



John Keel, CPA
State Auditor

A Report on
**The Audits of the Fiscal Year 2013 Financial Statements of
the Central Texas Turnpike System and the Texas Mobility Fund
at the Department of Transportation**

January 14, 2014

Members of the Legislative Audit Committee:

In our audit reports dated December 16, 2013, we concluded that the following financial statements were materially correct and presented in accordance with accounting principles generally accepted in the United States of America:

- The Department of Transportation's (Department) Central Texas Turnpike System's (System) basic financial statements for fiscal year 2013.
- The Department's Texas Mobility Fund's (Fund) basic financial statements for fiscal year 2013.

The Department published our audit reports in each set of its basic financial statements, which it posted on its Web site at:

- The System's basic financial statements:
<http://www.txdot.gov/inside-txdot/office/innovative-finance/investors/ctts-reports.html>.
- The Fund's basic financial statements:
<http://www.txdot.gov/inside-txdot/forms-publications/publications/finance/mobility-fund-reports.html>.

For the System, we also issued a report on internal control over financial reporting and on compliance and other matters as required by auditing standards (that report, including responses from management, is presented in the attachment to this letter). In that report, auditors identified deficiencies related to the preparation of the Notes to the financial statements and the controls over toll revenue transactions that were reported as significant deficiencies in the System's internal control.

For the Fund, we also issued a report on internal control over financial reporting and on compliance and other matters as required by auditing standards. Our procedures did not identify any material weaknesses in internal control over financial reporting or any noncompliance with laws or regulations that materially affected the financial statements. In addition, the major internal controls that we tested for the purpose of forming our opinions on the Fund's financial statements were operating effectively.

Our procedures were not intended to provide an opinion on internal control over financial reporting or to provide an opinion on compliance with laws and regulations. Accordingly, we do not express an opinion on the effectiveness of the Department's internal control over financial reporting or on compliance with laws and regulations.

SAO Report No. 14-017

Auditors communicated certain issues that were not material or significant to the audit objectives in writing to the Department's management.

As required by auditing standards, we will also communicate to the Texas Transportation Commission certain matters related to the conduct of a financial statement audit.

We appreciate the Department's cooperation during this audit. If you have any questions, please contact Angelica Ramirez, Audit Manager, or me at (512) 936-9500.

Sincerely,

John Keel, CPA
State Auditor

Attachment

cc: Members of the Texas Transportation Commission
Mr. Ted Houghton, Chair
Mr. Jeff Austin III
Mr. Jeff Moseley
Mr. Fred Underwood
Mr. Victor Vandergriff
Mr. Phil Wilson, Executive Director



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Attachment



Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

Independent Auditor's Report

Members of the Texas Transportation Commission

Mr. Ted Houghton, Chair
Mr. Jeff Austin III
Mr. Jeff Moseley
Mr. Fred Underwood
Mr. Victor Vandergriff

We have audited in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities of the Central Texas Turnpike System (System) of the Department of Transportation (Department) as of and for the year ended August 31, 2013, and the related notes to the financial statements, which collectively comprise the System's basic financial statements and have issued our report thereon dated December 16, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying schedule of findings and responses that we consider to be significant deficiencies.

Summary of Findings and Responses
Finding Number
2013-1
2013-2

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

System's Response to Findings

The System's response to the findings identified in our audit is included in the accompanying schedule of findings and responses. The System's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

John Keel, CPA
State Auditor

December 16, 2013

Schedule of Findings and Responses

Section 1

The Department of Transportation Should Strengthen Its Review of the Central Texas Turnpike System's Financial Notes and Note Adjustments

Reference No. 2013-1

Type of finding: Significant Deficiency

In the fiscal year 2013 financial statements for the Central Texas Turnpike System (System), the Department of Transportation (Department) initially overstated two items in Note 4. Specifically, the Department overstated future interest payments by \$230,514,000 and overstated long-term liability activity table by \$5,576,217. It subsequently corrected those errors.

Future interest payments. The Department incorrectly calculated future interest payments for one of its variable rate bonds in the debt service requirements table of Note 4. The Department used a 5 percent increased rate included in the official statement; however, it should have used the 1.25 percent effective interest rate at the financial statement date to ensure compliance with Governmental Accounting Standards Board (GASB) Codification, Section 1500.129 (see text box for additional details). That error resulted in a \$230,514,000 cumulative overstatement of future debt service.

