its portion of the economic recovery program, DOT and its grantees must ensure that effective contracting and financial practices are in place to make sound decisions under the tight time frames and quick roll out of the program. Actions needed are: (1) specifying contract requirements early, maximizing competition, and using appropriate contract types and (2) preventing unallowable costs, improper payments, and excessive overhead charges during contract execution.

The magnitude and the accelerated pace for spending ARRA dollars could exacerbate contract award problems we previously identified, such as use of inappropriate contract types, inadequate competition, and failure to ensure contract prices are fair and reasonable. Audits of DOT and state contracts used to respond to the Hurricane Katrina emergency found instances in which DOT money was spent inefficiently because grantees used risky contracting methods in spending Federal funds, such as sole-sourced contracts, which resulted in significantly higher costs.<sup>8</sup> For example, we found a state Department of Transportation awarded two sole-sourced contracts without assurance of fair and reasonable prices, which resulted in the state paying about \$1.7 million more than necessary for bridge repairs.

DOT is taking steps to avoid a repeat of the problems it experienced in response to Hurricane Katrina. For example, it is stepping up its oversight of ARRA funding through outreach to grantees and posting frequently asked questions on the

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<sup>7</sup> OIG Report Number MH-2007-060, "Baseline Report on Major Project Monitoring of the Dulles Corridor Metrorail Project," July 27, 2007.

<sup>8</sup> OIG Report Number MH-2006-065, "Audit of the Mississippi Department of Transportation's Award of Selected Hurricane Katrina Emergency Repair Contracts," September 6, 2006.

websites of DOT's Operating Administrations; and it has implemented a "help desk" email site. Further, DOT's Office of the Senior Procurement Executive (OSPE) revised its Financial Assistance Guidance Manual in March 2009 to reflect the increased demands posed by ARRA. The manual sets a standardized process for grant processing and management. It will be important to widely disseminate this information down to the local grantee level, particularly to those grantees that have little or no experience in managing Federal dollars.

### **Address Internal Control Weaknesses and Identify Unused Funds for Use on Other Eligible Projects**

DOT needs to identify and mitigate any internal control<sup>9</sup> weaknesses to be assured that ARRA funding is spent in an efficient and effective manner, and in accordance with Federal laws and regulations. OMB is requiring agencies to immediately assess risk and develop mitigation strategies to prevent internal control weaknesses in areas such as ensuring the prompt award and expenditure of ARRA dollars and minimizing improper payments. Our prior audit work shows that DOT has experienced problems in some of these areas. To comply with OMB's requirements and provide effective oversight of ARRA funding, DOT must: ensure that its risk mitigation plans address internal control weaknesses and actions to prevent them from recurring; identify unused funds promptly and take timely action to free them up for use on other projects; and detect and prevent improper payments.

#### *Develop Risk Mitigation Plans That Address Internal Control Weaknesses*

DOT and its Operating Administrations need to work with their grantees to correct internal control weaknesses that auditors have identified during DOT's financial statement audits and Single Audit Act reviews.<sup>10</sup> It is critical that DOT use the OMB-required risk assessment process as a way to identify strategies to prevent similar issues with ARRA funds. Taking action to prevent internal control lapses is particularly important for FHWA, which received more than half of DOT's total funding allocation under ARRA. DOT's Single Audit Act reviews related to FHWA grantees identified internal control weaknesses and instances of noncompliance with grant requirements at state DOTs across the country. For example, in the past year and a half, auditors issued qualified opinions on eight state DOTs' administration of Federal-aid grants because of problems identified during the Single Audit Act reviews.

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<sup>9</sup> Internal controls provide reasonable assurance of the effectiveness and efficiency of an agency's use of financial resources, the reliability of financial reporting, and compliance with applicable laws and regulations.

<sup>10</sup> The Single Audit Act requires state or local grantees to maintain a system of internal control over all Federal programs in order to demonstrate compliance with pertinent laws and regulations. Single Audit Act reviews are conducted to determine whether grantees are complying with these requirements.

DOT has been identifying internal control risks and developing a consistent risk management tool to ensure the successful implementation of ARRA. For example, FHWA Headquarters recently issued a memorandum directing its 52 Division Offices to implement a risk management program to identify primary risks in successfully implementing ARRA. First, FHWA directed its Division Offices to assess risks, prioritize them, and report the assessments to Headquarters. Second, the memorandum directed Division Offices to develop a risk management plan that involves “visual monitoring” of items, such as state financial transactions and consultant procurement and administration, enhanced financial oversight of states, and communications and outreach to assist states in mitigating risks. These are good first steps, but FHWA needs to make sure these efforts are conducted consistently and effectively across its 52 Division Offices, which are located in every state, the District of Columbia, and Puerto Rico.

Providing consistent oversight across field locations has presented a challenge in the past, particularly at FHWA. Our prior audit work indicates that FHWA had not always ensured consistency in oversight activities among its Division Offices. For example, our 2009 report on FHWA’s oversight of the National Bridge Inspection Program showed that bridge engineers in the 10 states we reviewed did not perform Headquarters-recommended risk assessments of bridge conditions in a consistent or systematic manner.<sup>11</sup> This inhibited FHWA’s ability to assess bridge-related risks nationwide, prioritize them, and target those higher priority risks for remediation in coordination with states.

### *Identify Unused Funds Promptly*

To maximize the impact of ARRA funds on the economy, DOT must improve its controls for identifying unused funds in its financial management systems and taking appropriate action to release them on completed, canceled, and reduced-scope projects. Without sufficient controls, it is possible for unused funds to remain idle for long periods of time. This could prevent other worthy projects from receiving Federal funds and potentially undermine ARRA’s ability to stimulate the U.S. economy by spurring construction activity across the country.

