

Audit Report

**Department of Transportation
Maryland Aviation Administration**

October 2016



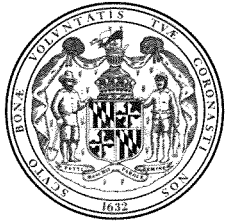
OFFICE OF LEGISLATIVE AUDITS
DEPARTMENT OF LEGISLATIVE SERVICES
MARYLAND GENERAL ASSEMBLY

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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Warren G. Deschenaux
Executive Director

Thomas J. Barnickel III, CPA
Legislative Auditor

October 7, 2016

Senator Guy J. Guzzone, Co-Chair, Joint Audit Committee
Delegate C. William Frick, Co-Chair, Joint Audit Committee
Members of Joint Audit Committee
Annapolis, Maryland

Ladies and Gentlemen:

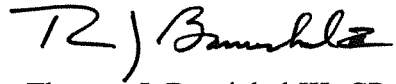
We have conducted a fiscal compliance audit of the Maryland Department of Transportation – Maryland Aviation Administration (MAA) for the period beginning August 1, 2011 and ending June 30, 2015. MAA is responsible for the operation, maintenance, protection, and development of the Baltimore/Washington International (BWI) Thurgood Marshall Airport and the Martin State Airport, and operates a program to foster, develop, and regulate aviation within the State.

Our audit disclosed that MAA had not fulfilled certain Federal Aviation Administration requirements relating to its noise compatibility program and, as a result, \$4.6 million in expenditures were not reimbursed with federal funds set aside for this purpose. As of September 30, 2015, MAA had \$12.4 million in an escrow account established for the noise compatibility program; however, no program costs had been reimbursed from this account. Instead, MAA advised that these costs were recovered through airline landing fees.

MAA also did not always competitively procure vehicle and equipment maintenance services or use an available Statewide contract. Finally, our audit noted control and record keeping deficiencies relating to cash receipts and purchasing transactions.

The Maryland Department of Transportation's response to this audit, on behalf of MAA, is included as an appendix to the report. We wish to acknowledge the cooperation extended to us during the course of this audit by MAA.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "TJ Barnickel III". The signature is fluid and cursive, with the first letters of the first and last names being capitalized and prominent.

Thomas J. Barnickel III, CPA
Legislative Auditor

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* **Denotes item repeated in full or part from preceding audit report**

Background Information

Agency Responsibilities

The Maryland Aviation Administration (MAA) is responsible for the operation, maintenance, protection, and development of the Baltimore/Washington International (BWI) Thurgood Marshall Airport and the Martin State Airport, and operates a program to foster, develop, and regulate aviation within the State.

According to the State's records, MAA's expenditures totaled approximately \$311 million (special funds of \$279 million and federal funds of \$32 million) during fiscal year 2015. Special fund revenue generated by airport operations totaled approximately \$224 million; the amount by which special fund expenditures exceeded special fund revenue was funded by the State's Transportation Trust Fund (TTF). According to MAA's records, during fiscal year 2015, approximately \$78 million of other revenue (passenger facility charges, customer facility charges, and a portion of parking revenue) was also generated and used for debt service and capital project expenditures. As needed, funding for capital projects is also provided by the TTF.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of eight findings contained in our preceding audit report dated November 16, 2012. We determined that MAA satisfactorily addressed seven of these findings and one is repeated in this report.

Findings and Recommendations

Federal Funds

Finding 1

The Maryland Aviation Administration (MAA) did not comply with requirements of a federal noise compatibility program and, as a result, \$4.6 million in related expenditures were not reimbursed with federal funds.

Analysis

MAA did not comply with requirements of a federal noise compatibility program and, as a result, \$4.6 million in related expenditures were not reimbursed with federal funds set aside for this purpose. As of September 30, 2015, MAA had \$12.4 million in an escrow account established for the noise compatibility program; however, no program costs had been reimbursed from this account. Instead, MAA advised that these costs were recovered through airline landing fees.

The noise compatibility program provides funding for residential sound insulation projects and for the acquisition of properties in areas exposed to significant aircraft noise. Federal funding is available to reimburse 80 percent of eligible expenditures, while 20 percent is required in State matching funds. MAA advised that it suspended the noise compatibility program in 2012 because of difficulty in complying with Federal Aviation Administration (FAA) reimbursement requirements.

