



# REVIEW OF THE ECONOMICALLY DISTRESSED AREAS PROGRAM

---

Project # 20140401  
September 2014

**Our Mission**

To provide leadership, information, education, and support for planning, financial assistance, and outreach for the conservation and responsible development of water for Texas.

**Board Members**

Carlos Rubinstein, Chairman | Bech Bruun, Member | Kathleen Jackson, Member  
Kevin Patteson, Executive Administrator

## **Project Team**

Amanda Jenami, CPA, CISA, CFE, CIA, CCSA, CGAP, Director  
Robert Sahm, CPA, CISA

# Table of Contents

<b>Executive Summary .....</b>	<b>1</b>
Overview .....	1
Background .....	1
Summary of Management’s Response.....	2
Closing .....	2
<b>Objectives and Conclusions .....</b>	<b>3</b>
Objective 1 – Operational Efficiency .....	3
Objective 2 – Operational Effectiveness.....	3
Objective 3 – Regulatory Compliance .....	4
<b>Detailed Issues with Management Responses .....</b>	<b>5</b>
Regulatory Compliance: Monitoring Recipient Compliance .....	5
<b>Scope and Methodology.....</b>	<b>6</b>
<b>Appendix:.....</b>	<b>7</b>
<b>Historical Performance of EDAP .....</b>	<b>7</b>
<b>Chart 1: Average Application Processing Time (Days).....</b>	<b>7</b>
<b>Chart 2: Average Processing Time for Grant/ Loan Closings.....</b>	<b>8</b>
<b>Chart 3: Completed Projects - Performance Measure Target versus Actual .....</b>	<b>8</b>

# Executive Summary

## Overview

Texas Water Development Board's (TWDB) Economically Distressed Areas Program (EDAP) processes include sufficient controls to provide reasonable assurance that program goals are achieved efficiently, effectively and in compliance with state and agency requirements. The Office of Water Supply and Infrastructure (WSI)'s financial assistance application review and project monitoring processes provide reasonable assurance that program eligibility requirements are met. The review noted operational efficiency improvements in the timeliness with which financial assistance applications, Board commitments, loan/grant closings, and project outlay payment requests are processed. These improvements have, in turn, enhanced overall project completion timeframes.

## Background

EDAP, established by the Texas Legislature (1989), provides financial assistance in the form of a grant or a combination of grant/loan to provide water and wastewater services to economically distressed areas where services do not exist or systems do not meet minimum state standards. The program also includes measures to prevent future substandard development. The 81<sup>st</sup> Texas Legislature (2009) passed further legislation that allows funds from EDAP to be used to pay for first-time water and wastewater connections for homes in areas served by the program. The homes must meet additional federal low-income criteria.

As of June 30, 2014, EDAP had provided financial assistance totaling approximately \$704 million, of which 11% (\$74 million) had been committed to specific projects but not yet spent. Of this unexpended amount, \$35 million comprised of Board commitments awaiting grant/loan closing while the rest, \$39 million, represented closed grants/loans in escrow accounts, available for project use.

EDAP is funded from both general revenue, and loan repayments. In addition, the program received a total of \$500 million in constitutional bond authority in fiscal years 1990, 1992 and 2008, of which approximately \$152 million authority remains on hand. Management estimates that the remaining \$152 million bond authority will last the program another 4-5 years.

Effective November 2013, the Office of Water Supply & Infrastructure (WSI) became responsible for the administration of EDAP, including, program administration, project management, field inspections, outlay payment approval, escrow release authorization, and operational reporting.

## **Summary of Management's Response**

*Management appreciates Internal Audit's efforts to identify issues for improvement. Implementation of the recommendation will enhance administrative processes and controls in regard to the EDAP. Management's action plan is included within the detailed section of this report.*

## **Closing**

We would like to thank WSI and Financial Compliance for the cooperation and assistance provided to the audit staff during this audit. For questions or additional information concerning this audit report, please contact Amanda Jenami at 512-463-7978.

# Objectives and Conclusions

The overall objective of this audit is to determine the extent to which the agency has processes and controls to ensure EDAP objectives are met efficiently, effectively, and in compliance with relevant laws, program requirements, and TWDB procedures.

The audit focused primarily on EDAP program activities from September 1, 2010, to June 30, 2014. Fieldwork was conducted from July through August 2014. The detailed audit objectives and conclusions are described next.

## Objective 1 – Operational Efficiency

**Determine if the program has processes in place to address unspent funds (including those that are tied up in projects). In addition, determine the extent to which the agency’s processes ensure timely completion of EDAP projects.**

WSI processes provide reasonable assurance that EDAP funds (including those that have been committed to projects) are spent in a timely manner. An analysis of agency timelines for processing EDAP applications and grant/loan closings found significant improvement in the last four years. Through June 30, 2014, the average EDAP financial assistance application processing time has improved by 125 days from the 2011 biennium (275 days) to current biennium (150 days) while the average timeliness of grant/loan closings has improved by 25 days, from 200 days to 175 days, as illustrated in charts 1 and 2 on pages 7 and 8.