In particular, DOT needs to ensure that it is addressing control weaknesses we have identified in the past regarding unused funds. For example, FHWA implemented the Financial Integrity Review and Evaluation (FIRE) in fiscal year (FY) 2005 to improve oversight of Federal highway funds, including its ability to identify idle funds that could be freed up for use elsewhere. FIRE has improved FHWA’s stewardship of Federal funds, but problems related to idle funds persist. This is evidenced by the fact that, in FY 2008, auditors again found idle funds at

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<sup>11</sup> OIG Report Number MH-2009-013, “National Bridge Inspection Program: Assessment of FHWA’s Implementation of Data-Driven, Risk-Based Oversight,” January 12, 2009.

FHWA estimated at about \$300 million. Similarly, we found that in 2007 FAA allowed numerous AIP grants to remain inactive and obligations to remain on closed grants, both for excessive periods of time.<sup>12</sup> These examples indicate that further management attention is needed to make sure that DOT's controls are effective at identifying unused funds that could be freed up for use on other eligible projects.

### *Detect and Prevent Improper Payments*

In its guidance on implementing ARRA, OMB emphasized the need for Federal agencies, including DOT, to prevent improper payments. Improper payments are those made to an ineligible recipient or for an ineligible service, duplicate payments, and payments for services not received. Avoiding improper payments presents a challenge to DOT.

For example, during our review of controls over DOT's contract for Hurricane Katrina emergency disaster relief transportation, we found that an FAA contracting officer routinely authorized invoices for payment without any documentation from the contractor showing that the services had actually been provided.<sup>13</sup> In one instance, this lack of controls resulted in a \$33 million overpayment to the contractor for emergency bus transportation services and chartered aircraft services, which was later recovered.

At FHWA, we have identified oversight weaknesses that led to improper payments, which must be avoided in the ARRA program. For example, in a recent audit of deficiencies in FHWA's oversight of design and engineering (D&E) firms' indirect costs claimed on Federal-aid grants, we reported that Federal funds were used to reimburse unallowable costs totaling nearly \$16 million.<sup>14</sup> This occurred in part due to ineffective oversight by FHWA, state departments of transportation, and the certified public accounting firms hired by the D&E firms.

## **IMPLEMENTING NEW ACCOUNTABILITY REQUIREMENTS AND PROGRAMS MANDATED BY ARRA**

In addition to increasing the funding levels of existing programs, ARRA placed additional challenges on DOT by (1) mandating several new reporting requirements that are designed to enhance accountability and transparency and

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<sup>12</sup> OIG Report Number AV-2007-073, "FAA's Oversight of Inactive Airport Improvement Program Grant Obligations," September 13, 2007.

<sup>13</sup> OIG Report Number AV-2006-032, "Report on Internal Controls Over the Emergency Disaster Relief Services Contract," January 20, 2006.

<sup>14</sup> OIG Report Number ZA-2009-033, "Oversight of Design and Engineering Firms' Indirect Costs Claimed on Federal-Aid Grants," February 5, 2009.

(2) creating two new large programs that provide for \$1.5 billion in supplementary discretionary grants to improve the Nation's transportation infrastructure and \$8 billion in grants for high-speed rail corridors and intercity passenger rail service.<sup>15</sup> To meet these new demands, DOT will need to:

- implement new ARRA tracking and reporting requirements that are designed to promote accountability and transparency,
- develop comprehensive plans and sound criteria for the new discretionary grant and passenger rail programs created by ARRA, and
- develop appropriate oversight strategies for the new programs created by ARRA by drawing lessons learned from DOT's Operating Administrations.

### **Implement New Tracking and Reporting Requirements Designed To Promote Accountability and Transparency**

To meet ARRA requirements, DOT must ensure that its financial management systems are able to track ARRA spending and produce reliable information to report on results in a meaningful way. These new requirements are spelled out in OMB's February 2009 implementation guidance. To carry out these requirements, DOT must ensure that its financial management systems are able to clearly and reliably track recovery funds separately from other program funds. Beginning in February 2009, OMB directed DOT and other agencies to distinguish ARRA funds from non-ARRA funds in all agency financial systems, business systems, and reporting systems. Further, OMB's guidance requires agencies to submit regular reports and the information to generate these reports will come largely from DOT's financial management systems. We met with officials in DOT's Operating Administrations to discuss these issues and they informed us they have been working to modify their financial management systems to meet the new ARRA-related requirements. The key will be following through with these plans and making any needed adjustments to DOT's financial management systems as ARRA is implemented.

DOT will need to stay focused on ensuring that its financial management systems are programmed to enable officials to meet ARRA requirements related to the tracking of funds. It will also need to report on the impact of the ARRA investment promptly (such as the number of jobs created) and provide meaningful information in these required reports. For example, beginning on May 8, 2009, current OMB guidance would require DOT to provide monthly financial reports citing obligations, expenditures, and other financial data by Treasury Account,

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<sup>15</sup> ARRA stipulates that the discretionary grant program can be used for a variety of projects, including highway, bridge, public transportation, passenger and freight rail, or port infrastructure projects.

vendor, and award number, and information on allocations of mandatory and entitlement programs by state or other appropriate geographical unit.

DOT also needs to aggressively enforce the new reporting requirements and ensure that grantees are reporting accurate and complete information. Further, DOT would face an even greater challenge if OMB decides to expand current contractor reporting requirements, which is under consideration.