In response to our inquiries during the audit, MAA determined that it had spent \$5.7 million for sound insulation projects during the period between 2003 and 2012, but it had not obtained reimbursement for the federal portion of these expenditures, totaling \$4.6 million. MAA also determined that \$2.7 million of the \$4.6 million would not qualify for reimbursement because the expenditures related to projects that were completed outside of the allowed airport perimeter or because MAA could not locate documentation that identified the associated properties. While MAA subsequently requested reimbursement for the remaining \$1.9 million, the FAA denied the request in October 2015 because the project expenditures identified were not eligible; specifically, MAA did not comply with certain program requirements such as pre-construction and post-construction noise level testing of residential properties.

MAA contends that all noise compatibility program costs have been included in its calculation of the landing fees charged to the airlines and, therefore, have been recovered. However, rather than requiring the airlines to absorb these costs,

MAA should be more diligent in complying with program requirements which would allow it to use the federal funding available in the escrow account.

This escrow account was established when the FAA changed the noise compatibility program in 2008 and required MAA to develop a plan to dispose of excess land that was originally purchased with federal funds as part of the program and deposit the federal proceeds into an escrow account. These proceeds, which were primarily received since 2012, represent the only funding source available for reimbursement of subsequent noise compatibility program expenditures, subject to FAA's authorization. However, as of September 30, 2015 no funds had been requested for reimbursement from the account. As allowed by federal regulations, MAA advised us it plans to use these escrow funds on eligible airport improvement projects as well as the noise compatibility program.

Recommendation 1

We recommend that MAA establish and implement formal procedures to ensure compliance with applicable program requirements and request reimbursement for all eligible expenditures from the federal funds available for this purpose.

Cash Receipts

Finding 2

MAA did not have adequate procedures to ensure that all collections, which totaled \$141 million during fiscal year 2015, were deposited and that deposits were made timely.

Analysis

MAA did not have an adequate procedure to ensure all collections were deposited and that deposits were made timely. According to agency records, collections processed during fiscal year 2015, which included receipts from airport tenants and airlines, totaled approximately \$141 million.

Specifically, MAA personnel did not use the initial record of receipts to perform the deposit verifications. Rather the deposited collections were only compared to the amounts recorded in the State's accounting records. As a result, there is a lack of assurance that all collections were deposited. The Comptroller of Maryland's *Accounting Procedures Manual* requires a reconciliation of collections recorded upon receipt to the bank deposit.

In addition, our test of 10 daily deposits totaling approximately \$44 million disclosed that all collections were deposited either two or three days after receipt. We were advised by MAA that this delay occurred because the armored courier service MAA used to transport its deposits to the bank could not make same day deposits. Alternatively, the controls over collections, including the security over the checks and the timeliness of deposit, could be enhanced if MAA requested its tenants, especially airlines, to remit funds electronically. The Comptroller of Maryland's *Accounting Procedures Manual* requires that collections be deposited no later than one business day after the date of receipt.

Recommendation 2

We recommend that MAA

- a. ensure deposit verifications are performed using all initial receipt records, and**
- b. pursue other arrangements to enhance the accountability and timeliness of deposits such as requesting that collections be remitted electronically.**

Purchases and Disbursements

Finding 3

Proper internal controls were not established to ensure independent approvals for purchasing and disbursement transactions.

Analysis

The security features available within the Maryland Department of Transportation's Financial Management Information System (MDOT FMIS) were not fully used by MAA to establish proper internal controls over the processing of purchasing and disbursement transactions. Specifically, MAA had not established adequate electronic approval paths over all critical purchasing and disbursement transactions for 9 of its 143 departments, including 6 accounts payable departments.

Consequently, 14 employees could process critical transactions without the system requiring an independent individual to approve those transactions. Specifically, 10 employees could initiate and approve purchase orders without independent approval. Four other employees could initiate and approve disbursements without independent approval.

Although our testing did not disclose any improper disbursements, unauthorized transactions could be processed and may not be readily detected. During fiscal year 2015, through May 2015, MAA used FMIS to process disbursements totaling approximately \$230 million. Similar conditions were commented upon in our preceding audit report.

Recommendation 3

We recommend that MAA fully use available FMIS security controls by establishing independent electronic approval requirements for all critical purchasing and disbursement transactions (repeat).

Vehicle Maintenance

Finding 4

MAA did not competitively procure certain vehicle and equipment maintenance services or use Statewide contracts when available.

Analysis

MAA did not consistently comply with State procurement regulations regarding the use of competitive procurements and Statewide contracts for certain vehicle and equipment maintenance services. In addition, certain disbursements were made with corporate purchasing cards without documentation identifying the vehicle or equipment being serviced. We tested 24 corporate purchasing card transactions between April 2014 and June 2015 totaling \$49,000 for vehicle and equipment maintenance services.