Government Accounting Standards Board Codification, Section 1500.129

Governments should disclose the following details of debt service requirements to maturity:

- a. Interest requirements for variable-rate debt should be determined using the rate in effect at the financial statement date.
- b. The terms by which interest rate change for variable-rate debt.

The Department subsequently corrected that error after auditors brought the error to its attention.

Long-term liability. The Department incorrectly made an adjustment in the premium and discount amortization for a bond series that was refunded during the year. That resulted in a \$5,576,217 overstatement of the long-term liabilities activity table in Note 4 for a revenue bond series.

The Department corrected that error in Note 4 in the System's financial statements after auditors brought the error to its attention.

In addition, the Department's procedures for preparing Note 4 did not contain sufficient detail to demonstrate the methodology used to prepare that note and allow a reviewer to ensure compliance with GASB requirements.

Recommendations

The Department should:

- Ensure that processes it uses to prepare and review notes to the System's financial statements are sufficient to determine compliance with GASB requirements.
- Develop detailed procedures for the preparation of the long-term liabilities note to the System's financial statements.
- Adequately review adjusting journal entries and retain accurate supporting documentation for the long-term liability note in the System's financial statements.

Management's Response

The Department agrees with the recommendations and will take action immediately to strengthen the procedures and processes used to prepare and review notes and adjusting journal entries to the System's financial statements. Specific focus will be given to increasing the detailed level of procedures related to preparation of the long-term liabilities note. Supporting documentation and permanent files related to the long-term liabilities note will be examined, inventoried and retained. The Department plans to address all recommendations by August 31, 2014.

The interest payments past 2015 on the bonds are an estimate of what the debt service on these bonds will be after that date. The GASB Codification section quoted in the finding addresses variable rate bonds. The put bonds in question, however, are not typical variable rate bonds and therefore the quoted GASB Codification disclosures alone do not accurately convey the nature of the debt service requirements for these bonds. Research conducted by the Department later on with GASB staff clarified that there are valid options for disclosure of this information for put bonds with the ultimate goal of presenting disclosures that do not mislead a reader of the financial statements by understating future debt service obligations of the System. The Department will implement additional procedures to ensure research is completed in advance of financial reporting for bond issuances to avoid confusion and ensure that the System's disclosures are in compliance with GASB requirements.

Section 2

The Department of Transportation Should Strengthen Its Reconciliation Controls for Central Texas Turnpike System Toll Revenue Transactions

Reference No. 2013-2

Type of finding: Significant Deficiency

The Department did not have effective reconciliation controls to help ensure that it recorded all System toll revenue transactions in fiscal year 2013. The Department's reconciliations of System toll revenue transactions in fiscal year 2013 were not always based on complete information.

Toll Revenue Information Systems

- The Toll Management System contains information on toll transactions that are generated at toll lanes.
- The Back Operating System contains toll data that is transferred from the Toll Management System that the Department uses to bill customers and record System toll revenue.

Source: The Department.

The System's toll revenue transactions are captured in the Toll Management System and transferred to the Back Office System for recording revenue (see text box for more information on those systems). To help ensure that the Toll Management System transfers all transactions to the Back Office System, the Department performs reconciliations between those two systems. However, the reconciliations the Department performed from September 2012 through March 2013 did not use complete information. Those reconciliations did not identify 2,505,817 toll revenue transactions that were not transferred to the Back Office System from October 2012 through December 2012 for one toll road. As a result, the System toll revenue recorded did not include the revenue associated with those 2,505,817 transactions and the Department did not

initially bill the related customers for the tolls. However, Department management asserts that the Department billed those customers for the tolls in February 2013.

The Department implemented a new reconciliation process after the end of fiscal year 2013 to reconcile System toll revenue transactions on a transaction level, and that process was based on complete information. In October 2013, the Department used the new reconciliation process to perform the reconciliations for April 2013 through August 2013.

Recommendation

The Department should ensure that its processes capture all System toll transactions to enable it to appropriately record and bill for all System toll revenue transactions.

Management's Response

The Department will continue to focus on ensuring that all Central Texas Turnpike System (System) toll revenue transactions are reconciled and recorded. The Toll Operations Division has performed and will institute a formalized revenue trending comparison to mitigate impacts of reporting anomalies by the Toll Management System. In addition, the Toll Operations Division will continue to reconcile toll revenue transactions, based on complete information.

Completion Date: January 15, 2014