Obtaining accurate information from DOT grantees has been an issue in the safety arena. For example, we previously reported on inaccuracies in FRA's national grade crossing inventory database<sup>16</sup> and significant weaknesses in the data reported by states and motor carriers to the Motor Carrier Safety Status Measurement System.<sup>17</sup> Some ARRA information will be available publicly on [www.recovery.gov](http://www.recovery.gov)<sup>18</sup> and, therefore, must meet DOT and OMB data quality requirements. This underscores the need to make sure DOT's financial systems are reporting reliable and complete information. Actions taken in the past to promote complete state reporting of data in the safety arena have included public disclosure of states with reporting problems by means of a data quality map, and individual state reviews to assess data quality issues.<sup>19</sup>

Our prior audit work highlights the need for DOT to focus attention on meeting the new tracking and reporting requirements. In the past, DOT has not always been able to use its financial management systems to ensure accountability for Federal dollars or report on results. For example, in the wake of the 2007 collapse of the I-35W bridge in Minnesota, we testified that FHWA must improve accountability by enhancing its ability to track states' use of Highway Bridge Program funding.<sup>20</sup> FHWA was unable to determine how much of this funding was actually spent on structurally deficient bridges, because its financial management system did not differentiate between spending on structurally deficient bridges and other bridge-related expenditures. This inhibited FHWA's ability to assess the impact of Federal dollars on bridge conditions.

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<sup>16</sup> OIG Report Number MH-2004-065, "Audit of the Highway Rail-Grade Crossing Safety Program," June 16, 2004.

<sup>17</sup> OIG Report Number MH-2004-034, "Improvements Needed in the Motor Carrier Safety Status Measurement System," February 13, 2004

<sup>18</sup> The Administration created a website, [www.recovery.gov](http://www.recovery.gov), to provide information to the public on the planning and implementation of ARRA.

<sup>19</sup> OIG Correspondence Control No. 2006-041, Correspondence to Representative Petri Regarding SafeStat Data Quality, May 7, 2007.

<sup>20</sup> OIG Testimony CC-2007-095, "Federal Highway Administration's Oversight of Structurally Deficient Bridges," September 5, 2007.

## **Develop Comprehensive Plans and Sound Criteria for OST's Discretionary Grant Program and FRA's Passenger Rail Program**

To design these new programs, DOT will need to accomplish a variety of tasks in a short time. First, it must develop a comprehensive plan for each program, including goals and objectives, to ensure that the capital improvements are integrated into a national system. Second, it must develop criteria and a transparent process for selecting projects within the time frames Congress specified. Third, it must issue clear guidance for program implementation.

DOT is planning for these programs, but meeting statutory deadlines will be difficult due to the number of tasks that must be completed in short time frames. Although DOT does not face the same deadlines for spending the money that ARRA mandated for existing programs, it is still required to quickly produce planning documentation and guidance. ARRA directs OST to publish criteria for its grant program within 90 days of ARRA enactment, accept applications for grants within 180 days after the criteria are published, and announce all projects selected within 1 year of ARRA enactment. Further, ARRA requires FRA to produce a strategic plan for the passenger rail program within 60 days of ARRA enactment and interim implementation guidance to applicants within 120 days.

### *OST's New Discretionary Grant Program*

To meet these deadlines, the Secretary established a working group within OST to develop criteria for the discretionary grant program and determine the best administrative structure. OST also has a task force providing advice, consisting of staff from the Operating Administrations. According to DOT officials, a central issue for the group is determining the most appropriate place to administer the grants—within OST or the Operating Administration that would normally be responsible for a particular type of project. For example, OST could delegate administrative responsibility for a bridge replacement project to FHWA. If the Secretary decides to delegate authority over projects to the Operating Administrations, the Department would need to decide how this delegation of authority would work within the established goals and requirements of ARRA.

### *FRA's New Passenger Rail Program*

DOT has not previously implemented the large-scale high-speed passenger rail program called for in the ARRA. It lacks recent experience overseeing the design and construction of a new high-speed rail system—in particular a new, stand-alone high-speed rail system. FRA has allocated staff to plan the high-speed rail and intercity rail service program, determine how to allocate the funds among the three

eligible purposes,<sup>21</sup> and develop program guidance within the statutory time frames. Because FRA is a small agency that had few grant programs before ARRA was passed, it is critical for FRA staff to leverage the in-house expertise throughout DOT and determine what additional resources it may need. According to FRA officials, they have consulted with other Operating Administrations for advice and are considering a variety of options to overcome staffing shortfalls and insufficient expertise, such as borrowing staff from FTA or FHWA and hiring consultants.

To design and implement this program, FRA will need to develop strategies to address several tough issues prior to implementation. Those key issues include:

- Ensuring that grantees obtain enforceable and meaningful capital investment agreements with private freight railroads so that users of intercity passenger rail receive benefits from these investments.
- Establishing sufficient controls to be assured that Federal investments do not simply supplant investments the freight railroads already planned to undertake on their rail lines.
- Integrating the capital improvements and associated service enhancements into a national intercity rail system that is tied to an overall strategic plan.
- Acquiring the financial and economic modeling expertise needed to evaluate a project's financing plans and revenue and ridership projections. This is important because most grantees will likely finance their projects through a mix of self-generated revenues (such as through the farebox), and Federal, state, and private investments. Equally important is conducting appropriate analysis of the viability of a high-speed rail project's long-term operating plan to ensure adequate resources are identified up-front that would allow these systems to continue operating over the long run.