- Our testing disclosed that MAA made 17 purchases from the same two vendors for vehicle and equipment maintenance services without consolidating these purchases, soliciting competitive bids, and entering into contracts with the vendors. We subsequently determined that MAA made repeated purchases from these two vendors during fiscal years 2013 through 2015. Specifically, purchases from the vehicle maintenance vendor totaled approximately \$277,000 and purchases from the equipment maintenance vendor totaled approximately \$138,000 during this period.

We also noted that certain vehicle maintenance services procured in 12 transactions, totaling approximately \$24,000, may have been available under a Statewide contract (including 9 of the aforementioned 17 purchases). While we were advised by MAA that certain cost savings were achieved by using alternate vendors, no documentation of this assertion was maintained. By

procuring these services in this manner, MAA's leverage as a high-volume purchaser may not have been maximized.

State procurement regulations generally specify that contracts in excess of \$25,000 shall be awarded by competitive sealed bidding, and that procurements exceeding \$5,000 have written contracts. State procurement regulations also generally require the use of Statewide commodity contracts when available.

- Vendor invoices for purchases of vehicle and equipment maintenance services were not adequately supported. Our testing disclosed that 13 transactions totaling approximately \$31,000 were not supported by documentation that identified the specific MAA vehicle or equipment being serviced. Without this information being furnished by the vendor there is no assurance that the vehicle or equipment serviced belonged to MAA.

Recommendation 4

We recommend that MAA

- a. comply with State procurement regulations by using a formal written procurement process for purchases that are reasonably expected to exceed \$25,000, ensuring procurements exceeding \$5,000 have written contracts, and using existing Statewide contracts for all applicable services; and**
- b. ensure documentation supporting corporate purchasing card transactions contains information that clearly identifies that the services provided were applicable to MAA.**

Audit Scope, Objectives, and Methodology

We have conducted a fiscal compliance audit of the Maryland Department of Transportation – Maryland Aviation Administration (MAA) for the period beginning August 1, 2011 and ending June 30, 2015. The audit was conducted 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.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine MAA's financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included procurements and disbursements for architectural and engineering and construction contracts and operating expenditures, as well as cash receipts. We also determined the status of the findings contained in our preceding audit report

Our audit did not include certain payroll support services (such as, processing of personnel transactions and maintenance of employee leave records) provided by the State Highway Administration to MAA. These payroll support services are included within the scope of our audit of the State Highway Administration.

Our audit also did not include an evaluation of internal controls over compliance with federal laws and regulations for federal financial assistance programs and an assessment of MAA's compliance with those laws and regulations because the State of Maryland engages an independent accounting firm to annually audit such programs administered by State agencies, including MAA.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, observations of MAA's operations, and tests of transactions. Generally, transactions were selected for testing based on auditor judgment, which primarily considers risk. Unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, the results of the

tests cannot be used to project those results to the entire population from which the test items were selected.

We also performed various data extracts of pertinent information from the State's Financial Management Information System and the Maryland Department of Transportation's Financial Management Information System (such as revenue and expenditure data) and from the contractor administering the State's Corporate Purchasing Card Program (credit card activity). The extracts are performed as part of ongoing internal processes established by the Office of Legislative Audits and were subject to various tests to determine data reliability. We determined that the data extracted from these various sources were sufficiently reliable for the purposes the data were used during the audit. Finally, we performed other auditing procedures that we considered necessary to achieve our objectives. The reliability of data used in this report for background or informational purposes was not assessed.

MAA's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records, effectiveness and efficiency of operations including safeguarding of assets, and compliance with applicable laws, rules, and regulations are achieved.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect MAA's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to MAA that did not warrant inclusion in this report.

The response from the Maryland Department of Transportation, on behalf of MAA, to our findings and recommendations is included as an appendix to this

report. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise MAA regarding the results of our review of its response.

APPENDIX



Maryland Department of Transportation
The Secretary's Office

Larry Hogan
Governor

Boyd K. Rutherford
Lt. Governor

Pete K. Rahn
Secretary

September 27, 2016

Thomas J. Barnickel III, CPA
Legislative Auditor
Office of Legislative Audits
301 West Preston Street, Room 1202
Baltimore MD 21201

Dear Mr. Barnickel:

Thank you for letter regarding the June 30, 2015 Maryland Department of Transportation – Maryland Aviation Administration (MAA) draft audit report.

Enclosed please find our responses to the Legislative Auditor's current audit for the period beginning August 1, 2011 and ending June 30, 2015. An electronic version was forwarded by email.

Thank you again for your letter. If you have any additional questions or concerns, you may contact Mr. David Kalampnayil, MAA Audit Section, Office of Finance, Manager at 410-859-7995 or via email at dkalampnayil@bwiairport.com. Mr. Kalampnayil will be happy to assist you. Of course, you may always contact me directly.