Since the first financial assistance commitment in 1991, the program has committed to 123 projects and completed 94 projects, with 29 projects remaining active. The improvement is attributable to more streamlined application review and closing processes, as well as more effective project monitoring.

We recognize that EDAP, like similar programs, is subject to project delays that are outside the direct control of the TWDB. However, agency staff has, over the life of the program, enhanced project monitoring strategies to reduce the impact of any such delays.

## Objective 2 – Operational Effectiveness

**Determine the extent to which the program has processes in place to ensure program goals are met, including those established by the Texas Legislature.**

Management reported that EDAP exceeded its performance target (of completed projects) by 2 as of August 31, 2014. This confirms the improved project completion timelines discussed earlier, when considering that the program has reported a shortfall of between one and three projects in its “completed projects” performance target in the last few biennium, as illustrated in chart 3 on page 8.

Our review of payment requests found them to have been processed in a timely manner. In addition, our review of the EDAP financial reports found them to be adequately supported.

Management has adequately addressed most of the recommendations from the State Auditor's Office's Report # 10-004 which was issued in September, 2009.

### **Objective 3 – Regulatory Compliance**

#### **Determine if the program has processes in place to ensure compliance with state requirements.**

EDAP processes and procedures provide reasonable assurance that the program fulfills its objectives in compliance with statutory and agency requirements. The review tested five EDAP projects for compliance with eligibility, and matching requirements. We reviewed relevant financial assistance application review documentation for evidence that the project is allowable; that the applicant is eligible; and that the Board commitment was approved by both the Executive Administrator and the Board. We ensured that cases where EDAP funds exceeded 50% of project cost were adequately supported by an affirmative nuisance finding. We also reviewed evidence that related disbursements were processed, appropriately approved and disbursed within 30 days of being considered administratively complete.

For financial assistance provided during the period September 1, 2010 until May 31, 2014, the review also tested compliance with various provisions of the Water Code such as WC17.933, which requires financial assistance provided by TWDB to political subdivisions not to exceed 90% of the principal amount of issued and unissued bonds.

The review found an opportunity to improve monitoring grant/loan recipients for compliance with §16.356, Texas Water Code.

#### **Determine if the program has a process in place to ensure the completeness, integrity and availability of program data. In addition, determine the extent to which program processes ensure reporting requirements are met in a complete, accurate, and timely manner.**

Our review of program information within the agency's enterprise information system for tracking, processing, monitoring and reporting project activities (TxWISE) and the EDAP quarterly status report found opportunities for improvement in the accuracy of information and the quality of reporting. Discussions indicated that the agency is migrating from various legacy systems to TxWISE, and that the documentation, business rules and reporting is still evolving. Management is aware of the issues with TxWISE and has indicated it is working to address them. As part of this exercise, management plans to design more robust system-generated reports for use by both senior management and the Board.

# Detailed Issues with Management Responses

## Regulatory Compliance: Monitoring Recipient Compliance

Current agency procedures do not include monitoring loan/grant recipients' compliance with §16.356, Texas Water Code. This elevates the risk that noncompliance with this provision could go undetected. TWDB's standard grant agreement includes language similar to:

*“The City agrees to comply with the requirement of §16.356, Texas Water Code, that no revenues received from rates or fees collected from the system to be constructed through this commitment be used for any purposes other than utility purposes, and that the annual financial statement prepared by the City under § 103.001, Texas Local Government Code, include a specific report on compliance with this condition.”*

## Recommendation

Management should ensure that compliance with §16.356, Texas Water Code, is addressed in the agency's loan/grant recipient monitoring activities.

## Management Action Planned:

*Management agrees with the finding and will update procedures to incorporate monitoring of this compliance reporting requirement.*

*The Finance Division will also coordinate efforts with Water Supply and Infrastructure to assure that EDAP recipients are aware of this requirement.*

## Responsible Parties:

*Chief Finance Officer, Director of Debt Portfolio Management and Financial Compliance Team Lead.*

## Estimated Completion Date:

*October 31, 2014.*

# Scope and Methodology

The overall objective of this audit is to determine the extent to which TWDB has processes and controls within EDAP that ensure program objectives are met efficiently, effectively, and in compliance with relevant laws, program requirements, and agency procedures.

The audit focused primarily on activities from September 1, 2010, to June 30, 2014. Fieldwork was conducted from July through August 2014.