### **Develop Appropriate Oversight Strategies for New Programs by Drawing Lessons From DOT's Operating Administrations**

Not all of the challenges facing FRA and OST are unique. Like the other DOT Operating Administrations receiving ARRA funds, they will need to eventually focus on deploying sufficient staff to implement these new programs and provide oversight to construction projects to ensure they are properly managed by grantees. However, the oversight challenges facing FRA and OST are exacerbated by the fact that they have limited experience managing large grant programs.

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<sup>21</sup> According to FRA, the \$8 billion can be used for three programs: (1) high-speed corridor program, (2) intercity passenger rail service grants, and (3) congestion grants.

Because both FRA and OST have some time before projects will be under construction, they need to use this period to evaluate the experiences of other Operating Administrations for lessons learned on what has worked well in the past. Then, they will need to decide what type and level of oversight to provide to projects. For example, FRA and OST could use a data-driven, risk-based approach to target their oversight efforts at projects that pose the highest risk due to certain factors, such as those projects with the largest dollar amounts committed or grantees with less experience in managing Federal grants. Along these lines, FHWA is implementing a data-driven, risk-based approach to overseeing the National Bridge Inspection Program, based on our recommendations.

Similarly, FRA and OST could learn from FTA's experience in standing up its Lower Manhattan Recovery Projects program. FTA created a separate Recovery Office to oversee the \$4.55 billion Federal investment.<sup>22</sup> This office included reassigned FTA staff and consultants to help provide oversight and advice on engineering, financial, environmental, security, and other issues. An approach like this could enable FRA and OST to quickly implement their new programs.

## **COMBATING FRAUD, WASTE, AND ABUSE**

DOT needs to tailor its counter-fraud efforts to adapt to the increase in capital funding associated with the recovery program and the expected surge in construction activity throughout the country. OMB's ARRA implementation guidance directs Federal agencies to be aggressive in preventing fraud, waste, and abuse. Accordingly, DOT will need to:

- enhance understanding among DOT staff, grantees, and their contractors on how to detect, prevent, and report potential fraud and
- take timely and effective action to suspend and/or debar individuals or firms that have defrauded DOT so they do not receive future Federal contracts.

### **Enhance Understanding Among DOT Staff, Grantees, and Their Contractors on How To Detect, Prevent, and Report Potential Fraud**

DOT must target its outreach efforts at deterring fraud schemes that have occurred on past DOT projects and could occur on projects that receive funding under the recovery program. They include false claims for materials and labor, bribes related to contracts for materials or labor, product substitution, and disadvantaged business enterprises fraud. Table 3 on the next page presents a list of common

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<sup>22</sup> OIG Testimony CC-2006-056, "Lower Manhattan Reconstruction Lessons Learned from Large Transportation Projects," July 13, 2006.

fraud schemes that must be prevented under ARRA. DOT will need to make sure that state and local grantees, and their contractors, understand how to detect, deter, and report these types of transportation-related fraud to the appropriate authorities.

An important way to deter fraud is for DOT staff and grantees to be aware of certain “red flag” indicators typically associated with fraud schemes. For example, any mismarking or mislabeling on products and materials might indicate product substitution fraud. The best way to make individuals aware of these indicators is to conduct systematic fraud prevention education in the field. A description of fraud indicators is presented in exhibit D.

**Table 3. Common Fraud Schemes Found on DOT-Funded Projects**

<b>Fraud Scheme</b>	<b>Description</b>
<b>Bid Rigging and Collusion</b>	Contractors misrepresent that they are competing against each other when they actually agree to cooperate on the winning bid to increase job profit.
<b>Materials Overcharging</b>	A contractor misrepresents how much construction material was used on a job and is paid for excess material to increase job profit.
<b>Time Overcharging</b>	A consultant misrepresents the distribution of employee labor to charge for more work hours, or a higher overhead rate to increase profit.
<b>Product Substitution</b>	A contractor misrepresents the product used in order to reduce costs for construction materials.
<b>Disadvantaged Business Enterprises Fraud</b>	A contractor misrepresents who performed the work in order to appear to be in compliance with contract goals for involvement of minority/women-owned businesses.
<b>Quality-Control Testing Fraud</b>	A contractor misrepresents the results of quality control tests to earn contract incentives falsely or to avoid production shutdown in order to increase profits or limit costs.
<b>Bribery</b>	A contractor compensates a government official in order to obtain contracts or permit overcharges.
<b>Kickbacks</b>	A contractor or subcontractor misrepresents the cost of performing work by secretly paying a fee for being awarded the contract and, therefore, inflating the cost to the government.
<b>Conflicts of Interest</b>	A contracting or oversight official has an undisclosed financial interest in a contractor or consultant, resulting in improper contract award or inflated costs.

Source: DOT OIG.

DOT has taken action to strengthen its fraud awareness and outreach efforts to more aggressively combat fraud, but continued vigilance and follow-through at all levels of the Department are needed to be assured that ARRA dollars are spent appropriately. DOT is taking action on fraud prevention in two key areas. First, DOT and the Operating Administrations receiving ARRA funds will need to increase outreach efforts to recipients of Federal grants and contracts to ensure they have meaningful ethics programs and sound internal controls to recognize, prevent, and report fraud. OIG has been working constructively with DOT officials to assist them in their counter-fraud outreach efforts. For example, earlier this month, the Secretary of Transportation and the Inspector General hosted a webcast to DOT staff that focused on how to prevent fraud, waste, and abuse involving common fraud schemes. Our special agents have also been and will continue providing fraud awareness briefings to DOT staff and grantees at the state and local levels throughout the Nation.

Second, DOT must continue to follow through to fully implement its ethics program. Last year, we reported that DOT needed to develop and maintain a robust ethics program to promote integrity across transportation programs. In response, in June 2008, the Department instituted an enhanced annual ethics training program for all acquisition and grants management personnel Department-wide. The implementation of ARRA underscores the need to follow through and fully implement this important annual training requirement.