Sincerely,

A handwritten signature in black ink, appearing to read "Pete K. Rahn", written over a large, stylized "P" and "K".

Pete K. Rahn
Secretary

Confidential Enclosures

cc: Mr. Patrick Bradley, Director, Office of Finance, MAA
Ms. Brenda Cachuela, Director, Office of Audits, MDOT
Mr. David L. Fleming, Chief Financial Officer, Office of Finance, MDOT
Mr. David Kalampnayil, Audit Manager, Office of Finance, MAA
Mr. R. Earl Lewis, Jr., Deputy Secretary, Policy, Planning, and Enterprise Services, MDOT
Mr. James F. Ports, Jr., Deputy Secretary of Operations, MDOT
Mr. Ricky D. Smith, Sr., Executive Director/CEO, MAA

My telephone number is 410-865-1000
Toll Free Number 1-888-713-1414 TTY Users Call Via MD Relay
7201 Corporate Center Drive, Hanover, Maryland 21076

**Maryland Department of Transportation
Maryland Aviation Administration
Draft Audit Report Responses
August 1, 2011 to June 30, 2015**

Federal Funds

Finding 1

The Maryland Aviation Administration (MAA) did not comply with requirements of a federal noise compatibility program and, as a result, \$4.6 million in related expenditures were not reimbursed with federal funds.

Recommendation 1

We recommend that MAA establish and implement formal procedures to ensure compliance with applicable program requirements and request reimbursement for all eligible expenditures from the federal funds available for this purpose.

MAA Response:

The MAA concurs with the auditors' recommendations.

As indicated in the analysis, MAA continued a Homeowner Sound Insulation Program, for all properties within the 75 DNL that had requested improvements, well after Federal Airport Improvement Program Noise funding ceased to be available, and the potential for reimbursement from Noise Land Disposal Proceeds was questionable.

Beginning in 2016, funds in the Noise Land Disposal Account have been used on eligible airport improvement projects based on the hierarchy defined under the Noise Land Management and Requirements for Disposal of Noise Land or Development Land Funded with AIP dated June 2014. Reimbursement from federal sources for our past Sound Insulation Program is not available. The State payments made over the audit period were included in the annual rates and charges billed to the airlines per the Use and Lease Agreement. All State paid costs have been recovered from the airlines. MAA was diligent in complying with noise program requirements which would allow it to use federal funding available in the escrow account. There were numerous correspondences between MAA and FAA since 2012 which demonstrated MAA's efforts in complying with noise program requirements. However, as MAA was not able to collect reimbursement for noise expenditures from federal sources, it collected this cost from the airlines.

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On August 30, 2016, the FAA announced that the 14 CFR Part 150 Noise Exposure Maps for BWI Marshall Airport are in compliance with applicable requirements with an effective date of August 31, 2016. This will allow the MAA to move forward with new programs for Sound Insulation and Voluntary Acquisition for eligible properties that fall within the 65 DNL, and homeowners interested in participating.

In the interim, the FAA has been working on an Updated Advisory Circular of Sound Insulation Guidelines which will provide airports standardized procedures in management and oversight for sound insulation programs and the associated grant requirements. The Circular will include the noise testing methodology and detailed procedures to ensure programs are implemented consistent with FAA policies.

Our plan is to begin the new programs once the FAA Updated Advisory Circular is available and MAA can develop Standard Operation Procedures (SOP) consistent with that guidance. MAA currently has approximately \$1.1 million in the escrow account to begin the program and is moving forward with some additional noise property sales that will provide additional funding. MAA's SOP will insure that the 20 percent State match and 80 percent Federal soundproofing funds, for eligible costs, are authorized and reimbursed in a timely manner. The State match payments will continue to be included in the annual rates and charges billed to the airlines per the Use and Lease Agreement.

Cash Receipts

Finding 2

MAA did not have adequate procedures to ensure that all collections, which totaled \$141 million during fiscal year 2015, were deposited and that deposits were made timely.

Recommendation 2

We recommend that MAA

- a. ensure deposit verifications are performed using all initial receipt records, and**
- b. pursue other arrangements to enhance the accountability and timeliness of deposits such as requesting that collections be remitted electronically.**

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MAA Response:

The MAA concurs with the auditors' recommendation.