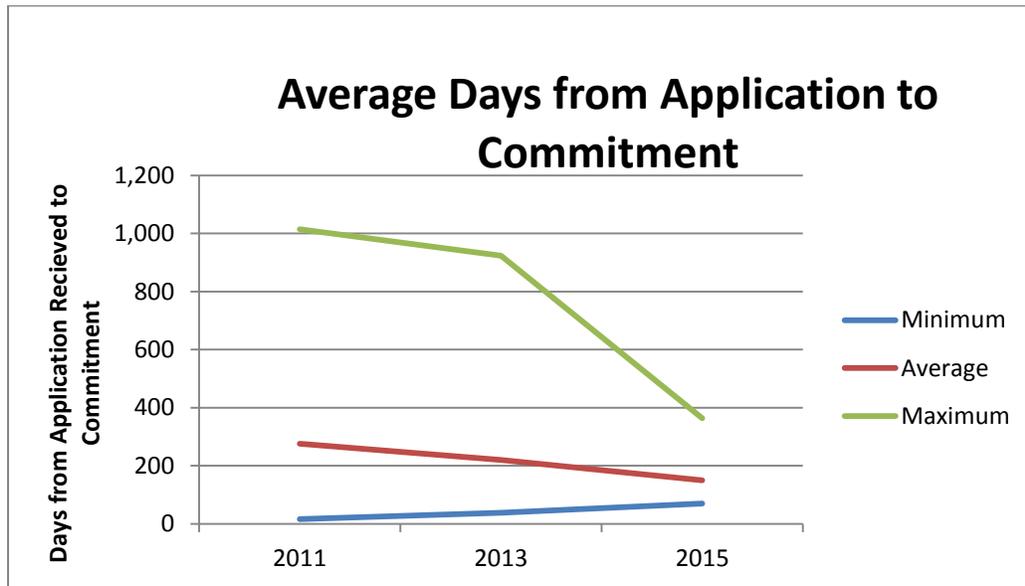
Our audit was based upon standards as set forth in the Texas Administrative Code, TWDB rules, and other sound administrative practices. The audit was performed in compliance with the Institute of Internal Auditors' "International Standards for Professional Practice of Internal Auditing."

Additionally, we conducted this performance audit 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. Our evidence-gathering methods included the following:

- We reviewed applicable laws, rules, and established procedures.
- We reviewed the quarterly EDAP Status Report.
- We performed trend analyses of gross commitments, spending, unspent commitments, and excess demand based on EDAP status reports presented to the Board.
- We evaluated the program's long-term goals, information flow within WSI, senior management and the Board, and project monitoring.
- We reviewed financial reports and supporting schedules for key ratios such as administrative costs to commitments closed current ratio, net assets and asset turnover.
- We tested a sample of EDAP projects and commitments for such things as eligibility, matching requirements, timeliness of payment and project completion.
- We reviewed key documents and reports in TxWISE including project milestones, inspection notes, project status reports, and project escrow releases.
- We compared actual to projected completion schedules for a sample of EDAP projects.
- We conducted interviews with staff.
- We followed up on the SAO's Report # 10-004 which was issued in September, 2009.

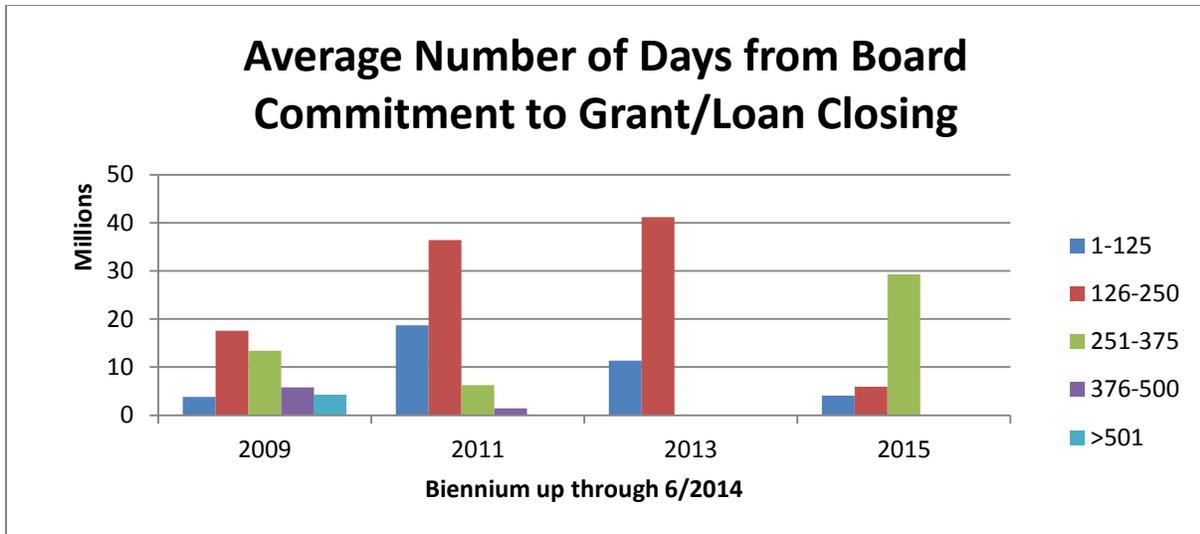
# Appendix:

## Historical Performance of EDAP



**Chart 1: Average Application Processing Time (Days)**

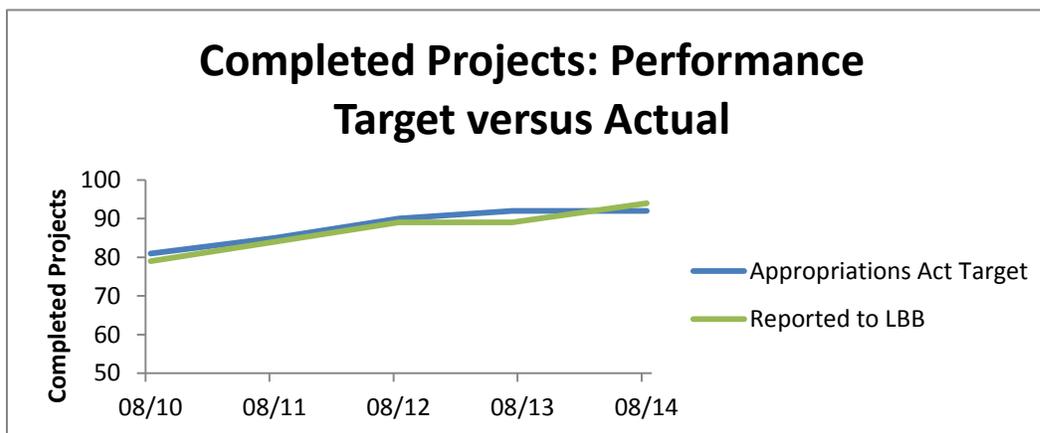
Through June 30, 2014, the average EDAP financial assistance application processing time has improved by 125 days from the 2011 biennium (275 days) to current biennium (150 days). The process times are calculated as the number of days from when the application was received to when the Board commitment was granted.



**Chart 2: Average Processing Time for Grant/ Loan Closings**

The process times are calculated as the number of days from when the Board commitment was granted to the grant/loan closing date.

The average time to close a commitment was 300 days in 2009, 200 days in 2011 and 150 days in 2013. The average time to close for 2014 is currently 175 days because of a \$29 million commitment (still open as of this report) which is expected to take a year to close.



**Chart 3: Completed Projects - Performance Measure Target versus Actual**

# Report Distribution

## Internal Distribution

### Board Members' Office

Carlos Rubinstein, Chairman  
Bech Bruun, Board Member  
Kathleen Jackson, Board Member  
Curtis Seaton, Chief of Staff to Chairman Rubinstein  
Lauren Graber, Chief of Staff to Board Member Bruun  
Jennifer White, Chief of Staff to Board Member Jackson  
Les Trobman, General Counsel

### Executive Director's Office

Kevin Patteson, Executive Administrator  
Jonathan Stinson, Special Assistant  
Stacy Barna, Assistant Executive Administrator  
Darrell Nichols, Assistant Executive Administrator

### Program Area

Jeff Walker, Deputy Executive Administrator (WSI)  
Amanda Lavin, Assistant Deputy Executive Administrator (WSI)  
Jo Dawn Bomar, Director, Program Administration & Reporting (WSI)  
Amanda Landry, Chief Financial Officer  
Byron Johnson, Director of Debt and Portfolio Management

## External Distribution

### Legislative Budget Board

[Ed.Osner@lbb.state.tx.us](mailto:Ed.Osner@lbb.state.tx.us)

### Governor's Office Email Drop Box

[internalaudits@governor.state.tx.us](mailto:internalaudits@governor.state.tx.us)

### State Auditor's Office

[iacoordinator@sao.state.tx.us](mailto:iacoordinator@sao.state.tx.us)

### Sunset Advisory Commission

[sunset@sunset.state.tx.us](mailto:sunset@sunset.state.tx.us)

## **TWDB Mission Statement**

The Texas Water Development Board's (TWDB) mission is to provide leadership, information, education, and support for planning, financial assistance, and outreach for the conservation and responsible development of water for Texas.

## **Internal Audit Division's Mission Statement**

Our mission is to assist all members of management and the Board with objective reports, recommendations, counsel, and information on the adequacy and effectiveness of TWDB's system of internal controls and the quality of performance in carrying out assigned responsibilities.

**To obtain a hard copy of this TWDB Audit Report, please e-mail [Amanda.jenami@twdb.texas.gov](mailto:Amanda.jenami@twdb.texas.gov) or call 512-463-7978.**