### **Take Timely and Effective Action To Suspend and/or Debar Individuals or Firms That Have Defrauded DOT so They Do Not Receive Future Federal Contracts**

DOT will need to ensure timely and effective action is taken on suspension and debarment cases against those individuals or firms that have defrauded the Department. Federal regulations prohibit firms and individuals without satisfactory records of integrity and business ethics from receiving Federal contracts or assistance agreements. DOT revised its policy in June 2005, in part, to improve timely decisionmaking of suspension and debarment actions. However, our ongoing work shows that the Department needs to improve the policy—and its implementation—to provide for more timely processing and reporting of suspension and debarment actions.

Our work has shown that the Operating Administrations do not consistently take suspension and debarment actions in a timely manner, even though the DOT order requires such decisions be made within 45 days. Taking action to address these deficiencies is critical as DOT embarks on the implementation of ARRA. For example, over half of the 45 actions we reviewed (56 percent) were not processed within the required 45 days. For 19 of these actions, the Operating

Administrations took from 10 days to more than 2 ½ years longer than the 45-day standard to render final decisions. The remaining six debarment actions we reviewed are still awaiting a decision from the debarring officials, which currently takes between 165 and 945 days.

Further, in February 2009, the Government Accountability Office (GAO) testified that it had confirmed allegations that businesses and individuals suspended or debarred for egregious offenses were continuing to receive Federal contracts.<sup>23</sup> Our work did not find any DOT contracts or assistance agreements awarded to suspended or debarred firms or individuals. However, deficiencies in DOT's suspension and debarment policy and implementation leave DOT, as well as other Federal agencies, vulnerable to doing business with fraudulent or unethical firms or individuals. This risk will increase significantly under the recovery program.

## CONCLUSIONS AND RECOMMENDATIONS

The significant increase in funding for transportation projects associated with ARRA adds new challenges on top of the longstanding ones we have highlighted in past reports to the Secretary of Transportation and Congress. At the same time, ARRA presents an opportunity for DOT to make needed or neglected investments in the repair, rehabilitation, and modernization of our aging transportation infrastructure; to fund projects to reduce congestion; and to improve the safety of our Nation's transportation system.

We recognize the TIGER team-led efforts that the Department has underway to successfully implement the ARRA program. To assist in these efforts, our report condensed the challenges into 10 areas where DOT must exhibit sustained and effective actions and oversight. To that end, our future audit work will use a risk-based strategy, carried out in coordination with the Government Accountability Office, to evaluate DOT's management of the ARRA programs and its oversight over grantees and contractors receiving recovery funding.

To ensure sufficient consideration of the potential risks discussed in this report, we recommend that the Secretary of Transportation, through the DOT TIGER team, develop an oversight implementation plan that outlines the key actions DOT already has underway or will take to:

- Acquire sufficient personnel with relevant expertise to oversee grantees;

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<sup>23</sup> GAO Testimony GAO-09-419T, "Excluded Parties List System: Suspended and Debarred Businesses and Individuals Improperly Receive Federal Funds," February 26, 2009.

- Adhere to existing Federal requirements for programs funded under ARRA;
- Evaluate the credibility and completeness of cost and schedule estimates;
- Oversee grantees' contracting management activities and ensure selection of appropriate contract types;
- Address internal control weaknesses and identify unused funds for use on other eligible projects;
- Implement new ARRA tracking and reporting requirements that are designed to promote accountability and transparency;
- Develop comprehensive plans and sound criteria for the new discretionary grant and passenger rail programs created by ARRA;
- Develop appropriate oversight strategies for the new programs created by ARRA by drawing lessons from DOT's Operating Administrations;
- Enhance understanding among DOT staff, grantees, and their contractors on how to recognize, prevent, and report potential fraud; and
- Take timely and effective action to suspend and/or debar individuals or firms that have defrauded the Department so they do not receive Federal contracts in the future.

In addition, the plan should prioritize the greatest risks for DOT and address open OIG recommendations from prior audit reports that have relevance to the implementation of ARRA.

## **AGENCY COMMENTS AND OFFICE OF INSPECTOR GENERAL RESPONSE**

We provided a draft of this report to DOT for review and comment on March 18, 2009. DOT provided us its formal comments on March 26, 2009, which we incorporated into this report, as appropriate. DOT's complete comments are included as the appendix to this report. DOT also provided informal technical clarifications, which we incorporated into this report, as appropriate. In its formal comments, DOT agreed that vigilant oversight of ARRA funding is critical to the successful implementation of ARRA and described some of the efforts it has underway, including the work of the DOT TIGER team. We have included highlights of DOT's key efforts in our report and recognize the ongoing

commitment and actions of the Department's leadership to ensuring the efficient and effective use of ARRA funds. DOT also concurred with our recommendation and agreed to provide us with a document outlining actions taken and planned to address our 10 focus areas.

## **ACTIONS REQUIRED**

We consider DOT's planned actions to be reasonable. However, in accordance with Department of Transportation Order 8000.1C, we request that DOT provide us with the plan called for in our recommendation within 30 days of the date of this report.

If you have any questions, please call me at (202) 366-1959, or Ann Calvaresi-Barr, Principal Assistant Inspector General for Auditing and Evaluation at (202) 366-1427.