- a. The MAA Accounting Office performs an independent review process for every deposit. As of December 2015, the cashier creates a certificate of deposit by using the initial records of cash and checks, which include pre-numbered cash receipts and the checks received prior to sending it to the bank, and initials it when completed. Another independent employee verifies the original records of cash and checks received to the MAA certificate of deposit form, and initials it when completed. A third independent employee verifies the MAA certificate of deposit form (which has already been verified to the original cash receipts and checks) to the daily bank journal and bank statement.
- b. MAA creates a deposit of all receipts daily. These deposits are picked up by a contracted armored service every day to deliver the deposits to the bank vault within a day. This usually equates to the deposit being posted to the bank within 2 business days due to timing. In consultation with the General Accounting Division, they have stated that this meets the requirement for timely deposit as proscribed in the Accounting Procedures Manual. The armored car company has stated that it is not possible for them to do a same day deposit.

MAA encourages all tenants to pay by ACH or wire transfer, however cannot mandate this as a practice. In September 2016, MAA sent a mass distribution email to all of our customers, recommending that they take advantage of paying MAA by ACH. MAA also inquired into remote deposit but was denied that option by the State Treasurer's Office (STO) because of the low volume of checks MAA receives. In addition, STO stated to MAA that "This is not an internal control problem because MAA did its part in getting the deposits to the courier timely."

Purchases and Disbursements

Finding 3

Proper internal controls were not established to ensure independent approvals for purchasing and disbursement transactions.

**Maryland Department of Transportation
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Recommendation 3

We recommend that MAA fully use available FMIS security controls by establishing independent electronic approval requirements for all critical purchasing and disbursement transactions (repeat).

MAA Response:

The MAA concurs with the auditors' recommendation.

MAA worked with The Secretary's Office (TSO) to determine what needed to be modified to correct these inadequate approval paths. Those corrections were applied in December 2015. In addition, TSO has created a security report that is sent quarterly to MAA to assist in identifying any future inadequate approval paths. TSO staff will follow up with MAA in October 2016 to review the approval paths to determine if they could be further strengthened.

With regard to the auditor's analysis of the 10 employees that could initiate and approve purchase orders without independent approval, MAA provides the following explanation. MAA agrees that these 10 employees could initiate and approve purchase orders; however FMIS approval paths established by MAA required an independent final approval from an independent employee in MAA's Budget Office. In addition, from December 2015 through April 2016 MAA changed the security for these 10 employees so that some could initiate and some could approve purchase orders, but none could both initiate and approve. The requirement that an independent employee from the MAA Budget Office provide a final approval for all purchase orders remained.

With regard to the auditor's analysis of the 4 employees that could initiate and approve disbursements without independent approval, MAA provides the following explanation. The Accounts Payable Technicians create and approve invoices and direct vouchers as part of their job duties. These invoices and direct vouchers do not interface into State FMIS (nor are they sent to the General Accounting Division for payment) until they are independently reviewed and approved by an Accounts Payable Supervisor (TSO FMIS designated 1VP approval process) and an additional independent employee (TSO FMIS designated 2VP approval process). Beginning in December 2015, this review is manually documented and retained as a historical record. The review is also electronically documented by these individuals approving the disbursements within FMIS and attaching their user IDs to these transactions. In addition to the 1VP and 2VP approval processes, all invoices and direct vouchers are manually approved by an authorized invoice approver (e.g. contract manager, buyer, end user, requestor etc.) and he/she is independent from the Accounts Payable office.

**Maryland Department of Transportation
Maryland Aviation Administration
Draft Audit Report Responses
August 1, 2011 to June 30, 2015**

Vehicle Maintenance

Finding 4

MAA did not competitively procure certain vehicle and equipment maintenance services or use Statewide contracts when available.

Recommendation 4

We recommend that MAA

- a. comply with State procurement regulations by using a formal written procurement process for purchases that are reasonably expected to exceed \$25,000, ensuring procurements exceeding \$5,000 have written contracts, and using existing Statewide contracts for all applicable services; and**
- b. ensure documentation supporting corporate purchasing card transactions contains information that clearly identifies that the services provided were applicable to MAA.**

MAA Response:

The MAA concurs with the auditors' recommendation.

- a. MAA has a policy in place where we follow State procurement regulations for formal written procurements over \$25,000; ensuring procurements exceeding \$5,000 have written contracts, and using existing statewide contracts.

The Office of Procurement is working with Vehicle & Equipment Maintenance to generate contracts for items which are not available through Statewide contracts and are frequently purchased by Vehicle & Equipment Maintenance. The contracts are estimated to be in place around December 1, 2016.

- b. Beginning June 2016, MAA required the vendor to document the vehicle information on the invoices where feasible. For cases where this is not practical, the MAA technician, after service is performed or the parts are installed at MAA's auto shop, will record the vehicle information on work order/invoice as appropriate. In addition, the MAXIMO system captures the work order, vehicle identification and the associated invoice information.

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