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cc: Members of the DOT TIGER team

## EXHIBIT A. SCOPE AND METHODOLOGY

The objective of this audit was to highlight key ARRA oversight challenges—based on prior OIG reports and other agencies’ relevant audit work—and identify actions DOT should take now in support of ARRA requirements. To address our audit objective, we conducted a comprehensive review of our prior work on relevant surface transportation and aviation oversight issues, including: work on major highway and transit projects, Hurricanes Katrina and Rita recovery projects, and AIP grant oversight projects. We also reviewed the relevant work of other organizations that have reported on transportation-related oversight issues, including GAO.

Specifically, we:

- reviewed the existing body of OIG, GAO, and others’ work (for example, Single Audits) to identify past challenges that are likely to apply to projects funded under ARRA.
- held discussions with OST, FHWA, FRA, FTA, FAA, and MARAD officials; DOT’s TIGER Team; and representatives of surface transportation groups and an aviation constituency group to identify what they believe are the oversight challenges to the economic stimulus projects and obtain information on DOT’s preliminary efforts to prepare for the implementation of ARRA.
- identified and analyzed internal DOT Operating Administration reports to identify challenges previously known within DOT.
- coordinated with OIG’s investigative offices to identify other work that was relevant to oversight challenges facing DOT.

We conducted this performance audit from January through March 2009 in accordance with Generally Accepted Government Auditing Standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## **EXHIBIT B. RELEVANT OIG REPORTS AND TESTIMONIES**

OIG Testimony Number CC-2009-045, “Top Management Challenges Facing the Department of Transportation,” March 10, 2009.

OIG Report Number ZA-2009-033, “Oversight of Design and Engineering Firms’ Indirect Costs Claimed on Federal-Aid Grants,” February 5, 2009.

OIG Report Number MH-2009-013, “National Bridge Inspection Program: Assessment of FHWA’s Implementation of Data–Driven, Risk–Based Oversight,” January 12, 2009.

OIG Report Number AV-2009-012, “FAA’s Management and Maintenance of Air Traffic Control Facilities,” December 15, 2008.

OIG Report Number PT-2009-005, “FY 2009 Top Management Challenges,” November 17, 2008.

OIG Report Number MH-2008-086, “Baseline Report on the Lower Manhattan Recovery Projects,” September 26, 2008.

OIG Report Number AV-2008-002, “Prioritization of Airport Improvement Program Funding,” October 26, 2007.

OIG Report Number CR-2007-079, “Growth in Highway Construction and Maintenance Costs,” September 26, 2007.

OIG Report Number AV-2007-073, “FAA’s Oversight of Inactive Airport Improvement Program Grant Obligations,” September 13, 2007.

OIG Report Number AV-2007-066, “Review of Congressional Earmarks Within Department of Transportation Programs,” September 7, 2007.

OIG Testimony Number CC-2007-095, “Federal Highway Administration’s Oversight of Structurally Deficient Bridges,” September 5, 2007.

OIG Report Number MH-2007-060, “Baseline Report on Major Project Monitoring of the Dulles Corridor Metrorail Project,” July 27, 2007.

OIG Report Number AV-2007-014, “Oversight of Airport Improvement Program Hurricane Grants,” December 13, 2006.

OIG Report Number MH-2006-065, “Audit of the Mississippi Department of Transportation’s Award of Selected Hurricane Katrina Emergency Repair Contracts,” September 6, 2006.

OIG Testimony Number CC-2006-056, Before the Committee on Homeland Security Subcommittee on Management, Integration, and Oversight, U. S. House of Representatives, “Lower Manhattan Reconstruction: Lessons Learned from Large Transportation Projects,” July 13, 2006.

OIG Report Number AV-2006-051, “Internal Controls over Payments for Emergency Disaster Relief Transportation Services,” June 30, 2006.

OIG Report Number AV-2006-032, “Internal Controls over the Emergency Disaster Relief Transportation Services Contract,” January 20, 2006.

OIG Report Number FI-2006-011, “Inactive Obligations,” November 14, 2005.

OIG Report Number AV-2005-062, “Safety Oversight of an Air Carrier Industry in Transition,” June 3, 2005.

OIG Report Number MH-2005-046, “FHWA Needs to Capture Basic Aggregate Cost and Schedule Data to Improve Its Oversight of Federal-Aid Funds,” February 15, 2005.

OIG Report Number FI-2005-044, “FAA Inactive Obligations,” January 31, 2005.

OIG Report Number MH-2005-012, “Managing Risk in the Federal-Aid Highway Program,” November 19, 2004.

OIG Report Number MH-2004-098, “Audit of the Tren Urbano Rail Transit Project,” September 29, 2004.

OIG Report Number AV-2004-094, “FAA's Administration and Oversight of Regionally Issued Contracts,” September 28, 2004.

OIG Report Number IN-2003-003, “Audit of the Springfield Interchange Project,” November 22, 2002.

OIG Report Number FI-2002-092, “Oversight of Cost-Reimbursable Contracts,” May 8, 2002.

## EXHIBIT C. ARRA ALLOCATION AND EXPENDITURE DEADLINES AND REDISTRIBUTION REQUIREMENTS

Funding Type	Amount	Available Through	Deadlines
FAA Infrastructure	\$200 million	9/30/2010	NA
FAA Airport Improvement Program	\$1.1 billion	9/30/2010	<ul style="list-style-type: none"> <li>• 50% of total to be awarded within 120 days of enactment</li> <li>• 100% of total within 1 year of enactment</li> </ul>
FHWA Infrastructure	\$27.5 billion	9/30/2010	<ul style="list-style-type: none"> <li>• 50% of total to be obligated within 120 days from the apportionment or forfeit the unobligated portion of that 50% to redistribution process</li> <li>• 100% of remainder within 1 year from the apportionment or forfeit 100% of unobligated funds to redistribution process</li> </ul>
FRA Rail	\$8 billion	9/30/2012	NA
FRA Amtrak	\$1.3 billion	9/30/2010	NA
FTA Transit Capital Assistance	\$6.9 billion	9/30/2010	<ul style="list-style-type: none"> <li>• 50% of total to be obligated within 180 days from the apportionment or forfeit the unobligated portion of that 50% to redistribution process</li> <li>• 100% of remainder within 1 year from the apportionment or forfeit 100% of unobligated funds to redistribution process</li> </ul>
FTA Transit Capital Investment Grants	\$750 million	9/30/2010	Priority for projects currently in construction or projects that can obligate funds within 150 days of enactment of Act
FTA Fixed Guideway Infrastructure Investment	\$750 million	9/30/2010	<ul style="list-style-type: none"> <li>• 50% of total to be obligated within 180 days from the apportionment or forfeit the unobligated portion of that 50% to redistribution process</li> <li>• 100% of remainder within 1 year from the apportionment or forfeit 100% of unobligated funds to redistribution process</li> </ul>
MARAD	\$100 million	9/30/2010	100% of total to be obligated within 180 days of the date of distribution
OST Discretionary	\$1.5 billion	9/30/2011	NA
OIG	\$20 million	9/30/2013	NA

### Exhibit C. ARRA Allocation and Expenditure Deadlines and Redistribution Requirements

## **EXHIBIT D. “RED FLAG” INDICATORS FOR COMMON FRAUD SCHEMES AND HOW TO REPORT SUSPECTED FRAUD**

The following are brief descriptions of selected fraud schemes commonly seen on transportation projects, along with sample “Red Flag” indicators for each scheme. It is important to note that the presence of one or more indicators does not prove fraud, nor are the indicators shown all inclusive for each of the schemes described.

### **Bid Rigging and Collusion**

In bid rigging and collusion schemes, contractors misrepresent the competition against each other when, in fact, they agree to cooperate on the winning bid to increase job profit. Watch for:

- Unusual bid patterns: too close, too high, rounded numbers, or identical winning margins or percentages.
- Different contractors making identical errors in contract bids.
- Bid prices dropping when a new bidder enters the competition.
- Rotation of winning bidders by job, type of work, or geographic area.
- Losing bidders hired as subcontractors.
- Apparent connections between bidders: common addresses, personnel, or phone numbers.
- Losing bidders submitting identical line item bid amounts on nonstandard items.

### **Materials Overcharging**

In materials overcharging schemes, a contractor misrepresents how much construction material was used on the job and is then paid for excess material to increase job profit. Watch for:

- Discrepancies between contractor-provided quantity documentation and observed data, including yield calculations.
- Refusal or inability to provide supporting documentation.
- Contractor consistently loading job materials into equipment away from inspector oversight.
- Truck weight tickets or plant production records with altered or missing information.
- Photocopies of quantity documentation where originals are expected.

- Irregularities in color or content of weight slips or other contractor documents used to calculate pay quantities.

### **Time Overcharging**

In a time overcharging scheme, a consultant misrepresents the distribution of employee labor on jobs in order to charge for more work hours or a higher overhead rate, to increase profit. Watch for:

- Unauthorized alterations to time cards and other source records.
- Billed hours and dollars consistently at or near budgeted amounts.
- Time cards filled out by supervisors, not by employees.
- Photocopies of timecards where originals are expected.
- Inconsistencies between a consultant's labor distribution records and employee timecards.

### **Product Substitution**

In product substitution schemes, a contractor misrepresents the product used in order to reduce costs for construction materials. Watch for:

- Any mismarking or mislabeling of products and materials.
- Contractor restricting or avoiding inspection of goods or service upon delivery.
- Contractor refusing to provide supporting documentation regarding production or manufacturing.
- Photocopies of necessary certification, delivery, and production records where originals are expected.
- Irregularities in signatures, dates, or quantities on delivery documents.
- High rate of rejections, returns, or failures.
- Test records reflect no failures or a high failure rate but contract is on time and profitable.
- Unsigned certifications.

### **Disadvantaged Business Enterprises (DBE) Fraud**

In disadvantaged business enterprises schemes, a contractor misrepresents who performed contract work in order to appear to be in compliance with contract goals for involvement of minority or women-owned businesses. Watch for:

- Minority owner lacking background, expertise, or equipment to perform subcontract work.

- Employees shuttling back and forth between prime contractor and minority-owned business payrolls.
- Business names on equipment and vehicles covered with paint or magnetic signs.
- Orders and payment for necessary supplies made by individuals not employed by minority-owned business.
- Prime contractor facilitated purchase of minority-owned business.
- Minority-owned business owner never present at job site.
- Prime contractor always uses the same minority-owned business.

### **Quality-Control Testing Fraud**

In quality-control testing schemes, a contractor misrepresents the results of quality control (QC) tests to falsely earn contract incentives or to avoid production shutdown in order to increase profits or limit costs. Watch for:

- Contractor employees regularly taking or labeling QC samples away from inspector oversight.
- Contractor insisting on transporting QC samples from the construction site to the lab.
- Contractor not maintaining QC samples for later quality assurance (QA) testing.
- Contractor challenging results, or attempting to intimidate QA inspectors who obtain conflicting results.
- Photocopies of QC test results where originals are expected.
- Alterations or missing signatures on QC test results.

### **Bribery**

In bribery schemes, a contractor compensates a government official to obtain a contract or permit contract overcharges. Watch for:

- Other government inspectors at the job site noticing a pattern of preferential contractor treatment.
- Government official having a lifestyle exceeding his/her salary.
- Contract change orders lacking sufficient justification.
- Oversight officials socializing with or having business relationships with contractors or their families.

### **Kickbacks**

In kickback schemes, a contractor or subcontractor misrepresents the cost of performing work by secretly paying a fee for being awarded the contract and therefore inflating job costs to the government. Watch for:

- Unexplained or unreasonable limitations on the number of potential subcontractors contracted for bid or offer.
- Continuing awards to subcontractors with poor performance records.
- Non-award of subcontract to lowest bidder.
- “No-value-added” technical specifications that dictate contract awards to particular companies.

### **Conflicts of Interest**

In conflict of interest schemes, a contracting or oversight official has an undisclosed financial interest in a contractor or consultant, resulting in improper contract award or inflated costs. Watch for:

- Unexplained or unusual favoritism shown to a particular contractor or consultant.
- Government official disclosing confidential bid information to a contractor or assisting the contractor in preparing the bid.
- Employee having discussions about employment with a current or prospective contractor or consultant.
- Close socialization with and acceptance of inappropriate gifts, travel, or entertainment from a contractor.
- Vendor or consultant address is incomplete or matching employee’s address.
- Government official leasing or renting equipment to a contractor for performing contract work.

### **Reporting Concerns About Fraud, Waste, or Abuse**

OIG maintains a Hotline to report allegations of fraud, waste, and abuse in DOT programs or operations. Allegations may be reported by DOT employees, contractors, or the public. The OIG Hotline is available 24 hours a day, 7 days a week. Individuals who contact the Hotline, via telephone or letter, are not required to identify themselves. However, persons who report allegations are encouraged to identify themselves in the event additional questions arise as the OIG evaluates or pursues their allegations.

### **Exhibit D. “Red Flag” Indicators for Common Fraud Schemes and How To Report Suspected Fraud**

Report suspicions and allegations of fraud, waste, and abuse to OIG by using one of the following methods:

- Online complaint form: [www.oig.dot.gov/hotlineform.jsp](http://www.oig.dot.gov/hotlineform.jsp)
- Telephone: (800) 424-9071
- Fax: (540) 373-2090
- E-mail: [hotline@oig.dot.gov](mailto:hotline@oig.dot.gov)
- Mail: DOT Inspector General  
P.O. Box 708  
Fredericksburg, VA 22404-0708

## APPENDIX. MANAGEMENT COMMENTS



**U.S. Department of  
Transportation**

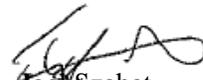
Office of the Secretary  
Of Transportation

1200 New Jersey Ave., S.E.  
Washington, DC 20590

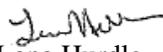
March 26, 2009

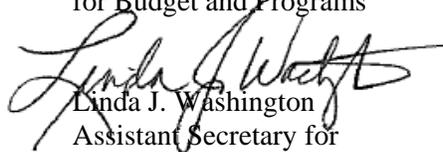
MEMORANDUM TO:

Calvin L. Scovel, III  
Inspector General

  
Joel Szabat  
Deputy Assistant Secretary  
for Transportation Policy

FROM:

  
Lana Hurdle  
Acting Assistant Secretary  
for Budget and Programs

  
Linda J. Washington  
Assistant Secretary for  
Administration

SUBJECT:

Departmental Comments on Office of Inspector General (OIG)  
Draft Report, "American Recovery and Reinvestment Act of  
2009: Oversight Challenges Facing the Department of  
Transportation"

The Department of Transportation is committed to performing an outstanding job implementing the President's initiative to enhance economic growth through the American Recovery and Reinvestment Act (ARRA). This commitment to excellence started well in advance of the Act being signed into law. In January, the Department assembled a leadership team to provide oversight and serve as a conduit for coordinated and consistent intermodal implementation of the Act. Under the auspices of this overall Transportation Investment Generating Economic Recovery (TIGER) Team, the leadership created a dynamic forum for exchanging information and provided guidance for consistent action throughout the Department. The benefits of the Department's fast response in anticipation of ARRA are already becoming apparent. For example, these efforts positioned DOT to rapidly obtain direct hire and rehired annuitant authority from OPM. Further, a DOT risk management tool was developed early to strengthen internal DOT controls and the tool was subsequently adopted verbatim by OMB for government-wide application. In addition, the TIGER Team is using leading edge, web-based interactive technology to enable expedited information

sharing and data tracking. For example, it developed a web-based interactive master planning document that tracks progress and assigns responsibility for each of the Department's major actions. We also created a web-based capability for tracking action and responsibility on recommendations made by the OIG and the Government Accountability Office (GAO) pertaining to ARRA implementation.

In addition to the overall perspective provided by the TIGER Team, it also created the capabilities to provide detailed guidance and leadership in key areas affecting ARRA implementation. Individual stewardship groups were established to gather expertise from across the Department to address common issues and identify coordinated and appropriate actions. These groups provide leadership in the areas of financial stewardship, data collection, procurement, and grant management, job measurement, information technology and communication. Finally, an Accountability Stewardship group has been established with the participation of TIGER leadership, the OIG and GAO. The purpose of this group is to achieve the type of transparency envisioned by ARRA, and provide an efficient forum for sharing information between management and the audit entities.

We appreciate the information provided in the OIG's draft report and will provide detailed information to the OIG on actions taken and planned in each of the ten emphasis areas identified in the report. We intend to provide this information within 30 days of the final report's issuance. Finally, please note that we shared with your staff, a separate listing of technical and specific comments from throughout DOT to correct errors in your report and for your consideration in finalizing the report. Please contact Martin Gertel at (202) 366-5145 with any questions or if you require further information.